



# THE FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA

## 2013 ARTICLE IV CONSULTATION

October 2013

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2013 Article IV consultation with The Federal Democratic Republic of Ethiopia, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on September 18, 2013, following discussions that ended on July 3, 2013, with the officials of The Federal Democratic Republic of Ethiopia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on August 29, 2013.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the World Bank.
- An **Informational Annex** prepared by the IMF.
- A **Press Release** summarizing the views of the Executive Board as expressed during its September 18, 2013 consideration of the staff report that concluded the Article IV consultation with The Federal Democratic Republic of Ethiopia.
- A **Statement by the Executive Director** for The Federal Democratic Republic of Ethiopia.

The document listed below has been or will be separately released.

### Selected Issues Paper

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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# THE FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA

## STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION

August 29, 2013

### KEY ISSUES

**Context:** Ethiopia's public sector-led development strategy has contributed to considerable poverty reduction and progress toward achieving the Millennium Development Goals (MDGs) as envisaged under the authorities' Growth and Transformation Plan (GTP). Economic growth has been robust, and inflation has declined to single digits. The investment requirements of the GTP are large and securing the associated financing remains a challenge. Without greater scope for the private sector the realization of the GTP's objectives could be elusive.

**Growth and inflation prospects:** Real GDP growth remains robust and is estimated by staff at 7 percent in 2012/13 and projected to increase to 7.5 percent in 2013/14 and 2014/15 before tapering-off slightly in subsequent years under current policies.<sup>1</sup> Inflation has been brought down to around 7 percent at end 2012/13 and is projected to remain in single digits.

**Policy mix:** The discussions focused on policies to sustain robust and inclusive growth and structural transformation in the context of prudent fiscal and monetary policies. Staff recommendations centered on maintaining pro-poor expenditure, improving the investment climate, and adjusting the overall fiscal stance with the aim of creating greater room for the private sector to further leverage large public investments. Enhancing external competitiveness and building adequate foreign reserves (to at least three months of imports) through greater exchange rate flexibility and improved productivity of the traded goods sector were recommended to enhance resiliency. Bolstering capacity at the National Bank of Ethiopia (NBE) for the formulation and implementation of financial sector policies to promote financial deepening and broader inclusion were considered important for the realization of the GTP objectives.

**Risks:** Persistent shortfalls in the financing of planned infrastructure investment and a tightening of foreign exchange availability could constrain medium-term growth in the absence of policy adjustments. A significant slow-down of the major emerging markets could also hamper development plans and robust growth.

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<sup>1</sup> Historical GDP statistics are official data and are subject to significant weaknesses. Applying plausible factor productivities would suggest that the annual GDP growth rate prior to 2011/12 could be overestimated by as much as 3 percentage points (Annex 1).

Approved By  
**Michael Atingi-Ego**  
**and Masato Miyazaki**

Discussions were held in Addis Ababa on June 19–July 3, 2013. The mission met with Prime Minister Hailemariam Desalegn, Minister of Finance and Economic Development Sufian Ahmed, National Bank Governor Teklewold Atnafu, Economic Advisor to the Prime Minister Newai Gebre-ab, other senior officials, and representatives of the donor, business, and civil society communities. The mission team comprised Mr. Wajid (head), Mr. Yèhoué, Mr. Ramirez (all AFR), Mr. Kinoshita (STA), and Mr. Nielsen (SPR); Ms. Radzewicz-Bak (MCM) participated in some meetings; Mr. Mikkelsen, resident representative, assisted. Ms. Teferra, senior advisor to Mr. Saho (OED) participated in some key meetings. Staff collaborated closely with the World Bank staff.

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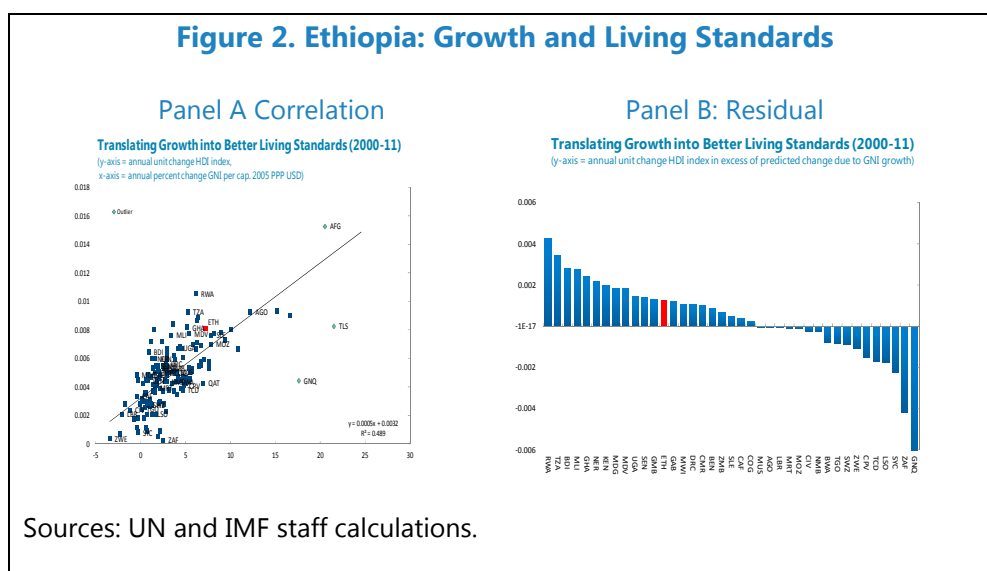
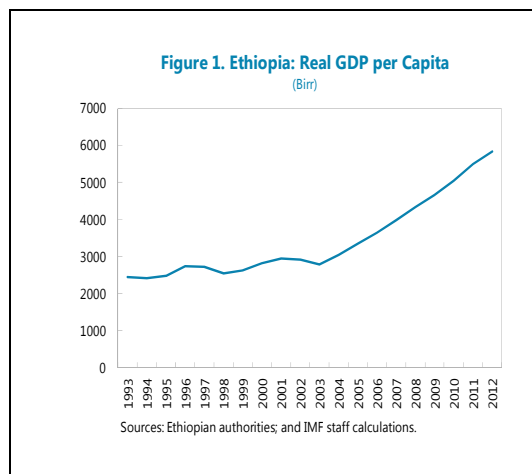
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## BACKGROUND

### 1. During the last decade, Ethiopia has made strides in economic and social development.

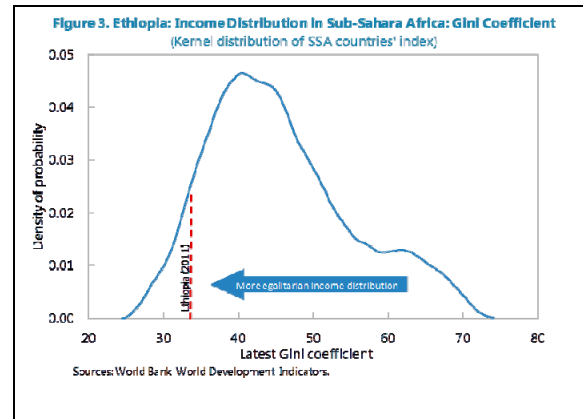
Robust economic growth averaging more than 7 percent since 2001/02 and social assistance—that now reaches more than 8 million beneficiaries in about 1.5 million households—have resulted in a several-fold rise in real per capita GDP (Figure 1) and a dramatic drop in the national poverty rate (from 60.5 percent in 2005 to 30.7 percent in 2011).<sup>2</sup> In addition to the dramatic decline in the incidence of poverty over the last decade, nonmonetary dimensions of well-being have also improved, including in the rural areas. Based on the Human Development Index (HDI), Ethiopia has been successful in translating economic growth into higher living standards for its citizens and has outperformed many sub-Saharan African countries and a number of non-African countries (indicated by Ethiopia’s higher actual HDI than that predicted by a cross-country correlation between the HDI and per capita gross national income (Figure 2)).<sup>3</sup>



<sup>2</sup> Based on the international standard of US\$1.25 a day, purchasing-power-parity adjusted (World Bank’s World Development Indicators, August 2013).

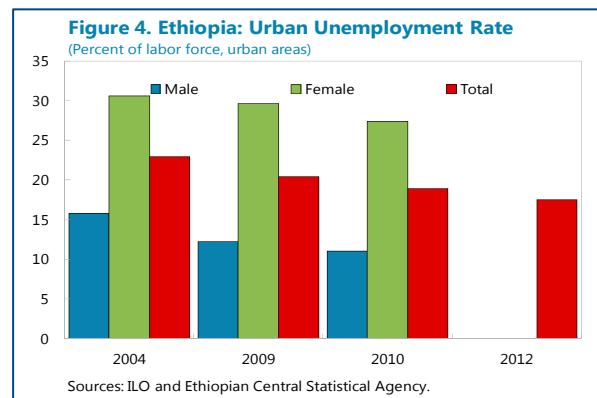
<sup>3</sup> A forthcoming Selected Issues Paper, “Translating Economic Growth into Higher Living Standards: Inclusive Growth in Ethiopia,” provides an in-depth analysis of inclusive growth in Ethiopia.

**2. Income distribution in the country is relatively even.** Among Sub-Saharan African countries, Ethiopia is one of the most egalitarian with a Gini coefficient of 33.6 (Figure 3) and it has consistently maintained this distribution in the last ten years. With a large population and more than 80 percent of it in rural areas, Ethiopia stands out among comparable African countries regarding relatively even income distribution, although there are likely differences between rural and urban populations.



**3. Economic growth has helped to reduce unemployment particularly in urban areas.**

While overall unemployment rate stands at about 25 percent, urban unemployment rate declined from 22.9 percent in 2004 to 17.5 percent in 2012 (Figure 4). In urban areas, both female and male unemployment declined and the large gap between the two groups has narrowed for the two years of available and comparable data (2009 and 2010). Unemployment rate remains particularly high among young females, with almost one third of them unable to find a job in the urban areas.



**4. A public sector-led growth strategy centered on high public investment has been instrumental in delivering these results.** The strategy, which calls for substantial external financing and state mobilization of domestic resources, has provided an important impetus to growth. Combined with pro-poor spending that has averaged more than 12 percent of GDP over the past decade, this has helped improve living standards. Following the passing of Prime Minister Meles in August 2012, the new Prime Minister Hailemariam has reaffirmed the state-led model and the public investment plan embodied in the GTP. Developments in the first two years (2010/11–2011/12) of the GTP suggest that the required external financing is not materializing, and the investment drive in the priority projects through directed domestic credit is squeezing the availability of credit and foreign exchange for the rest of the economy.

**5. The recommendations from the 2012 Article IV consultation have only been partially implemented.** The authorities brought inflation down to single digits. While, owing to the decline in inflation, the extent to which real interest rates were negative have been reduced, positive real interest rates are yet to be realized and liquidity management at the National Bank of Ethiopia (NBE) remains to be improved. Similarly, progress has been slow on structural reforms to allow proper functioning of financial markets; to liberalize the foreign exchange or improve the business climate. Much emphasis continue to be put by the authorities on improving physical infrastructure such as roads, railway, and electricity supply, which they believe would help improve business climate. The 2013 Article IV discussions touched upon these recommendations, which remain valid.

## RECENT DEVELOPMENTS AND OUTLOOK

### A. Recent Economic and Policy Developments

**6. Recent macroeconomic developments are encouraging, with a significant deceleration in inflation and continued robust economic growth (Figures 5, 6, and 7).** Despite significant decline in coffee prices and supply bottlenecks growth remains robust, supported by better agricultural output and construction and other services activities.<sup>4</sup> Inflation declined from the peak of 40 percent in July 2011 to around 7 percent in June 2013, lower than initially projected by staff. This has significantly eased the extent to which real interest rates were negative, reducing the severity of the distortionary effect on financial intermediation. Pressures resulting in foreign exchange shortages in the wake of the passing away of Prime Minister Meles, have eased, although the spread between the official and parallel markets is yet to be eliminated.

**7. Fiscal policy at the general government level remains prudent with cautious execution of the government budget.**<sup>5</sup> Overall revenue-to-GDP ratio is estimated to fall from 14.0 percent in 2011/12 to 13.2 percent in 2012/13. Reflecting the strong pro-poor focus, the ratio of poverty-reducing expenditure to GDP is being maintained and non-priority expenditure will likely be compressed in 2012/13. Staff estimates the government budget deficit, including grants, to be 2.8 percent of GDP.

<sup>4</sup> GDP statistics in Ethiopia are subject to significant weaknesses. Applying plausible factor productivities would suggest that the annual GDP growth rate could be off by as much as 3 percentage points in recent years. In the past two years, staff used its own estimates showing lower GDP growth. The methodology improved considerably in 2011/12 and the authorities are continuing efforts to further strengthen national accounts statistics. Staff has thus reverted to using official statistics, but has stressed the need to further improve national accounts data and offered technical assistance (see Annex I).

<sup>5</sup> Excluding public enterprises.

**8. However, public enterprises continue to expand their investment activities.** Net credit expansion (through loans and corporate bonds) from the Commercial Bank of Ethiopia (CBE) to public enterprises (in the 10 months up to April, 2013) alone accounted for 3 percent of GDP. In addition, they borrowed from the Development Bank of Ethiopia (DBE) and through bond issuance for the construction of Renaissance Dam, which is proceeding as planned. The dam is estimated by the authorities to cost 10 percent of 2012/13 GDP and is intended to be entirely financed domestically.

**9. An accurate overall fiscal stance for the consolidated public sector (including public enterprises) is difficult to gauge, although it would seem considerably more expansionary.** While appropriately consolidated data on the overall public sector finances were not available, external financing of public enterprises in 2012/13 was 2.3 percent of GDP and the monetary survey indicates additional domestic financing of public enterprises from the banking sector of 4.3 percent of GDP in 2012/13, not taking into account non-bank financing of the Renaissance Dam. This implies overall public sector (including public enterprises) borrowing of at least 9.4 percent of GDP in 2012/13.

**10. Although the monetary stance remains generally tight to keep inflation in single digits, recent developments point to some relaxation.** Base money contracted by 4 percent in 2011/12, achieved by not extending any new NBE credit to the government and foreign exchange sales. Annual base money growth at end-May 2013 stood at 18 percent (compared to one percent contraction for end-May 2012) and the authorities adjusted only slightly the base money target for the year at 13 percent from 12.2 percent. The pickup reflects an increase in net domestic credit, net foreign assets, and in other items net. Achieving the 13 percent target implies a very tight monetary policy for the remainder of the fiscal year. The reserve requirement ratio has been further lowered recently (March 2013) from 10 percent to 5 percent, following an earlier (January 2012) lowering by 5 percentage points, and NBE sterilized the resulting liquidity injection through the sale of certificate deposits, reflecting lack of clarity in monetary policy decision-making. Broad money growth remains somewhat high and stood at 28 percent in 2012/13.

**11. The external current account deficit widened slightly to US\$3 billion in 2012/13 from US\$2.8 billion in 2011/12, reflecting a weaker trade balance, although it improved as a ratio of GDP from 6.6 percent to 6.4 percent.** Export performance suffered from a decline in prices and weak external demand conditions, growing only 3.2 percent (in nominal terms), while continued infrastructure and industrial investment and higher fuel importation contributed to an increase in imports by 6.3 percent. Transfers brought in a net inflow of around US\$5 billion due to a surge in net private transfers that more than offset a decline in official transfers. Increased loan



disbursements to the central government and public enterprises yielded a capital account surplus of US\$3.4 billion. The resulting surplus on the overall balance of payments was less than US\$0.2 billion (0.4 percent of GDP) compared to a deficit of US\$1.1 billion (2.5 percent of GDP) in 2011/12. The NBE's gross international reserves slightly declined to US\$2.2 billion (1.8 months of imports) at the end of 2012/13 from US\$2.3 (1.9 months of imports) at the end of 2011/12.

**12. Foreign exchange supply came under pressure in the first half of 2012/13.** The passing of Prime Minister Meles created uncertainty and excess demand in the foreign exchange market which was also reflected in a widening of the premium in the parallel market. Since its previous peak in October 2008, the Real Effective Exchange Rate (REER) reached the highest level in November 2012, indicating an erosion of competitiveness gains from previous devaluations which may also be a factor in the recent trade performance. This has started to turn around with the recent decline in inflation, although the REER may still be significantly overvalued based on the IMF's Consultative Group on Exchange Rate methodology (Annex II).

## B. Medium Term Outlook and Risks

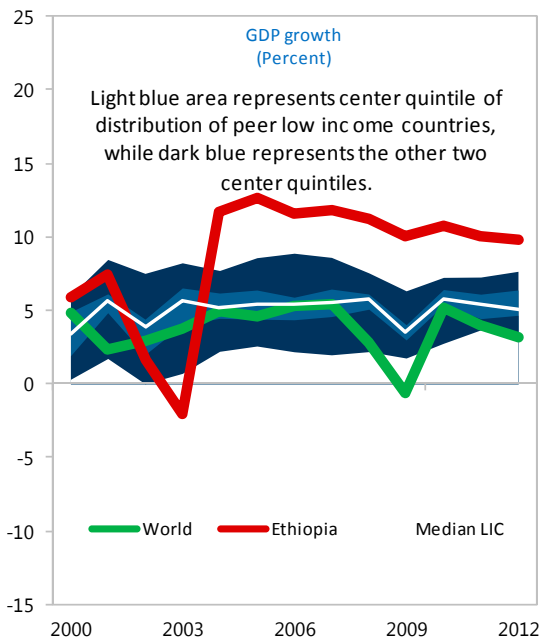
**13. Outlook.** Inflation has been brought down to about 7 percent at end-2012/13 and is projected to remain in single digit over the medium-term.<sup>6</sup> The current account deficit as a percentage of GDP is projected to slightly improve over the medium-term, as exports recover after declining in 2012/13. Moderate recovery in external demand and ongoing efforts to improve productivity, increase value-added, and diversification of the export base (covering, for example, agricultural and agro-industrial, horticultural, livestock, light manufactures, and electricity exports) are expected to support export growth. Overall economic growth is projected to remain robust in 2013/14 and beyond but fall short of the highly ambitious GTP target. Constraints on external financing for public investment, uncertain external demand, and a cumbersome business environment are the factors underpinning the growth shortfall. Reflecting continued uncertain global environment and unchanged policies, the projected growth rate tapers-off over the medium-term falling further short of the ambitious GTP target.

**14. Risks.** Key risks to the outlook include (i) a continuation of limited financing for infrastructure investment in the GTP; (ii) re-emergence of severe foreign exchange shortages; (iii) significant growth slowdown in the major emerging market countries; and (iv) weather-related shocks, particularly a possible drought returning to the Horn of Africa (Table 1).

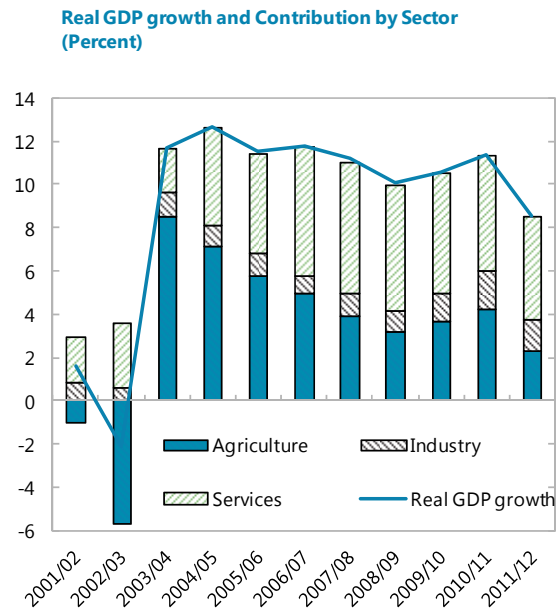
<sup>6</sup> Taking into account developments on the ground, in particular better than anticipated inflation at the end of the fiscal year 2012/13 and less severe negative real interest rates, staff has adjusted its projections, notably on broad money.

**Figure 5. Ethiopia: Comparative Growth and Inflation Performance**

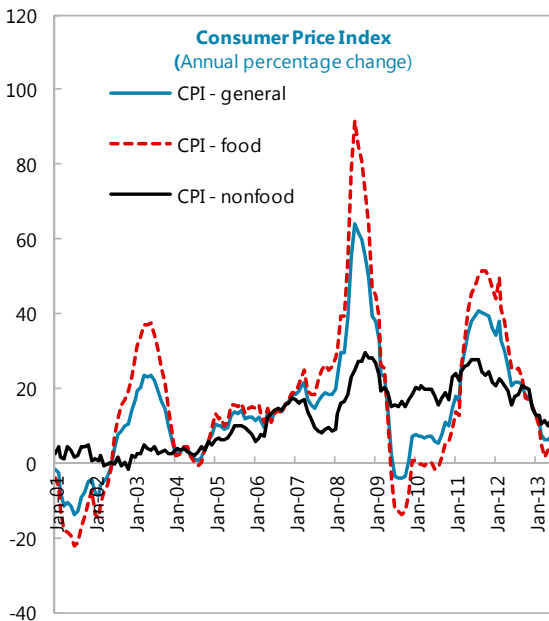
Growth remains above the median LIC and the world...



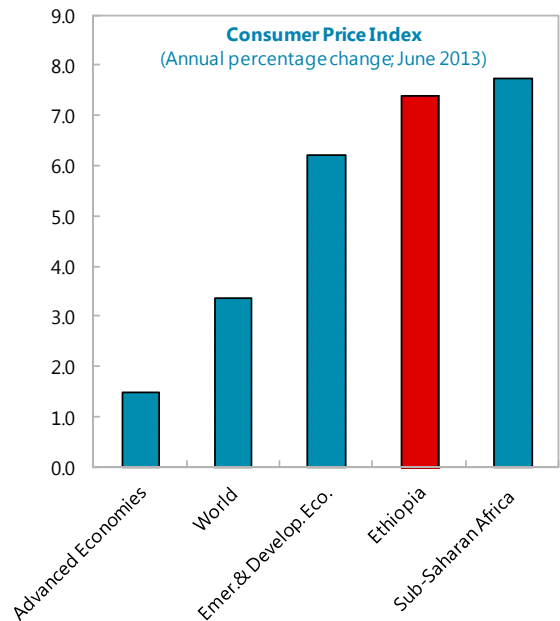
...driven mainly by agriculture and services.



Inflation has drastically come down ...



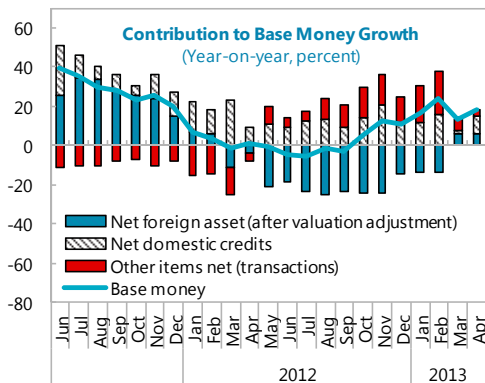
...although it remains slightly high compared to emerging and developing economies.



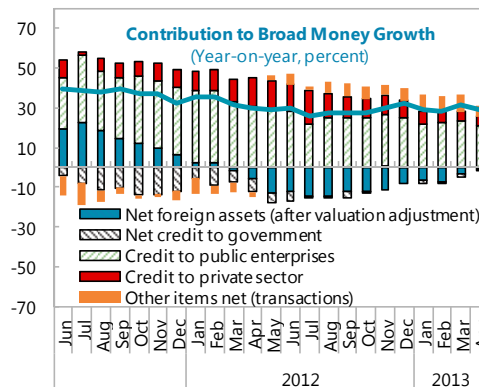
Sources: Ethiopian authorities and IMF staff estimates.

**Figure 6. Ethiopia: Recent Economic Developments**

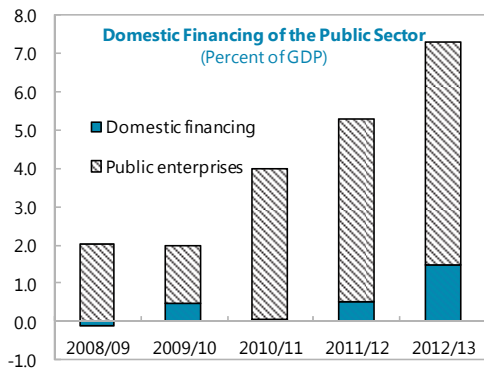
After a drastic tightening of base money reflecting the implementation of base money nominal anchor, base money growth has moderately increased in 2012/13...



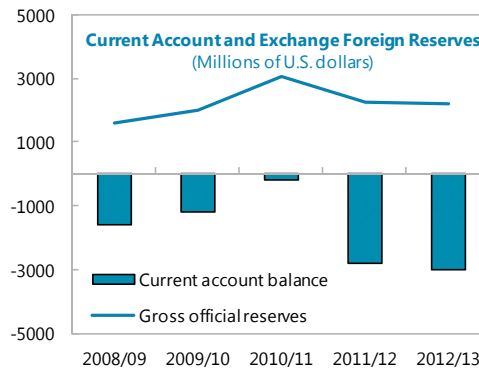
...and broad money growth remains high on account of strong lending to public enterprises.



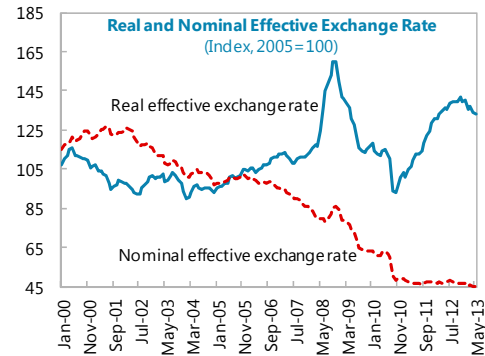
Government budget execution has been tight but the public sector as a whole has been stimulative.



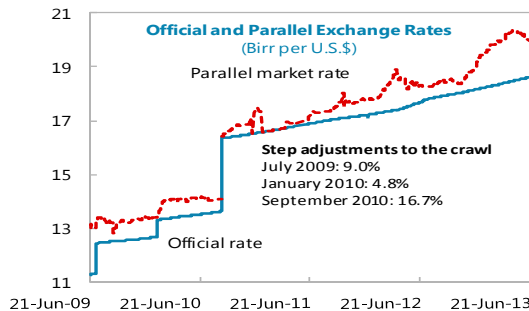
Foreign reserves which were initially run down to control liquidity remain at low level.



Due largely to high inflation, improved competitiveness as a result of exchange rate adjustments in 2009-10 had fully given way by end-2012/13.



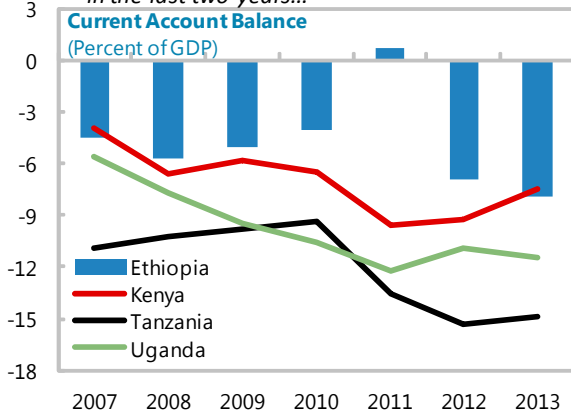
Foreign exchange supply came under pressure in the first half of 2012/13 resulting in a widening of the premium in the parallel market.



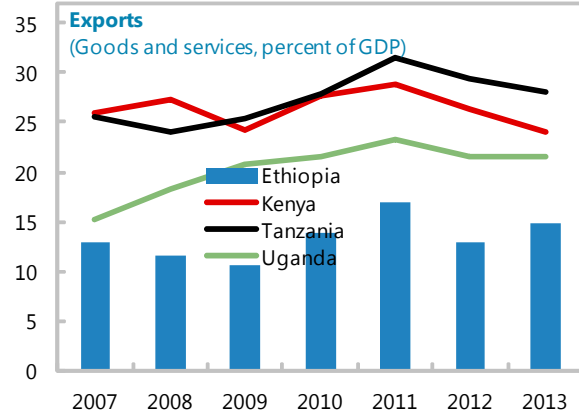
Sources: Ethiopian authorities and IMF staff estimates.

**Figure 7. Ethiopia: International Comparison: External Vulnerability**

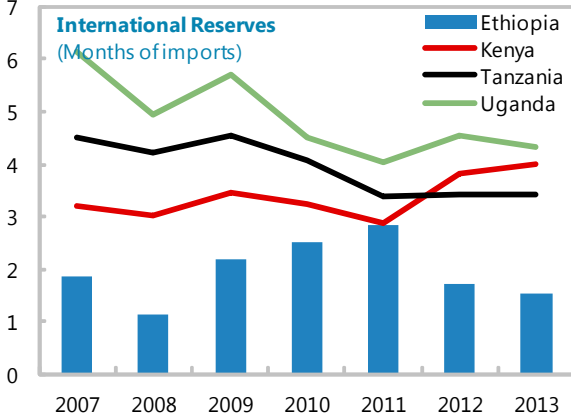
*Ethiopia's current account deficit widening in the last two years...*



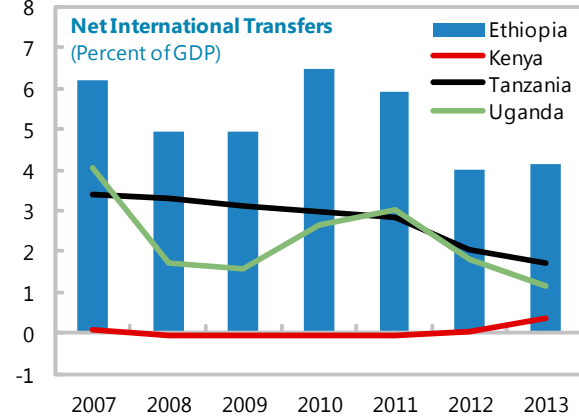
*... with relatively low exports base...*



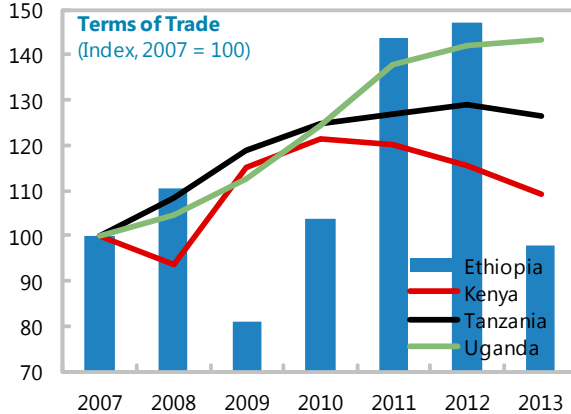
*...and low reserve coverage...*



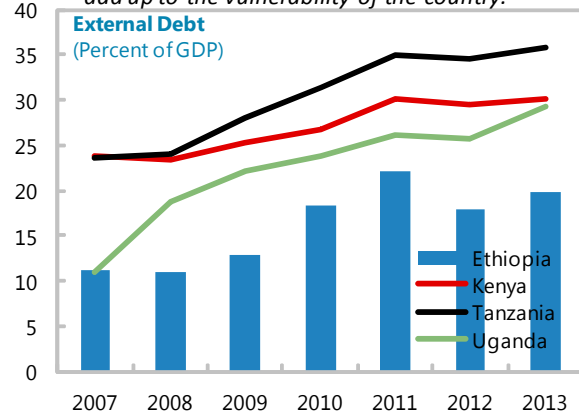
*...but strong remittances and official transfers.*



*Particularly volatile terms of trade...*



*...and low but growing external debt could add up to the vulnerability of the country.*



Source: IMF World Economic Outlook.

Table 1. Ethiopia: Risk Assessment Matrix<sup>1</sup>

Source of Risks	Relative Likelihood	Impact if Realized	Policy response
Financial stress in the euro area re-emerges (triggered by stalled or incomplete delivery of national and euro area policy commitments).	Medium	The impact of such a stress would include falling commodity prices and higher risk aversion. Specifically, it would reduce demand for Ethiopian exports and lower coffee prices, and also result in shortfalls of aid flows, lower remittances, and limited financing for infrastructure investment in the GTP.	Restrain fiscal policy while shielding low-income and vulnerable households, in particular appropriate pacing of public enterprises and infrastructure investment.
Deeper than expected slowdown in Emerging Markets (EMs) (reflecting lower than anticipated potential growth).	Medium	A deeper than expected slowdown in EMs would lead to commodity price decline with a negative impact on Ethiopian exports. It would result in severe shortfalls of financing (especially from China), and a decline in remittances. The financing of the GTP would be jeopardized with significantly lower growth.	Restrain fiscal policy while shielding low-income and vulnerable households, in particular appropriate pacing of public enterprises and infrastructure investment.
Sharp slowdown in growth in China (buildup of excess capacity eventually resulting in large financial losses).	Medium	FDI from China, which has been rising rapidly across sectors, could decrease, slowing development of newly emerging export sectors, like textile and leather manufacturing. Major infrastructure investments, particularly in power, telecom, and roads, may not be fully financed, delaying the implementation of the GTP.	Appropriate pacing of public enterprises and infrastructure investment.

Table 1. Ethiopia: Risk Assessment Matrix<sup>1</sup> (concluded)

Source of Risks	Relative Likelihood	Impact if Realized	Policy response
Strain on the state-owned Commercial Bank of Ethiopia resulting from increased domestic financing of GTP.	Medium	Given the systemic importance of CBE (70 percent of total banking sector assets), it would slow down the entire Ethiopian economy, resulting in significant deceleration of medium-term growth and a buildup of further vulnerabilities on both domestic and external fronts.	Greater role for private banks (including opening up to foreign banks). Strengthen banking supervision capacity at NBE and rigorously apply the limit of 25 percent of capital for loans to related parties and the limit of 15 percent of capital for a single borrower.
Lack of sufficient financing for GTP.	High	Lower growth.	Appropriate pacing of public enterprises and infrastructure investment.
A worsening of the foreign exchange shortage.	High	Difficulties in financing imports with negative impacts on growth. Rapid devaluation, leading to higher inflation and larger fiscal deficit	Greater flexibility in the exchange rate management. Buildup of foreign reserves to 3 months of import cover.
The return of drought to the Horn of Africa.	Medium	Higher food prices, leading to an increase in inflation and lower growth.	Shielding poor households and tight monetary policy, minimizing second round effects.
Global oil shock triggered by geopolitical events (driving oil prices to US\$140 per barrel).	Low	A global oil shock triggered by geopolitical events (driving oil prices to US\$140 per barrel) would not only worsen trade and current account balances, it would also put pressure on inflation and slow growth.	Maintain full pass-through into domestic prices to contain fiscal impact, while minimizing impact on the poor through well targeted subsidies.
Non-oil commodity price increases.	Low	Non-oil commodity price fluctuations affect both export price (coffee) and import price (wheat) in Ethiopia. The negative impact from the import price increases is likely to be offset by the benefit of export price increases.	Build policy buffers as a contingent plan by increasing international reserves coverage.

<sup>1</sup>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 of risks listed 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 of 30 percent or more). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities.

## PROMOTING INCLUSIVE GROWTH AND REDUCING VULNERABILITIES

**15. Ethiopia has been able to translate its broad-based economic growth into significant poverty reduction.** Both rural and urban areas have experienced significant increases in per capita consumption between 1995 and 2011. Improvements in nonmonetary measures, such as primary schooling and life expectancy have been particularly impressive (Table 7). However, further efforts are needed, to identify and address the needs of those in severe and chronic poverty and to significantly reduce malnutrition. In addition, to sustain the gains in poverty reduction, improving access to factor and product markets for the bulk of the population would be important.

**16. The government's objective is to become a middle-income country by 2025.** The GTP envisages achieving an average economic growth target of 11.2 percent over 2010/11–2014/15 and realizing the MDGs. Among the key pillars are raising agricultural productivity and scaling-up infrastructure and human capital development. The authorities seek to realize their ambitious development objectives through proactive public policies with heavy state involvement in infrastructure and industrial investments. Although the required financing for the GTP has not been fully spelled out, the expansion of domestic credit to public entities has constrained the availability of credit and foreign exchange for the private sector. Policies thus need to be adapted for an appropriate balance between the public and private sectors to enhance the resiliency of the country's developmental model.

**17. On the basis of a continuation of current policies, a deceleration of medium-term growth is expected, pointing to the need for policy adjustments.** The baseline projections assume the continuation of current policies, including constraints on private banking activities, directed lending with artificially low real interest rates and allocation of foreign exchange to priority public investment projects. Some of these policies undermine the authorities' growth objectives and have contributed to the recent foreign exchange shortages, especially for the private sector. Domestic financing is unlikely to meet the requirements of the GTP and prospective external inflows are insufficient to fill the gap. Absent mid-course policy correction, in particular strengthening private sector leverage in the economy, the government's 11 percent growth target is likely to be elusive. Based on a domestic financing which is less compared to full financing of the GTP, staff projects growth in the 7–7.5 percent range over the medium term (Table 2).<sup>7</sup>

<sup>7</sup> Domestic financing and prospective external inflows amount roughly to two third of full financing of the GTP.

**18. Policy discussions focused on sustaining robust and inclusive growth and structural transformation while maintaining macroeconomic and financial stability and mitigating vulnerabilities.** Key recommendations include (i) rationalizing and appropriately pacing public sector investment, especially for state-owned enterprises, (ii) keeping inflation under control, eliminating exchange rate overvaluation, and restoring reserve adequacy; (iii) strengthening financial deepening and inclusiveness, bringing real interest rates to positive levels, and enhancing access to finance for farmers and small and medium enterprises; and (iv) increasing the scope for the private sector's role in the economy (Table 1). The implementation of these recommendations would facilitate financial development that should enable less distortionary financing of the GTP that is consistent with debt sustainability.

**19. Staff has developed an alternative scenario that targets stronger growth while safeguarding macroeconomic stability and reducing vulnerabilities and that is consistent with the policies mentioned above (Table 6).** Under staff's alternative (adjustment) scenario, the growth rate is projected to rise to 9.5 percent in 2016–17 and inflation is targeted to decline further to 6 percent by 2014–15, as positive real interest rates expand the deposit base, the exchange rate is kept competitive, private sector access to credit from the banking system increases.

## C. Fiscal Policy: Stance and Inclusion

### Fiscal stance

**20. The fiscal stance embodied in 2013/14 general government budget submitted to parliament recently is appropriately restrained (Tables 3a and 3b).** However, despite the government's revenue mobilization efforts, the revenue-to-GDP ratio is projected to fall from 13.2 percent in 2012/13 to 12.9 percent in 2013/14. Reflecting the ongoing efforts to improve tax administration, the tax-to-GDP ratio is projected to rise but nontax revenue is slated to fall on account of lower dividends from state-owned enterprises. The authorities are relying on administrative improvements to increase revenue substantially. Staff encouraged the authorities to consider the revenue potential of reducing tax expenditure and tax incentives and improved tax collection, along the lines identified by IMF FAD technical assistance.<sup>8</sup>

**21. The budgetary focus on pro-poor spending has been impressive and the 2013/14 budget aims to strengthen this further (Box 1).** To maintain the ratio of poverty-reducing expenditure to GDP, its share in the total expenditure will need to rise as federal government

<sup>8</sup> Since 2012 FAD undertook a series of TA missions, recommending rationalization of tax incentives and tax expenditures. Staff alternative scenario suggests that annual tax revenue gain ranges from 0.4 percent to 2 percent of GDP over the next five years.



support to regional governments for MDGs wanes as projects receiving this allocation approach completion by 2014/15, the target year for the MDGs (for a discussion of pro-poor spending see also the accompanying Selected Issues Paper).

**22. Public financial management (PFM) reforms are yielding significant improvements in the budgetary processes.** Program-based budgeting is in the second year of full implementation and cash management reform, with the aim of reducing idle cash in the various government accounts and improving the quality of fiscal reporting, is progressing well. Staff stresses the need to maintain the momentum in these areas. The IMF's Fiscal Affairs Department is prepared to provide continued technical assistance as requested by the authorities.

### **Public sector debt**

**23. The pace of accumulation of overall public sector debt deserves close attention.** A rapid growth of credit to public enterprises to finance major investments in dams, factories, and housing construction continues to drive this buildup. The net worth of the government is thus heavily exposed to the direct borrowing by these enterprises and contingent liabilities stemming from such lending by CBE and DBE. Staff stresses the need for comprehensive and timely information on the financial position of public enterprises as part of the enhancement to the medium-term debt strategy.

**24. Debt sustainability analysis continues to show that Ethiopia remains at a low risk of external debt distress.** It is predicated on a conservative disbursement profile that is considerably lower than the requirements for the full implementation of the GTP. Staff encourages the authorities as in the 2012 Article IV consultation to seek concessional external financing and reconsider the pacing of the investments if scaled-up external financing on manageable terms is not forthcoming and authorities intend to maintain their low risk of external debt distress.

**25. Domestic debt is rising and vulnerabilities will continue to increase as large public investments draw financing from domestic sources.** Beyond a certain limit, such financing could be destabilizing and/or inflationary, suggesting that careful consideration should be given to the sustainability of the overall financing envisaged in the GTP. Consideration should be given to developing a comprehensive debt management strategy covering total public debt, including the debt of public enterprises, to improve public fiscal management and monitoring of the total fiscal stance.

## Fiscal policy and inclusiveness

### 26. The tax structure of Ethiopia with its heavy reliance on indirect taxes suggests scope for making it more equitable even though income tax brackets appear somewhat progressive.

Staff could not estimate the incidence of taxes for various income cohorts due to data constraints. However, tax revenue in Ethiopia derives largely from international transactions—on average 4.8 percent of GDP in 1999/00–2011/12, compared with regional comparators' average of 1.4 percent—suggesting a relatively

Text Table 1. Tax-to-GDP ratio  
(Average over the period 1999/2000 — 2011/2013)

	Income	Goods & Services	International Trade
Ethiopia	3.70	2.42	4.82
Kenya	7.53	8.50	1.89
Tanzania	3.54	6.23	1.12
Uganda	3.30	6.89	1.13
Regional comparators' average	4.79	7.21	1.38

Sources: National authorities and IMF staff calculations.

regressive revenue structure. Income taxes, which are considered more progressive than indirect taxes, averaged 3.7 percent of GDP in the same period against the regional comparators' average of 4.8 percent of GDP. On the other hand, domestic taxes on goods and services stand only at 2.4 percent of GDP as opposed to 7.2 percent of GDP for regional comparators' average. There is an apparent potential to raise more revenue from income tax and domestic taxes on goods and services to support growth promoting and social expenditure. Income tax revenue could be boosted by ensuring adequate tax collection from public enterprises and by broadening the tax base through promoting the private sector.

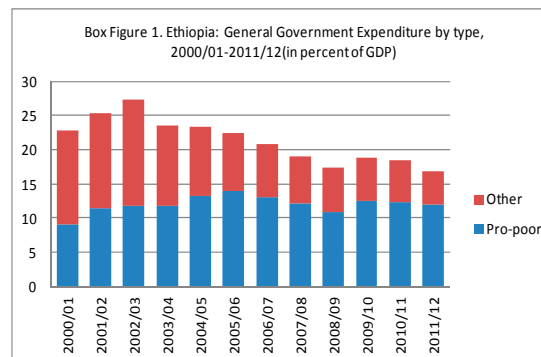
**27. The authorities' focus on pro-poor capital expenditure has resulted in improvements in human capital and physical infrastructure.** Strong investment-led economic growth has also delivered improvements in the employment conditions in the urban areas, but youth and female unemployment are still high and bringing them down remain a challenge. While the poor have generally benefited from strong economic growth the benefits have not been realized by poorest to the same extent. Thus, more focused efforts would be needed to lift up the poorest of the poor.

### Box 1. Ethiopia: The Budgetary Focus on Pro-poor Spending

Despite the tight resource constraint, the government has been successfully maintaining public investment and pro-poor spending in line with GDP (Box Figure 1). While the expenditure-to-GDP ratio has declined from the peak of 27.3 percent in 2002/03 to 16.9 percent in 2011/12 (partly reflecting an exceptionally high emergency food assistance in 2002/03), pro-poor expenditure have been maintained, averaging 12.4 percent of GDP over the 10 year period.<sup>1</sup> The key to achieve this outcome has been the prioritization through the budgetary processes, and the strong pro-poor focus that has been instrumental in Ethiopia's progress toward the MDGs.

Within pro-poor spending, recurrent expenditure has been restrained and more emphasis has been given to capital expenditure. The restraining of recurrent spending has taken place across all the sectors, with notable decline in the ratios of current spending-to-GDP in the education and health sectors, reflecting public sector wage restraint during the episode of high inflation.

The rise in pro-poor capital expenditure has been concentrated mostly in the road sector. This heavy investment in roads has paid off as the total road length has increased by a third (from about 36 thousand kilometers to about 49 thousand during the Plan for Accelerated and Sustained Development to End Poverty (PASDEP) period), the road conditions have improved (with the proportion of roads assessed as being in good condition having increased from 64 percent to 81 percent during the PASDEP period), and the access to all-weather roads has improved.



<sup>1</sup> Pro-poor expenditure in the official definition consists of education, health, agriculture, natural resources (water), and roads.

#### Authorities' views

#### 28. The authorities expect their revenue mobilization efforts through administrative improvements to deliver substantial revenue increases (some 4 percent of GDP by 2014/15).

They concurred with staff on the desirability of increasing the share of direct taxes over the medium term and on the need to review tax expenditures and exemptions. They indicated that all public enterprises were subject to corporate income taxes. They also noted the difficulty of identifying the appropriate investment-friendly exemptions and stressed that continued technical assistance from the Fund and other development partners was necessary to support their efforts.

### D. Monetary Policy

29. The NBE seeks to control inflation through targeting base money and intervenes in credit allocation to ensure that broad money is consistent with government's inflation, growth and employment objectives. Although inflation has been brought down to single digits, the risks remain on the upside, especially considering the downward stickiness of nonfood inflation

and the successive reductions of reserve requirements. To the extent that directed credit allows access to finance across selected industries and geographical areas, it could contribute to financial inclusion. However, significant segments of the economy, especially in rural areas, remain constrained by lack of access to credit. The conduct of monetary policy suffers from rigidity in interest rates and inflexible instruments to achieve monetary objectives. Changes in reserve and other requirements and foreign exchange sales are used for liquidity management and for achieving other developmental objectives.

**30. The NBE's monetary policy stance has contributed to the decline in inflation.** Inflation has come down to single digits with beneficial effects for the general population and especially for the poor. Base money increased by 13 percent in 2012/13 (Table 4). In addition to the slowdown in global food and fuel price inflation, this has been instrumental in the recent decline in inflation to 7.4 percent in June. Limited resort to NBE financing of the government and mopping of liquidity through sales of foreign exchange also helped in this regard, although this is at the expense of building foreign exchange reserve buffer.

**31. Monetary policy implementation and liquidity management would be greatly enhanced by the use of indirect monetary policy instruments and allowing for price discovery.** At present, the NBE uses changes in reserve requirement and foreign exchange sales as the main tools and has also deployed offsetting deposit requirements for liquidity management, and for achieving other developmental objectives. While the reserve requirement ratio has been lowered recently (March 2013) for a second time from 10 percent to 5 percent, the NBE simultaneously sterilized the associated excess reserves through the issuance of the NBE's certificate of deposits. To preserve the gains on inflation monetary policy will need to remain vigilant, taking into account the effect of changes in reserve requirement on the money multiplier and the growth of broad money. Going forward, monetary policy implementation would need to take into account the renewed NBE financing of the government's budget deficit and changing money demand conditions. In the context of relatively low levels of foreign exchange reserves, monetary operations with market priced Treasury or NBE bills can provide the NBE with greater flexibility in liquidity management.

**32. Activating the Treasury bills market would be important for the development of the money market.** It could also improve the monetary transmission mechanism, allow for establishing a short-term risk-free yield curve, encourage banks to more actively manage their own liquidity positions and allocate risks. Treasury bill market remains also a precondition for establishing a market for longer-term instruments, such as Treasury bonds. Technical assistance from the Fund could be helpful in this regard.

**33. Proper coordination and consistency between monetary and exchange rate policies are critical for further financial market development and orderly conditions in the foreign exchange market.** The foreign exchange market developments in the first half of 2012/13 and the premium in the parallel market suggest considerable scope for improving the functioning of the NBE's foreign exchange sale mechanism and the interbank market. Greater flexibility in exchange rate and presence of NBE in the foreign exchange market whenever necessary can be helpful in preventing excessive volatility and disorderly conditions in the market. Exchange rate flexibility is also essential for the competitiveness of the traded goods sector which staff considers critical for the realization of the authorities' growth objectives. For NBE to effectively play its role in this regard, staff welcomes its objective of raising its foreign exchange reserve target to US\$2.5 billion (about 1.9 months of imports) by the end of 2013/14 and further to the equivalent of 3 months of imports over the longer term as a move in the right direction. However, staff would prefer a faster buildup of foreign exchange reserves—which would be facilitated by an increased use of domestic securities (rather than foreign exchange sale) for liquidity management—to 3 months of import cover (Table 6).

#### ***Authorities' views***

**34. The authorities agreed on a restrained monetary stance to sustain single digit inflation but were more circumspect about any policy response to international food and fuel prices shocks.** They noted that low nominal interest rates were necessary to finance public investment but agreed on the need to have positive or near zero real interest rates. They were also open to considering flexible pricing of securities for the conduct of monetary policy but indicated that this would be dependent on sustaining single-digit inflation for some time. They indicated that renewed NBE financing of the budget is consistent with the demand for base money and in the event that money demand conditions changed, direct instruments will be used. They also stressed that foreign exchange market pressures in the first half of 2012/13 reflected the uncertainty and a speculative element in the wake of Prime-Minister Meles' passing away.

## **E. Financial Sector Policy and Inclusion**

**35. Access to finance in Ethiopia is mainly through the banking sector and to some extent the microfinance institutions; capital markets are yet to be developed.** The country's banking sector comprises one state-owned development bank and 18 commercial banks—including two state-owned, with one dominant, CBE, with assets representing about 70 percent of the sector total—as of May 2013. The remaining 17 commercial banks, mainly private, together account for the remainder. Out of a population of nearly 90 million, only 7.1 million have deposit accounts, i.e., less

than 8 percent of Ethiopians have a banking account. The proportion of borrowers is even smaller (a mere 112,793). Access to finance in rural areas is limited, with only 31 microfinance institutions (MFIs) as of end-June 2012, providing financial services to 2.9 million clients. Fifteen insurance companies exist with each insurance branch serving on average a population of 335,000. The industry is not sufficiently developed to mobilize significant contractual savings.

**36. Broadening financial inclusion could have a significant payoff in terms of economic growth.** The limited reach of the financial sector constrains the opportunities for small entrepreneurs and savings instruments for the poor, subjecting them to vulnerabilities in the event of shocks. The structure and regulation of Ethiopia's financial system contribute to these limitations. The authorities' development strategy relies heavily on directed lending to public enterprises mainly by the CBE.

**37. Commercial banks continue to be subject to the April 2011 directive requiring them to hold 27 percent of new loan disbursements in low-yield NBE bills.** The proceeds of these bonds are transferred to the state-owned Development Bank of Ethiopia (DBE) which, according to the stated policy is supposed to on-lend them to government targeted private sector activities. However, an analysis of DBE balance sheet reveals that more than half of the proceeds are used to buy T-bills. This, combined with the policy of directed lending mainly to public enterprises in an environment of negative real interest rates, results in a significant transfer of resources from creditors (savers) to borrowers, especially the public sector.

**38. The banking sector remains highly profitable despite a slowdown in overall credit extension to the economy.** Overall credit to the nongovernment sector grew by 22 percent over the first 10 months of the fiscal year 2012/13 compared to 50 percent over the same period last year in the context of higher inflation. Of this, 79 percent was allocated to the public enterprises and the rest to the private sector. The authorities indicate that the composition of very short-term fast rolling-over borrowing of the public and private sectors was more even. Driven by aggressive expansion of the number of branches by banks, demand deposits increased by 16 percent while time and saving deposits increased by 22 percent over the same period. Owing to increased lending rates and net interest margins, profitability in the banking sector remains strong with return on assets of 3.1 percent and return on capital of 47 percent as of March 2013.

**39. The NBE directive requiring banks to hold NBE bills equivalent to 27 percent of their lending has been distortionary and has triggered unnecessary portfolio adjustment by banks.** Since the directive initially did not discriminate short-term from long-term loans, private banks adjusted their portfolios toward long-term loans to avoid high NBE-bills purchase due to higher

turnover of short-term loans. They also raised fees and commissions to make up for lower returns on NBE bills holding. The subsequent amendment to the NBE directive also requires banks' short-term loans to be at least 40 percent of total loans at any given time.

**40. Staff reiterated the 2012 Article IV recommendation and suggested phasing out the 27 percent NBE bills holding requirement.** The directive was introduced to provide funding to DBE for lending to priority projects. This modality is indirect and it would be better if DBE funds itself through bond issuance, supported by appropriate credit enhancements, including attractive pricing, as needed. In the interim, proceeds from this requirement transferred to the DBE and not yet committed could be used to increase credit for small scale entrepreneurs to promote financial inclusion. Purchase of T-bills by DBE from these proceeds should be substantially reduced and limited to the DBE's day-to-day liquidity management requirements. In addition, the recent amendment of the NBE directive requiring banks to hold 40 percent of total loans in short-term loans should be withdrawn.

**41. Although available financial soundness indicators (Table 8) do not point to immediate risks,** the systemic importance of the CBE and the concentration of large exposures to single entities warrant strict supervision of compliance by the NBE. On the whole, the banking sector seems sound with aggregate CAR at 14.6 percent and system-wide NPL ratio at 2.4 percent as of March 2013. The NBE is strengthening its oversight of the financial sector through risk based supervision. NBE regulations set a limit of 25 percent of capital for loans to related parties and a limit of 15 percent of capital for a single borrower. These limits should be rigorously applied to the borrowings of public enterprises where they currently do not apply. The DBE should also be subject to similar oversight and supervision. Going forward, allowing greater role for private banks (including opening up to foreign banks) could reduce the systemic importance of CBE and the associated vulnerabilities (Table 1).

**42. Promoting financial inclusion is an essential requirement for pro-poor development.** Staff supports the efforts the authorities are already devoting in this area. Among the promising avenues are seeking greater technology based penetration in rural areas to promote access to financial services; allowing banks to operate microfinance institutions with funding for on-lending purposes from international financial institutions eager to increase access in rural areas in low income countries, thereby giving time for domestic intermediation efforts to be created; and forging partnerships with international organizations with experience in rural and microfinance.

**Authorities' views**

**43. The authorities do not share staff concerns about the financial sector.** They disagreed with staff assessment of the impact of the 27 percent NBE bill requirement arguing that private banks remain highly profitable. They disagreed that private banks are raising fees and commissions to make up for lower returns on NBE bills holding. The authorities indicated that NBE was vigilant in taking actions to mitigate any risks that would emerge. They had adopted risk-based supervision and assigned a desk officer to each bank and were holding monthly prudential meeting with banks as well as conducting quarterly credit and liquidity risk stress testing. In addition, implementation of World Bank financial sector capacity building recommendations was ongoing. The authorities acknowledged the CBE's systemic importance and were confident in their close supervision of the bank. They considered an assessment such as under the FSAP premature until the capacity building exercise being undertaken was completed. While they would welcome technical assistance and knowledge sharing partnerships with international organizations with respect to rural and microfinance institutions, they saw risks in allowing IFIs to provide funding to MFIs.

**F. External Policy**

**44. External competitiveness has eroded and foreign exchange reserves cushion remains modest considering that foreign exchange sales are used to sterilize liquidity.** Improved competitiveness—as a result of exchange rate adjustments in 2009–10—had fully given way by end-2011/12<sup>9</sup>, with the exchange rate currently estimated to be overvalued by 10–14 percent (Annex II). In the absence of an active Treasury bill market, foreign exchange reserves have been the primary monetary policy tool to affect liquidity. Gross official reserves have declined since early-2012 and are currently at about 1.8 months of imports (Table 5)—compared to the reserve adequacy assessment, which points to the need for a much higher (6.8 months) cushion (Annex III). Going forward the real appreciation needs to be reversed in order to reduce vulnerabilities and restore competitiveness and foreign exchange reserves need to be replenished.

**45. The NBE is targeting annual increases of US\$300 million in gross international reserves over the medium term.** This would maintain reserves at around 2 months of imports. Together with the expected replenishment of foreign exchange reserves of commercial banks, the target implies achieving an overall balance of payments surplus of 1 percent of GDP in 2013/14. The authorities expect to achieve this outcome through appropriate monetary and foreign exchange policies.

<sup>9</sup> The de facto exchange rate regime is crawling peg to the U.S. dollar and the de jure regime is managed floating. Adjustments to the peg took place in July 2009 (9.0 percent), January 2010 (4.8 percent), and September 2010 (16.7 percent).



However, given the lack of monetary instruments for sterilization and the overvalued exchange rate, this could be challenging.

### **Authorities' views**

**46. The authorities were of the view that in the context of their de jure managed float regime, the exchange rate was allowed to adjust to maintain competitiveness but it was very difficult to pin this down precisely and determine magnitude of the over- or under-valuation.**

## **KEY STRUCTURAL REFORMS FOR PROMOTING INCLUSIVE GROWTH**

**47. There is a pressing need for policies to translate positive growth outcomes into stronger employment gains and further reduction in poverty and set off a dynamic, virtuous cycle of self sustaining and broad-based growth.** Thus far, the informal agricultural and trade sectors have been the main drivers of growth. The authorities see economic diversification and increased competitiveness as vital to creating more formal sector jobs and achieving strong inclusive growth. Their strategy of quickly addressing major infrastructure gaps (mainly in power and transportation) is a major step toward achieving their objectives. The GTP envisioned the structural transformation of the country, with the public housing scheme, roads, railroads, hydro-electric generation plants, sugar factories and other projects transforming the national labor market. Technical and vocational training for construction workers is provided and the program Competence of Excellence has certified more than 400,000 individuals. However, availability and high turnover of qualified workers constitutes a major challenge for the execution of the projects included in the GTP. Staff emphasized that achieving these objectives would require correcting structural bottlenecks, strengthening financial intermediation, leveraging more the private sector, and reducing the costs of doing business.

**48. Promoting financial deepening and inclusion in the country's development model is crucial, as borrowing by the public sector risks crowding out the private sector in a context of limited savings.** As in many developing economies, domestic savings in Ethiopia are low. Small and medium enterprises (SMEs) have very limited access to bank credit or other financial services. Over the first 10 months of 2012/13, 79 percent of total loans issued by the banking sector were allocated to the big public enterprises, with only 21 percent going to the private sector. Not surprisingly, in various business climate surveys, access to finance has been identified as one of the key obstacles to doing business. Enhancing access to credit (especially for agriculture and SMEs) will require efforts in many areas, including the elimination of the 27 percent NBE bill directive; training for entrepreneurs

in the preparation of adequate business plans; improving credit reporting systems; and strengthening enforcement of lenders' rights over collateral. Developing nonbank sources of financing such as contractual savings through promoting insurance companies and pension schemes should be considered to boost domestic savings. An assessment, such as under the FSAP, could provide a comprehensive diagnostic of the financial sector.

**49. Promoting the private sector's role in the country's development model is vital.** While Ethiopia has so far pursued a state-led development strategy, it may be approaching the limits of this strategy in engendering broad-based growth. A number of key sectors, especially manufacturing, are lagging behind and the scope seems wide for private sector involvement, while retaining control in some strategic sectors. In particular, opening up the telecommunication sector, sugar industry, and transport sector to private sector (including foreign investors) could attract new investments, improve efficiency and delivery of services, and increase public revenues.

**50. Transforming agriculture with the aim of improving its productivity is the linchpin of the reform program.** Transforming agriculture—which employs more than 50 percent of the labor force—from a subsistence into a commercial sector with value-chain linkages to manufacturing holds a great potential for reducing poverty. The authorities' strategy involves better use of the land inputs and labor with growing needs of qualified and better remunerated workers; an agricultural credit insurance scheme; and the setting up of the Agricultural Transformation Agency (ATA) to help poor farmers improve their production technology. Staff welcomes these developments, which are contributing to productivity improvements.

**51. Addressing the external competitiveness issue is critical (Box 2).** In the context of an overvalued exchange rate (10–14 percent), deteriorating terms of trade, and limited foreign exchange reserves, the authorities intend, going forward, to implement foreign exchange policy with a view of containing inflationary pressures. This policy—together with measures aimed at lowering domestic transportation costs, streamlining customs clearance procedures, putting in place needed infrastructure, and enhanced access to credit—should over time address the competitiveness problem. Staff's analysis indicates that bringing more flexibility in the exchange rate to eliminate its overvaluation would better support the country's economic development (Annex II).

### Box 2. Ethiopia: Export Competitiveness and Diversification

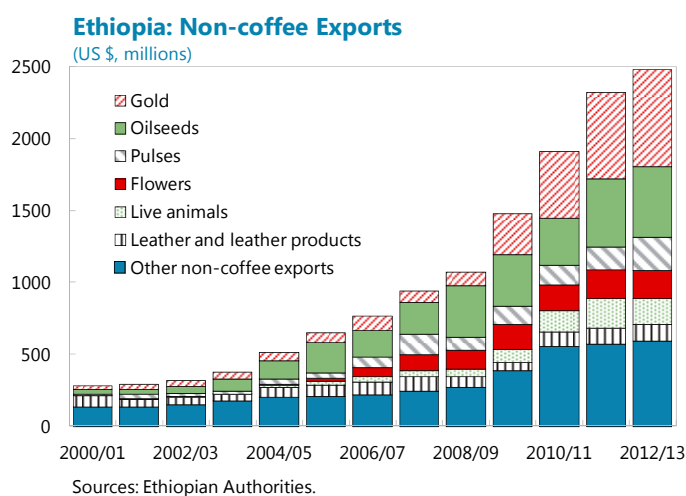
**Strengthening export competitiveness is critical to the success of authorities' development strategy.** In 2012/13, Ethiopia's exports of goods and services amounted to the equivalent of some 13 percent of GDP, about the average over the past two decades. The commodity-heavy export structure is subject to developments in international markets and has tended to vary significantly over the years—ranging from 9 to 17 percent of GDP—without demonstrating a clear trend.

**While exchange rate flexibility is critical, addressing structural factors are also important for improving productivity and performance of export industries.** The cost of transporting goods to markets is high, but improved transportation links are expected to significantly lower these costs. Several major road projects are under way along with a railroad from Addis Ababa and Djibouti. Together with streamlined customs clearance and other government procedures, the authorities aim at increasing gradually farm-gate prices relative to export prices (farm-gate prices currently constitute only 60 percent of export prices), thereby improving the incentives for exports.

**Ongoing and planned non-government investments—including in cold storage facilities and increased airline capacity—augur well for export diversification.** The

labor intensive cut flowers industry has the competitive advantage of low wages in Ethiopia which, in conjunction with a widening of export markets, should boost the nascent industry's exports. The development of Ethiopia's ample hydro-electric potential should also contribute to improved diversification of the export sector. Electricity exports to Kenya are expected to commence in 2014/15 and once the Renaissance Dam has been completed, electricity export is expected to increase further.

**Labor-intensive manufacturing hold considerable potential for further export diversification.** FDI into leather manufacturing and textile production indicate areas where Ethiopia seems to have a comparative advantage. Public sector investments in electricity and transport infrastructure would provide the necessary support for a scaling up of additional FDI into these and other manufacturing sectors. Their success will also depend on a competitive exchange rate.



**52. Reforming the current tax structure with its heavy reliance on indirect taxes with the aim of making it more equitable will further support inclusion.** Staff and authorities concurred that further technical assistances from the Fund's Fiscal Department will be helpful in this regard.

## OTHER ISSUES

**53. Data provided to the Fund are adequate for surveillance, albeit with notable shortcomings and delays.** Although GDP statistics in Ethiopia are subject to significant weaknesses, the national accounts compilation methodology improved considerably in 2011/12 and the authorities are continuing efforts to further strengthen their statistics. Staff has stressed the need to further improve national accounts data and offered technical assistance. Substantial information gaps on the health of the financial sector remain as the mission did not have access to detailed banks' balance sheet data in order to undertake a banking sector diagnostic. In addition, fiscal and BOP statistics require improvements. For example, comprehensive public sector data, including on public enterprises, are still lacking and would be desirable for a proper assessment of public sector finances.

**54. Ethiopia has yet to move to Article VIII status and maintains several exchange restrictions on payments and transfers for current international transactions that are not consistent with Article VIII.**<sup>10</sup> A unification of the official and parallel exchange markets would free up significant efficiency gains. Staff enquired about the terms of the 2006 China EXIM Bank Framework agreement with Ethiopia. The authorities indicated that the agreement is consistent with Ethiopia's commitments under the IMF's Articles of Agreement.

**55. WTO accession negotiations are ongoing.** Since the submission of the Memorandum of Foreign Trade Regime in 2006, four rounds of Working Party meetings have taken place. The authorities intended to join the WTO within the current development plan period, i.e., before end-2014/15, but this timetable may be stretched. Outstanding issues relate to domestic market access, including non-financial and financial services, state trading regime, and customs valuation practices.

**56. Ethiopia's anti-money laundering and combating the financing of terrorism (AML/CFT) regime is not in conformance with international standards.** In consequence, Ethiopia continues to be listed by the Financial Action Task Force (FATF) as among the jurisdictions with strategic

<sup>10</sup> See Informational Annex.

AML/CFT deficiencies that have not made sufficient progress in addressing them. The authorities explained the delay in addressing the FATF requirements by their interest in also ensuring compliance of their legal framework with the new FATF standard. In order to avoid further scrutiny by the FATF and possible counter-measures, Ethiopia should continue to work on addressing the long standing strategic deficiencies highlighted by the FATF, particularly in the areas of terrorist asset freezing and sanctions. In the meantime progress is being made in part owing to training provided by bilateral donors. Further technical assistance has been requested from the World Bank.

## STAFF APPRAISAL

**57. Ethiopia’s public sector led developmental strategy has delivered robust growth and rising standards of living.** Staff commends the authorities for their prudent macroeconomic management and the realization of robust growth and impressive progress in poverty reduction. Restrained fiscal and monetary policies have been instrumental in reducing inflation to single digits.

**58. A restrained overall fiscal stance is essential for macroeconomic stability and sustaining growth.** While the budgetary stance at the general government level has been restrained, staff urges the authorities to carefully monitor the operations of the overall public sector (including public enterprises) to properly calibrate the fiscal stance. Concentrating data collection on federal and regional governments, as currently is the case, provides only a partial view and fiscal policy would benefit from a more complete picture, including public enterprises, of the overall fiscal stance.

**59. Staff applauds the authorities for their achievements and urges them to continue and strengthen the policies for inclusive growth.** The poverty reduction strategies have achieved important results and the government’s focus on pro-poor expenditure has been paying off in terms of improved social indicators. The authorities should continue the momentum of revenue administration reforms and staff welcomes the ongoing reforms in public financial management to achieve the GTP fiscal objectives. Introducing measures to mobilize more revenue from income taxes and domestic taxes on goods and services equitably should be considered. Authorities should also consider adopting the FAD TA recommendations on rationalizing tax incentives and tax expenditures. Staff advises the authorities to strengthen the policies for inclusive growth, especially by making the tax system more progressive and maintaining and possibly expanding pro-poor spending as more revenues are mobilized.

**60. Preserving these gains and mitigating vulnerabilities and risks in order to achieve the objectives embodied in the GTP would require continued cautious policy stance as well as private sector involvement.** Ethiopia's public sector led developmental strategy is now at cross-roads. There is a need to carefully consider the balance between the public and private sectors in the economy. In light of the large financing need in the GTP, staff urges the authorities to reduce and streamline the role of public enterprises in the economy. Development of a strong and vibrant private sector is essential to sustain growth and attain middle income status. This would mean fostering competition in areas where public enterprises enjoy monopolies, gradually withdrawing from areas where they displace and crowd-out the private sector, and fully corporatizing and orienting outward through foreign partnerships those that remain. In particular, foreign direct investment should also be encouraged for example in trade logistics and communications sectors.

**61. The transformational power of the private sector could be further harnessed to generate employment and sustain development.** Opportunities for the private sector are an important dimension of inclusion. With its strong investment and trade capabilities, the sector could be a strong engine for creating employment opportunities for the youth. The authorities should thus strengthen competitiveness by improving the business climate and enhancing public private dialogue to better understand the needs of the private sector and create a supportive policy environment. They should also work with the World Bank—in particular its private sector arm, the International Finance Corporation—to incubate entrepreneurship for SMEs, youth, and women. They should increase vocational schools to address skills mismatch and support job creation for youth.

**62. NBE needs to continue its focus on keeping inflation in single digits, as the risks are on the upside considering the still high nonfood inflation and potential of shocks to food prices.** Staff suggests a cautious stance of monetary policy that keeps base money growth consistent with preserving the gains on inflation and achieving robust economic growth. Monetary policy will need to remain vigilant to increasing resource pressures and changes in broad monetary conditions taking into account the aggressive deposit mobilization by banks. It would also need to be supported by proper pacing of public enterprises' investment and a reconsideration of the renewed NBE financing of the government budget deficit.

**63. Staff urges the authorities to improve the efficiency and flexibility of NBE instruments, including through flexibility of nominal interest rates and development of market-based liquidity management.** Avoiding the use of reserve requirements as the main monetary policy instrument and focus on developing indirect instruments to achieve the monetary targets should be considered. Flexibility would be needed to make T-bills an effective instrument for liquidity management. Staff underscores that, with inflation in the single digit, the timing is right for bringing

flexibility in interest rates to increase domestic saving and to support inclusive growth. Raising interest rates should encourage saving which is important for scaling up investment, which in turn is vital for sustaining growth and broader inclusion.<sup>11</sup>

**64. More broadly, introducing policy measures to support higher domestic savings should be explored.** Consideration could be given to developing nonbank sources of financing such as contractual savings—e.g., (i) providing incentives for the emergence of more insurance companies; and (ii) strengthening pension schemes and other long-term savings instruments. Introducing mobile banking to increase access to finance is also vital to support inclusive growth.

**65. Phasing out the forced 27 percent holding of NBE bills by commercial banks would help promote financial deepening and facilitate the GTP financing.** The impact of this policy measure has been to crowd out private sector credit even if commercial banks are currently enjoying high profitability from higher non-interest income and interest rate spreads which is further squeezing out the private sector. Its phasing out would help realize the objectives of GTP in a much more sustainable manner. In the interim, at a minimum, the proceeds from this requirement that are transferred to the DBE should be used to increase credit for small scale entrepreneurs to promote financial inclusion. Purchase of T-bills by DBE from these proceeds should be discontinued.

**66. Strengthening capacity at the NBE for supervision and formulation of financial policies to promote inclusion for all segments of the economy is crucial.** This also encompasses banking supervision capacity to enable regular inspection of all banks and improve the quality of the analysis of banks' soundness.

**67. Staff supports the authorities' objective of building foreign exchange reserves, while encouraging them to bring some flexibility in the exchange rate.** Accumulation of foreign reserves initially to at least three months of imports would be desirable. Allowing more market-based movement of exchange rate with a view toward enhancing competitiveness and eliminating the spread between the parallel and official foreign exchange markets would be helpful. Using foreign reserves to manage liquidity in the context of a rigid (and overvalued) exchange rate risks external stability. In addition, better coordination of monetary and exchange rate policies with a view toward strengthening external competitiveness on a lasting basis would be welfare improving.

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<sup>11</sup> According to the Commission on Growth and Development (2008), for growth to be inclusive it is critical that it is sustainable (see also the October 2011 *Regional Economic Outlook: Sub-Saharan Africa*).

**68. Staff underscores the need for continued improvements in data quality.** There are significant financial sector data gaps and fiscal and BOP statistics require improvements. Comprehensive public sector data, including on public enterprises, data would be desirable for a proper assessment of public sector finances.

**69. Staff recommends that the next Article IV consultation with Ethiopia be held on the 12-month consultation cycle.** This is in accordance with the decision on consultation cycles, Decision No. 14747-(10/96) (9/28/2010).



**Table 2. Ethiopia: Selected Economic and Financial Indicators, 2009/10–2017/18<sup>1</sup>**

	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18
	Act.	Act.	Act.	Prel.	Proj.	Proj.	Proj.	Proj.	Proj.
(Annual percentage change)									
<b>National income and prices</b>									
GDP at constant prices (at factor cost) <sup>2</sup>	10.6	11.4	8.5	7.0	7.5	7.5	7.0	7.0	7.0
GDP deflator	1.6	20.0	34.2	11.3	6.9	8.9	8.0	7.9	8.1
Consumer prices (period average)	2.8	18.1	34.1	13.5	7.3	8.0	8.0	8.0	8.0
Consumer prices (end period)	7.3	38.1	20.7	7.4	8.0	8.0	8.0	8.0	8.0
<b>External sector</b>									
Exports (U.S. dollars, f.o.b.)	38.4	37.1	14.8	3.2	14.9	15.1	15.2	15.1	15.6
Imports (U.S. dollars, c.i.f.)	7.0	-0.2	34.0	6.3	7.5	10.7	8.5	7.8	7.2
Export volume	10.5	8.9	-0.4	14.0	15.3	12.8	16.6	16.6	15.1
Import volume	14.1	-3.8	25.9	6.8	8.9	12.4	9.7	8.3	7.3
Terms of trade (deterioration –)	38.3	23.5	8.2	-10.3	0.9	3.9	-0.3	-1.0	0.6
Nominal effective exchange rate (end of period)	-13.4	-26.5	2.8	...	...	...	...	...	...
Real effective exchange rate (end of period)	-9.7	-2.3	20.9	...	...	...	...	...	...
(Percent of beginning-period stock of broad money, unless otherwise indicated)									
<b>Money and credit</b>									
Net foreign assets	9.6	29.1	-12.7	2.2	3.6	2.3	2.3	2.1	1.8
Net domestic assets (including other items net)	14.7	10.1	43.0	26.4	18.4	17.7	17.2	16.9	17.2
Claims on the government	1.7	-2.9	-7.0	3.2	4.6	3.8	3.5	3.1	3.7
Claims on public enterprises	6.8	25.1	28.5	20.2	10.8	13.0	13.1	13.0	12.2
Claims on private sector	10.5	9.8	13.2	4.4	4.5	3.9	3.4	2.9	2.6
Broad money	24.3	39.2	30.3	28.5	22.0	20.0	19.5	19.0	19.0
Base money (annual percentage change)	6.5	40.7	-3.6	13.2	14.9	17.1	15.6	15.5	15.7
Velocity (GDP/broad money)	3.64	3.49	3.90	3.62	3.41	3.32	3.21	3.12	3.03
(Percent of GDP, unless otherwise indicated)									
<b>Financial balances</b>									
Gross domestic savings	5.2	12.8	16.5	15.9	11.3	13.7	14.1	14.6	15.5
Public savings	4.5	4.3	5.7	4.9	4.6	5.1	5.3	5.5	5.7
Private savings	0.6	8.5	10.8	11.0	6.6	8.6	8.8	9.1	9.8
Gross domestic investment	23.6	27.2	34.6	32.6	27.2	29.4	29.3	29.3	29.3
Public investment	14.9	19.6	26.5	24.3	18.8	20.9	20.7	20.6	20.5
Private investment	8.7	7.5	8.1	8.3	8.4	8.5	8.6	8.7	8.8
Resource gap	-18.4	-14.4	-18.1	-16.7	-16.0	-15.7	-15.2	-14.6	-13.8
External current account balance, including official transfers	-4.1	-0.7	-6.6	-6.4	-5.7	-6.0	-5.8	-5.6	-5.2
<b>Government finances</b>									
Revenue	14.2	13.7	14.0	13.2	12.9	13.3	13.4	13.5	13.6
Tax revenue	11.4	11.7	11.6	11.4	11.7	12.1	12.2	12.3	12.4
Nontax revenue	2.8	2.0	2.3	1.8	1.2	1.2	1.2	1.2	1.2
External grants	3.3	3.3	1.7	2.0	1.6	1.6	1.4	1.3	1.2
Expenditure and net lending	18.8	18.5	16.9	18.0	17.5	17.6	17.4	17.2	17.2
Fiscal balance, excluding grants (cash basis)	-4.6	-4.9	-2.9	-4.8	-4.6	-4.3	-4.0	-3.7	-3.6
Fiscal balance, including grants (cash basis)	-1.3	-1.6	-1.2	-2.8	-3.1	-2.7	-2.6	-2.4	-2.4
Total financing (including residuals)	1.3	1.6	1.2	2.8	3.1	2.7	2.6	2.4	2.4
External financing	1.1	1.5	0.9	1.3	3.1	2.7	2.6	2.4	2.4
Domestic financing (not including privatization)	0.5	0.0	0.5	1.5	1.6	1.4	1.4	1.3	1.4
<b>Public debt<sup>3</sup></b>	39.4	37.8	32.8	38.6	41.7	43.7	46.3	48.0	49.0
Domestic debt	21.1	15.6	14.9	19.7	21.0	22.3	23.8	25.1	26.2
External debt (including to the IMF)	18.3	22.2	17.9	18.9	20.7	21.4	22.5	22.9	22.9
Overall balance of payments (in millions of U.S. dollars)	685	1446	-1067	189	500	321	350	356	356
Gross official reserves (in millions of U.S. dollars)	1,979	3,044	2,262	2,218	2,518	2,818	3,118	3,418	3,718
(months of imports of goods and nonfactor services of following year)	2.4	2.7	1.9	1.8	1.8	1.9	1.9	2.0	2.0
<b>GDP at current market prices (billions of birr)</b>	379.2	506.1	736.6	877.5	1,008.6	1,180.8	1,364.8	1,575.7	1,823.2

Sources: Ethiopian authorities and IMF staff estimates and projections.

<sup>1</sup> Data pertain to Ethiopian fiscal year from July 8 to July 7.<sup>2</sup> Historical GDP statistics are official data and are subject to significant weaknesses. Applying plausible factor productivities would suggest that the annual GDP growth rate could be off by as much as 3 percentage points in recent years.<sup>3</sup> Including debt of major public enterprises.

**Table 3a. Ethiopia: General Government Operations, 2009/10–2017/18**

	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18
	Act.	Act.	Act.	Est.	Proj.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	66,237	85,611	115,659	133,296	145,612	175,539	202,286	233,683	269,690
Revenue	53,861	69,120	102,864	115,808	129,804	156,603	182,804	212,798	247,757
Tax revenue	43,315	58,981	85,740	99,838	118,092	142,892	166,956	194,501	226,586
Direct taxes	14,903	19,550	28,858	34,653	40,592	48,905	57,289	67,026	78,609
Indirect taxes	28,412	39,431	56,882	65,186	77,500	93,988	109,668	127,476	147,978
Domestic indirect taxes	10,727	15,705	23,326	27,964	33,396	40,805	47,801	55,925	65,589
Import duties and taxes	17,685	23,726	33,556	37,220	44,103	53,182	61,866	71,549	82,387
Nontax revenue	10,546	10,139	17,124	15,970	11,712	13,711	15,848	18,297	21,171
Grants	12,376	16,491	12,795	17,488	15,808	18,936	19,482	20,885	21,934
Emergency assistance (food and nonfood aid)	631	338	0	0	0	0	0	0	0
Program grants <sup>1</sup>	6,816	9,633	4,706	4,608	4,022	4,708	5,442	6,283	7,270
Project grants	4,930	6,521	8,089	12,880	11,786	14,228	14,040	14,602	14,664
Total expenditure and net lending (cash basis) <sup>2</sup>	71,335	93,831	124,417	157,987	176,511	207,714	237,252	270,908	313,230
Recurrent expenditure <sup>2</sup>	32,012	40,535	51,445	60,555	70,251	82,971	95,636	110,335	127,789
Defense spending	4,000	4,750	6,486	6,500	7,500	8,500	8,500	8,500	8,500
Poverty-reducing expenditure <sup>3</sup>	14,750	18,995	24,994	29,775	34,224	40,064	46,308	53,463	61,862
Interest payments	1,587	1,913	2,230	3,153	4,242	5,978	7,969	10,435	13,531
Domestic interest and charges	1,220	1,300	1,388	1,784	2,589	4,064	5,941	8,296	11,320
External interest payments <sup>4</sup>	368	613	842	1,369	1,653	1,915	2,028	2,139	2,210
Emergency assistance (food and other emergency aid)	631	338	0	0	0	0	0	0	0
Other recurrent expenditure	11,044	14,539	17,735	21,128	24,285	28,429	32,860	37,937	43,897
Capital expenditure	39,322	53,297	72,971	97,432	106,261	124,743	141,615	160,573	185,441
Central treasury	29,947	38,340	57,439	76,578	83,438	99,405	116,293	134,504	159,131
External project grants	4,930	6,521	8,089	12,880	11,786	14,228	14,040	14,602	14,664
External project loans	4,446	8,436	7,443	7,973	11,037	11,110	11,282	11,467	11,646
Of which: poverty-reducing expenditure <sup>3</sup>	32,704	43,383	62,574	74,651	86,079	100,689	117,289	136,021	157,746
Overall balance									
Including grants	-5,097	-8,220	-8,758	-24,690	-30,899	-32,175	-34,965	-37,225	-43,540
Excluding grants	-17,473	-24,712	-21,553	-42,178	-46,707	-51,111	-54,447	-58,110	-65,474
Financing	6,586	9,506	13,087	24,690	46,934	48,805	53,761	57,656	69,723
Net external financing	4,131	7,798	6,530	11,682	30,899	32,175	34,965	37,225	43,540
Gross borrowing	4,446	8,436	7,443	13,011	16,479	16,820	17,882	19,086	20,462
Project loans	4,446	8,436	7,443	7,973	11,037	11,110	11,282	11,467	11,646
Protection of Basic Services (PBS)	0	0	0	5,037	5,442	5,710	6,599	7,619	8,816
Amortization <sup>4</sup>	-315	-638	-1,063	-1,329	-1,614	-1,275	-1,712	-2,292	-3,106
Total net domestic financing	1,758	251	3,793	13,008	16,034	16,630	18,795	20,431	26,183
Privatization	697	1,458	2,764	0	0	0	0	0	0
<i>Memorandum items:</i>									
Poverty-reducing expenditure	47,453	62,379	87,568	104,425	120,302	140,753	163,597	189,484	219,608
Primary fiscal balance, including grants	-3,510	-6,308	-6,528	-21,538	-26,657	-26,197	-26,996	-26,790	-30,009
Domestic fiscal balance, including grants	-7,099	-8,804	-5,178	-19,956	-22,231	-23,858	-27,097	-29,902	-36,953
Gross domestic government debt	53,009	53,260	57,053	70,061	86,095	102,725	121,521	141,952	168,135

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

<sup>1</sup> Including the disbursements under the PBS operations starting from 2005/06.<sup>2</sup> Excluding special programs (demobilization and reconstruction).<sup>3</sup> Poverty-reducing spending is defined to include total spending on health, education, agriculture, roads, and food security.<sup>4</sup> External interest and amortization are presented after HIPC debt relief from the World Bank and African Development Bank.

**Table 3b. Ethiopia: General Government Operations, 2009/10–2017/18**  
(Percent of GDP)

	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18
	Act.	Act.	Act.	Est.	Proj.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	17.5	16.9	15.7	15.2	14.4	14.9	14.8	14.8	14.8
Revenue	14.2	13.7	14.0	13.2	12.9	13.3	13.4	13.5	13.6
Tax revenue	11.4	11.7	11.6	11.4	11.7	12.1	12.2	12.3	12.4
Direct taxes	3.9	3.9	3.9	3.9	4.0	4.1	4.2	4.3	4.3
Indirect taxes	7.5	7.8	7.7	7.4	7.7	8.0	8.0	8.1	8.1
Domestic indirect taxes	2.8	3.1	3.2	3.2	3.3	3.5	3.5	3.5	3.6
Import duties and taxes	4.7	4.7	4.6	4.2	4.4	4.5	4.5	4.5	4.5
Nontax revenue	2.8	2.0	2.3	1.8	1.2	1.2	1.2	1.2	1.2
Grants	3.3	3.3	1.7	2.0	1.6	1.6	1.4	1.3	1.2
Emergency assistance (food and nonfood aid)	0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Program grants <sup>1</sup>	1.8	1.9	0.6	0.5	0.4	0.4	0.4	0.4	0.4
Project grants	1.3	1.3	1.1	1.5	1.2	1.2	1.0	0.9	0.8
Total expenditure and net lending (cash basis) <sup>2</sup>	18.8	18.5	16.9	18.0	17.5	17.6	17.4	17.2	17.2
Recurrent expenditure <sup>2</sup>	8.4	8.0	7.0	6.9	7.0	7.0	7.0	7.0	7.0
Defense spending	1.1	0.9	0.9	0.7	0.7	0.7	0.6	0.5	0.5
Poverty-reducing expenditure <sup>3</sup>	3.9	3.8	3.4	3.4	3.4	3.4	3.4	3.4	3.4
Interest payments	0.4	0.4	0.3	0.4	0.4	0.5	0.6	0.7	0.7
Domestic interest and charges	0.3	0.3	0.2	0.2	0.3	0.3	0.4	0.5	0.6
External interest payments <sup>4</sup>	0.1	0.1	0.1	0.2	0.2	0.2	0.1	0.1	0.1
Emergency assistance (food and other emergency aid)	0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other recurrent expenditure	2.9	2.9	2.4	2.4	2.4	2.4	2.4	2.4	2.4
Capital expenditure	10.4	10.5	9.9	11.1	10.5	10.6	10.4	10.2	10.2
Central treasury	7.9	7.6	7.8	8.7	8.3	8.4	8.5	8.5	8.7
External project grants	1.3	1.3	1.1	1.5	1.2	1.2	1.0	0.9	0.8
External project loans	1.2	1.7	1.0	0.9	1.1	0.9	0.8	0.7	0.6
Of which: poverty-reducing expenditure <sup>3</sup>	8.6	8.6	8.5	8.5	8.5	8.5	8.6	8.6	8.7
Overall balance									
Including grants	-1.3	-1.6	-1.2	-2.8	-3.1	-2.7	-2.6	-2.4	-2.4
Excluding grants	-4.6	-4.9	-2.9	-4.8	-4.6	-4.3	-4.0	-3.7	-3.6
Financing	1.7	1.9	1.8	2.8	4.7	4.1	3.9	3.7	3.8
Net external financing	1.1	1.5	0.9	1.3	3.1	2.7	2.6	2.4	2.4
Gross borrowing	1.2	1.7	1.0	1.5	1.6	1.4	1.3	1.2	1.1
Project loans	1.2	1.7	1.0	0.9	1.1	0.9	0.8	0.7	0.6
Protection of Basic Services (PBS)	0.0	0.0	0.0	0.6	0.5	0.5	0.5	0.5	0.5
Amortization <sup>4</sup>	-0.1	-0.1	-0.1	-0.2	-0.2	-0.1	-0.1	-0.1	-0.2
Total net domestic financing	0.5	0.0	0.5	1.5	1.6	1.4	1.4	1.3	1.4
Privatization	0.2	0.3	0.4	0.0	0.0	0.0	0.0	0.0	0.0
<i>Memorandum items:</i>									
Poverty-reducing expenditure	12.5	12.3	11.9	11.9	11.9	11.9	12.0	12.0	12.0
Primary fiscal balance, including grants	-0.9	-1.2	-0.9	-2.5	-2.6	-2.2	-2.0	-1.7	-1.6
Domestic fiscal balance, including grants	-1.9	-1.7	-0.7	-2.3	-2.2	-2.0	-2.0	-1.9	-2.0
Gross domestic government debt	14.0	10.5	7.7	8.0	8.5	8.7	8.9	9.0	9.2

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

<sup>1</sup> Including the disbursements under the PBS operations starting from 2005/06.

<sup>2</sup> Excluding special programs (demobilization and reconstruction).

<sup>3</sup> Poverty-reducing spending is defined to include total spending on health, education, agriculture, roads, and food security.

<sup>4</sup> External interest and amortization are presented after HIPC debt relief from the World Bank and African Development Bank.

Table 4. Ethiopia: Monetary Survey and Central Bank Accounts, 2009/10–2017/18<sup>1</sup>

	2009/10	2010/11	2011/12	2012/13		2013/14		2014/15	2015/16	2016/17	2017/18
	Act.	Act.	Act.	Auth.	Est.	Auth.	Proj.	Proj.	Proj.	Proj.	Proj.
(Millions of birr)											
<b>Monetary survey</b>											
Net foreign assets	27,905	58,157	39,788	43,863	43,863	57,793	52,623	59,498	67,521	76,253	85,596
Central bank	15,895	35,637	21,254	21,197	21,197	28,125	27,193	34,068	42,091	50,823	60,166
Commercial banks	12,010	22,520	18,533	22,666	22,666	29,668	25,430	25,430	25,430	25,430	25,430
Net domestic assets	76,212	86,735	149,051	198,850	198,850	254,773	243,458	295,805	357,066	429,006	515,662
Domestic credit	105,407	138,696	189,080	240,994	241,464	301,131	289,816	351,001	422,219	503,056	596,779
Claims on government (net) <sup>2</sup>	34,695	31,655	21,571	27,027	27,527	37,027	38,720	49,919	62,436	75,619	94,510
Claims on nongovernment	70,712	107,041	167,510	213,966	213,936	264,104	251,096	301,082	359,783	427,437	502,269
Public enterprises	31,436	57,613	98,897	...	137,004	...	163,311	201,844	248,392	303,649	365,207
Private sector	39,276	49,428	68,613	...	76,933	...	87,785	99,238	111,391	123,788	137,062
Other items (net)	-29,195	-51,961	-40,030	-42,144	-42,614	-46,358	-46,358	-55,196	-65,152	-74,050	-81,117
Broad money	104,117	144,892	188,838	242,713	242,713	312,566	296,081	355,303	424,587	505,258	601,257
Money	51,985	75,763	94,280	...	118,912	...	141,444	173,210	209,172	251,433	300,306
Currency outside banks	23,950	32,768	38,537	45,432	45,432	53,156	50,834	58,511	65,884	75,438	87,282
Demand deposits	28,034	42,996	55,743	...	73,480	...	90,610	114,699	143,288	175,995	213,023
Quasi money	52,133	69,129	94,558	...	123,801	...	154,637	182,093	215,415	253,825	300,952
Savings deposits	48,196	64,405	82,489	...	115,490	...	144,306	169,590	200,303	235,717	279,299
Time deposits	3,937	4,724	12,070	...	8,311	...	10,332	12,503	15,112	18,108	21,653
<b>Central bank</b>											
Net foreign assets	15,895	35,637	21,254	21,197	21,197	57,793	27,193	34,068	42,091	50,823	60,166
Foreign assets	26,805	51,517	40,101	40,986	40,986	28,125	46,982	53,406	60,280	67,636	75,506
Foreign liabilities	10,910	15,880	18,847	19,790	19,790	48,904	19,790	19,339	18,190	16,813	15,340
Net domestic assets	32,774	32,832	44,718	53,455	53,485	60,421	58,608	66,406	74,058	83,331	95,051
Domestic credit	36,421	48,647	57,846	70,346	70,846	85,346	85,846	100,846	115,346	128,346	140,346
Government (net)	36,421	42,397	45,344	53,844	54,344	62,844	63,344	75,344	87,344	99,344	111,344
Other items (net)	-3,647	-15,815	-13,128	-16,892	-17,362	-24,925	-27,238	-34,440	-41,288	-45,015	-45,295
Base money	48,670	68,469	65,973	74,651	74,681	88,546	85,801	100,474	116,149	134,154	155,217
Currency outside banks	23,950	32,768	38,537	53,894	45,432	63,056	50,834	58,511	65,884	75,438	87,282
Commercial bank reserves	24,719	35,701	27,435	20,757	29,249	25,490	34,967	41,963	50,265	58,716	67,935
Cash in vault	4,977	6,693	7,248	...	7,435	...	8,538	9,827	11,771	13,750	15,909
Reserve deposit	19,742	29,008	20,187	...	21,814	...	26,428	32,136	38,494	44,965	52,025
(Annual percentage change, unless otherwise indicated)											
<b>Monetary survey</b>											
Net foreign assets	40.4	108.4	-31.6	10.2	10.2	31.8	20.0	13.1	13.5	12.9	12.3
Net domestic assets	19.3	13.8	71.8	...	33.4	...	22.4	21.5	20.7	20.1	20.2
Domestic credit	17.7	31.6	36.3	27.5	27.7	25.0	20.0	21.1	20.3	19.1	18.6
Claims on government (net)	4.1	-8.8	-31.9	25	27.6	37	40.7	28.9	25.1	21.1	25.0
Claims on nongovernment	25.7	51.4	56.5	28	27.7	23	17.4	19.9	19.5	18.8	17.5
Public enterprises	22.0	83.3	71.7	...	38.5	...	19.2	23.6	23.1	22.2	20.3
Private sector	28.9	25.8	38.8	...	12.1	...	14.1	13.0	12.2	11.1	10.7
Broad money	24.3	39.2	30.3	28.1	28.5	28.8	22.0	20.0	19.5	19.0	19.0
Money	20.6	45.7	24.4	...	26.1	...	18.9	22.5	20.8	20.2	19.4
Quasi money	28.2	32.6	36.8	...	30.9	...	24.9	17.8	18.3	17.8	18.6
<b>Memorandum items:</b>											
Base money growth	6.5	40.7	-3.6	13	13.2	19	14.9	17.1	15.6	15.5	15.7
Excess reserve deposit (billions of birr)	3,838	7,033	3,722	...	11,234	...	13,450	16,581	19,843	22,759	25,611
Percent of deposits	4.2	6.6	2.3	...	5.3	...	5.2	5.3	5.5	5.3	5.0
Money multiplier (broad money/reserve money)	2.14	2.12	2.86	...	3.25	...	3.45	3.54	3.66	3.77	3.87
Velocity (GDP/broad money)	3.64	3.49	3.90	...	3.62	...	3.41	3.32	3.21	3.12	3.03
Currency-deposit ratio	0.299	0.292	0.256	...	0.230	...	0.207	0.197	0.184	0.176	0.170
Gross official foreign reserves (millions of U.S. dollars)	1,979	3,044	2,262	...	2,218	...	2,518	2,818	3,118	3,418	3,718
Birr per U.S. dollar (end of period)	13.54	16.91	17.77	18.63	...	...	...	...	...	...	...
Nominal GDP (millions of birr)	379,219	506,079	736,612	...	877,512	...	1,008,633	1,180,757	1,364,778	1,575,658	1,823,183

Sources: National Bank of Ethiopia; and IMF staff estimates and projections.

<sup>1</sup> Year ending July 7. Including commercial bank claims and liabilities to Eritrea. The columns for the authorities reflect NBE's estimates and targets for end-June.<sup>2</sup> Claims on the general government by the banking system less deposits of the general government with the banking system.

**Table 5. Ethiopia: Balance of Payments, 2009/10–2017/18<sup>1</sup>**

	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18
	Act.	Act.	Act.	Est.	Proj.	Proj.	Proj.	Proj.	Proj.
	(Millions of U.S. dollars, unless otherwise indicated)								
Current account balance	-1,193	-211	-2,800	-3,037	-2,849	-3,283	-3,426	-3,612	-3,613
(Percent of GDP)	-4.1	-0.7	-6.6	-6.4	-5.7	-6.0	-5.8	-5.6	-5.2
Current account balance, excl. official transfers	-3,099	-2,071	-4,588	-4,519	-4,690	-5,257	-5,572	-5,932	-6,132
(Percent of GDP)	-10.5	-6.6	-10.8	-9.5	-9.3	-9.5	-9.4	-9.2	-8.8
Trade balance	-6,265	-5,506	-7,908	-8,500	-8,899	-9,690	-10,228	-10,660	-10,952
Exports of goods	2,004	2,747	3,153	3,254	3,740	4,306	4,959	5,709	6,601
Imports of goods	-8,269	-8,253	-11,061	-11,754	-12,640	-13,995	-15,187	-16,369	-17,553
Services (net)	513	758	171	581	844	1,009	1,175	1,258	1,348
Exports	2,044	2,586	2,811	2,905	3,340	3,692	4,047	4,331	4,636
Imports	-1,531	-1,828	-2,639	-2,323	-2,497	-2,683	-2,871	-3,073	-3,289
Income (net)	-55	-70	-96	-132	-198	-259	-330	-410	-477
Private transfers (net)	2,708	2,747	3,246	3,532	3,563	3,683	3,811	3,879	3,949
Official transfers (net)	1,906	1,861	1,788	1,481	1,841	1,973	2,145	2,320	2,519
Capital account balance	2,176	2,989	2,243	3,406	3,348	3,604	3,777	3,968	3,969
Foreign direct investment (net)	956	1,243	1,072	1,179	1,399	1,689	2,030	2,379	2,654
Other investment (net) <sup>2</sup>	1,040	1,747	1,171	2,227	1,950	1,915	1,747	1,589	1,315
Official long-term loans	1,044	1,903	1,292	1,704	1,394	1,274	1,189	966	799
Disbursements	1,127	2,073	1,605	2,095	1,807	1,850	1,861	1,740	1,710
Amortization	-83	-170	-313	-390	-413	-576	-672	-774	911
Monetary Authority	180	0	0	0	0	0	0	0	0
Errors and omissions	-298	-1,332	-510	-180	0	0	0	0	0
Overall balance	685	1,446	-1,067	189	500	321	350	356	356
Financing	-685	-1,446	1,067	-189	-500	-321	-350	-356	-356
Central bank (net; increase –)	-323	-1,002	782	43	-300	-321	-350	-356	-356
Reserves (increase –)	-398	-1,065	782	43	-300	-300	-300	-300	-300
Liabilities (increase +)	75	62	0	0	0	-21	-50	-56	-56
Commercial banks (net; increase –)	-361	-444	285	-232	-200	0	0	0	0
	(Annual percentage change, unless otherwise indicated)								
<i>Memorandum items:</i>									
Exports of goods	38.4	37.1	14.8	3.2	14.9	15.1	15.2	15.1	15.6
Export volume index	10.5	8.9	-0.4	14.0	15.3	12.8	16.6	16.6	15.1
Imports of goods	7.0	-0.2	34.0	6.3	7.5	10.7	8.5	7.8	7.2
Import volume index	14.1	-3.8	25.9	6.8	8.9	12.4	9.7	8.3	7.3
Services exports	5.7	26.5	8.7	3.3	15.0	10.5	9.6	7.0	7.0
Services imports	1.1	19.4	44.4	-12.0	7.5	7.5	7.0	7.0	7.0
Exports of goods and services (percent of GDP)	13.8	17.0	14.0	13.0	14.0	14.5	15.1	15.6	16.2
Imports of goods and services (percent of GDP)	-33.3	-32.1	-32.2	-29.7	-30.0	-30.2	-30.3	-30.3	-30.0
Gross official reserves (millions U.S. dollars)	1,979	3,044	2,262	2,218	2,518	2,818	3,118	3,418	3,718
(Months of following year imports of goods and services)	2.4	2.7	1.9	1.8	1.8	1.9	1.9	2.0	2.0
Terms of trade index	38.3	23.5	8.2	-10.3	0.9	3.9	-0.3	-1.0	0.6
GDP (millions of U.S. dollars)	29,396	31,400	42,516	47,335	50,398	55,139	59,563	64,267	69,498

Sources: Ethiopian authorities and IMF staff estimates and projections.

<sup>1</sup> Data pertain to Ethiopian fiscal year from July 8 to July 7.<sup>2</sup> For 2008/09 and 2009/10, other investment (net) includes a correction for the timing difference between entry of ETC imports and corresponding loan disbursements.

**Table 6. Ethiopia: Alternative Scenario: Selected Economic and Financial Indicators, 2009/10–2017/18<sup>1</sup>**

	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18
	Act.	Act.	Act.	Prel.	Proj.	Proj.	Proj.	Proj.	Proj.
(Annual percentage change)									
National income and prices									
GDP at constant prices (at factor cost) <sup>2</sup>	10.6	11.4	8.5	7.0	8.0	8.5	9.0	9.5	9.5
GDP deflator	1.6	20.0	34.2	11.3	7.1	7.3	6.0	5.9	6.1
Consumer prices (period average)	2.8	18.1	34.1	13.5	6.7	6.5	6.0	6.0	6.0
Consumer prices (end period)	7.3	38.1	20.7	7.4	7.0	6.0	6.0	6.0	6.0
External sector									
Exports (U.S. dollars, f.o.b.)	38.4	37.1	14.8	3.2	15.9	17.1	18.7	18.6	18.6
Imports (U.S. dollars, c.i.f.)	7.0	-0.2	34.0	6.3	9.2	11.4	7.0	7.0	7.0
Export volume	10.5	8.9	-0.4	14.0	16.3	14.8	20.1	20.1	18.0
Import volume	14.1	-3.8	25.9	6.8	10.6	13.1	8.2	7.5	7.0
Terms of trade (deterioration –)	38.3	23.5	8.2	-10.3	0.9	3.9	-0.3	-1.0	0.6
Nominal effective exchange rate (end of period)	-13.4	-26.5	2.8	...	...	...	...	...	...
Real effective exchange rate (end of period)	-9.7	-2.3	20.9	...	...	...	...	...	...
(Percent of beginning-period stock of broad money, unless otherwise indicated)									
Money and credit									
Net foreign assets	9.6	29.1	-12.7	2.2	3.2	2.9	5.9	8.2	10.1
Net domestic assets (including other items net)	14.7	10.1	43.0	26.4	19.3	19.6	14.2	11.8	9.4
Claims on the government	1.7	-2.9	-7.0	3.2	4.4	3.3	2.7	2.6	2.5
Claims on public enterprises	6.8	25.1	28.5	20.2	8.5	10.4	12.6	12.7	13.6
Claims on private sector	10.5	9.8	13.2	4.4	8.0	9.8	12.1	15.4	20.9
Broad money	24.3	39.2	30.3	28.5	22.5	22.5	20.1	20.0	19.5
Base money (annual percentage change)	6.5	40.7	-3.6	13.2	15.8	16.6	15.5	15.9	16.2
Velocity (GDP/broad money)	3.64	3.49	3.90	3.62	3.42	3.25	3.13	3.02	2.94
(Percent of GDP, unless otherwise indicated)									
Financial balances									
Gross domestic savings	5.2	12.8	16.5	15.9	15.3	15.4	16.8	17.8	18.6
Public savings	4.5	4.3	5.7	4.9	6.7	7.2	7.5	7.7	7.9
Private savings	0.6	8.5	10.8	11.0	8.6	8.2	9.3	10.1	10.7
Gross domestic investment	23.6	27.2	34.6	32.6	31.5	31.5	31.8	31.8	31.5
Public investment	14.9	19.6	26.5	24.3	18.7	17.3	15.9	15.0	14.6
Private investment	8.7	7.5	8.1	8.3	12.8	14.2	15.9	16.8	16.9
Resource gap	-18.4	-14.4	-18.1	-16.7	-16.2	-16.1	-15.0	-14.0	-12.9
External current account balance, including official transfers	-4.1	-0.7	-6.6	-6.4	-6.0	-6.2	-5.1	-4.1	-3.0
Saving-investment (government)	-4.0	-9.5	-16.8	-16.6	-8.7	-7.0	-5.4	-4.4	-3.8
Gross Fixed Capital Formation	10.9	10.1	9.7	7.7	10.0	10.3	10.5	10.6	10.8
Saving-investment (private)	9.8	17.2	18.4	18.4	15.6	14.8	15.7	16.1	16.4
External current account balance, excluding official transfers	20.3	22.9	18.2	16.1	17.6	18.2	19.1	19.9	20.7
Government finances									
Revenue	14.2	13.7	14.0	13.2	13.9	14.7	15.7	15.9	16.1
Tax revenue	11.4	11.7	11.6	11.4	12.1	12.9	13.9	14.1	14.3
Nontax revenue	2.8	2.0	2.3	1.8	1.8	1.8	1.8	1.8	1.8
External grants	3.3	3.3	1.7	2.0	1.6	1.6	1.4	1.3	1.2
Expenditure and net lending	18.8	18.5	16.9	18.0	17.4	17.8	18.7	18.7	19.0
Fiscal balance, excluding grants (cash basis)	-4.6	-4.9	-2.9	-4.8	-3.5	-3.1	-3.0	-2.8	-2.9
Fiscal balance, including grants (cash basis)	-1.3	-1.6	-1.2	-2.8	-1.9	-1.5	-1.6	-1.5	-1.7
Total financing (including residuals)	1.3	1.6	1.2	2.8	1.9	1.5	1.6	1.5	1.7
External financing	1.1	1.5	0.9	1.3	3.0	2.7	2.6	2.3	2.4
Domestic financing (not including privatization)	0.5	0.0	0.5	1.5	1.6	1.4	1.4	1.3	1.4
Public debt <sup>3</sup>	39.4	37.8	32.8	38.6	35.0	36.1	36.4	34.9	33.9
Domestic debt	21.1	15.6	14.9	19.7	14.6	14.8	13.9	12.2	11.3
External debt (including to the IMF)	18.3	22.2	17.9	18.9	20.5	21.3	22.5	22.8	22.6
Overall balance of payments (in millions of U.S. dollars)	685	1446	-1067	-275	448	401	938	1462	2018
Gross official reserves (in millions of U.S. dollars)	1,979	3,044	2,262	2,218	2,466	2,847	3,734	5,140	7,101
(months of imports of goods and nonfactor services of following year)	2.4	2.7	1.9	1.8	1.7	1.9	2.3	3.0	3.6
GDP at current market prices (billions of birr)	379.2	506.1	736.6	877.5	1,016.5	1,185.0	1,369.0	1,587.1	1,844.3

Sources: Ethiopian authorities and IMF staff estimates and projections.

<sup>1</sup> Data pertain to Ethiopian fiscal year from July 8 to July 7.<sup>2</sup> GDP statistics in Ethiopia are subject to significant weaknesses. Applying plausible factor productivities would suggest that the annual GDP growth rate could be off by as much as 3 percentage points in recent years.<sup>3</sup> Including debt of major public enterprises.

**Table 7. Ethiopia: Millennium Development Goals**

	1990	1995	2000	2005	2006	2007	2008	2010	2011
<b>Goal 1: Eradicate extreme poverty and hunger</b>									
Employment to population ratio, 15+, total (%)	76	75	75	80	80	80	80	80	79
Employment to population ratio, ages 15-24, total (%)	70	70	70	73	73	73	72	71	71
GDP per person employed (constant 1990 PPP \$)	1,303	1,189	1,296	1,441	1,557	1,688	1,818	2,001	2,087
Income share held by lowest 20%	...	7	9	9	...	...	...	...	8
Malnutrition prevalence, weight for age (% of children under 5)	...	...	42	35	...	...	...	...	29
Poverty gap at \$1.25 a day (PPP) (%)	...	21	16	10	...	...	...	...	8
Poverty headcount ratio at \$1.25 a day (PPP) (% of population)	...	61	56	39	...	...	...	...	31
Vulnerable employment, total (% of total employment)	...	91	91	91	52	...	...	...	...
<b>Goal 2: Achieve universal primary education</b>									
Literacy rate, youth female (% of females ages 15-24)	...	28	...	39	...	47	...	...	...
Literacy rate, youth male (% of males ages 15-24)	...	39	...	61	58	63	...	...	...
Persistence to last grade of primary, total (% of cohort)	...	...	61	61	58	40	38	41	...
Primary completion rate, total (% of relevant age group)	23	15	23	43	47	48	52	62	58
Total enrollment, primary (% net)	36.6	30.9	55	81	87	95	102	102	106
<b>Goal 3: Promote gender equality and empower women</b>									
Proportion of seats held by women in national parliaments (%)	...	2	2	21	22	22	22	28	28
Ratio of female to male tertiary enrollment (%)	22	25	28	32	32	35	44	43	43
Ratio of female to male primary enrollment (%)	65	59	65	83	86	88	89	91	91
Ratio of female to male secondary enrollment (%)	75	79	66	60	63	67	72	82	87
Share of women employed in the nonagricultural sector (% of total nonagricultural employment)	...	...	41	44	47	...	...	42	...
<b>Goal 4: Reduce child mortality</b>									
Immunization, measles (% of children ages 12-23 months)	38	38	33	38	41	42	50	56	57
Mortality rate, infant (per 1,000 live births)	111	98	87	77	65	62	59	54	52
Mortality rate, under-5 (per 1,000)	184	161	141	122	101	96	90	82	77
<b>Goal 5: Improve maternal health</b>									
Adolescent fertility rate (births per 1,000 women ages 15-19)	...	112	103	82	77	72	68	58	53
Births attended by skilled health staff (% of total)	...	...	6	6	...	...	...	...	10
Contraceptive prevalence (% of women ages 15-49)	5	3	8	15	...	...	...	...	29
Maternal mortality ratio (modeled estimate, per 100,000 live births)	950	880	700	510	...	...	470	350	...
Pregnant women receiving prenatal care (%)	...	...	27	28	...	...	...	...	43
Unmet need for contraception (% of married women ages 15-49)	...	...	35	34	...	...	...	...	26
<b>Goal 6: Combat HIV/AIDS, malaria, and other diseases</b>									
Children with fever receiving antimalarial drugs (% of children under age 5 with fever)	...	...	3	3	...	10	...	...	...
Condom use, population ages 15-24, female (% of females ages 15-24)	...	...	2	2	...	...	...	...	3
Condom use, population ages 15-24, male (% of males ages 15-24)	...	...	20	18	...	...	...	...	25
Incidence of tuberculosis (per 100,000 people)	173	182	235	276	324	308	293	269	258
Prevalence of HIV, female (% ages 15-24)	...	...	...	...	...	2	...	...	0
Prevalence of HIV, male (% ages 15-24)	...	...	...	...	...	1	...	...	0
Prevalence of HIV, total (% of population ages 15-49)	...	...	...	...	...	2	...	...	1
Tuberculosis case detection rate (all forms)	110	25	59	61	50	54	61	69	72
<b>Goal 7: Ensure environmental sustainability</b>									
CO2 emissions (kg per PPP \$ of GDP)	0	0	0	0	0	0	...	...	...
CO2 emissions (metric tons per capita)	0	0	0	0	0	0	...	...	...
Forest area (% of land area)	14	...	14	13	13	13	...	12	...
Improved sanitation facilities (% of population with access)	3	4	9	14	16	17	18	21	...
Improved water source (% of population with access)	14	20	29	37	39	41	42	44	...
Marine protected areas (% of total surface area)	...	...	...	...	...	...	...	...	...
<b>Goal 8: Develop a global partnership for development</b>									
Net ODA received per capita (current US\$)	21	15	10	26	27	33	42	42	42
Internet users (per 100 people)	0	0	0	0	0	0	0	1	1
Mobile cellular subscriptions (per 100 people)	0	0	0	1	1	2	2	8	17
Telephone lines (per 100 people)	0	0	0	1	1	1	1	1	1
<b>Other</b>									
Fertility rate, total (births per woman)	7	7	6	6	5	5	5	4	4
GNI per capita, Atlas method (current US\$)	250	150	130	160	190	230	280	360	370
GNI, Atlas method (current US\$) (billions)	12	8	8	12	14	18	22	30	31
Gross capital formation (% of GDP)	13	18	20	23	24	23	20	25	26
Life expectancy at birth, total (years)	47	49	52	55	56	57	57	59	59
Literacy rate, adult total (% of people ages 15 and above)	...	27	...	36	...	...	36	30	...
Population, total (millions)	48	57	66	75	77	79	81	83	85
Trade (% of GDP)	14	25	36	51	50	45	42	47	49

Source: 2013 World Development Indicators database

**Table 8. Ethiopia: Financial Soundness Indicators of the Commercial Banking Sector, 2008–12**  
(In percent, unless otherwise indicated)

	Jun-08	Jun-09	Jun-10	Jun-11	Jun-12	Mar-13
<b>Capital adequacy</b>						
Regulatory capital to risk-weighted assets	18.9	18.7	18.7	18.1	13.4	14.6
Regulatory Tier I capital to risk-weighted assets	18.9	18.7	18.7	18.1	13.4	14.6
Capital (net worth) to assets	10.1	9.6	9.1	7.8	6.7	6.6
<b>Asset quality and composition</b>						
NPLs to gross loans	6.8	6.0	3.5	2.1	1.4	2.4
NPLs net of provision to capital	5.6	7.3	0.7	-3.8	-5.6	1.5
Spread between highest and lowest interbank rate	...	...	...	...	...	...
<b>Earning and profitability <sup>1</sup></b>						
ROA	2.9	3.2	4.0	3.0	4.1	3.1
ROE (total capital) <sup>2</sup>	27.7	31.5	42.2	31.5	34.2	46.7
ROE (core capital) <sup>3</sup>	29.8	34.0	46.4	34.9	55.8	...
Gross interest income to total income <sup>4</sup>	54.9	57.1	60.1	54.4	54.7	...
Interest margin to gross income <sup>5</sup>	46.1	50.6	38.7	40.0	45.0	...
Noninterest expenses to gross income	36.6	27.8	28.0	28.7	26.6	...
Personnel expenses to noninterest expenses	40.6	50.5	46.0	51.1	42.3	...
Trading and fee income to gross income	53.9	49.4	61.3	52.0	55.0	...
Spread between reference loan and deposit rates	7.0	7.4	6.4	6.4	6.4	...
<b>Liquidity</b>						
Liquid assets to total assets	31.5	30.8	32.7	32.7	20.6	19.7
Liquid assets to short term liabilities	41.9	40.4	42.7	43.4	26.7	25.4
Total (non-interbank) loans to customer deposit <sup>6</sup>	87.2	82.0	80.1	81.9	94.0	96.7
FX liabilities to total liabilities						

Source: Ethiopian authorities.

1/ Earning ratios indicated for March 2013 is provisional.

2/ The average capital used to calculate the ROE includes retained earnings, profits and loss.

3/ The average capital used to calculate the ROE excludes retained earnings, profits and loss.

4/ Total income comprises gross interest income and gross non-interest income.

5/ Gross income comprises net interest income and total non-interest income.

6/ Customer deposit includes time, current and saving deposits and total loans include bonds.



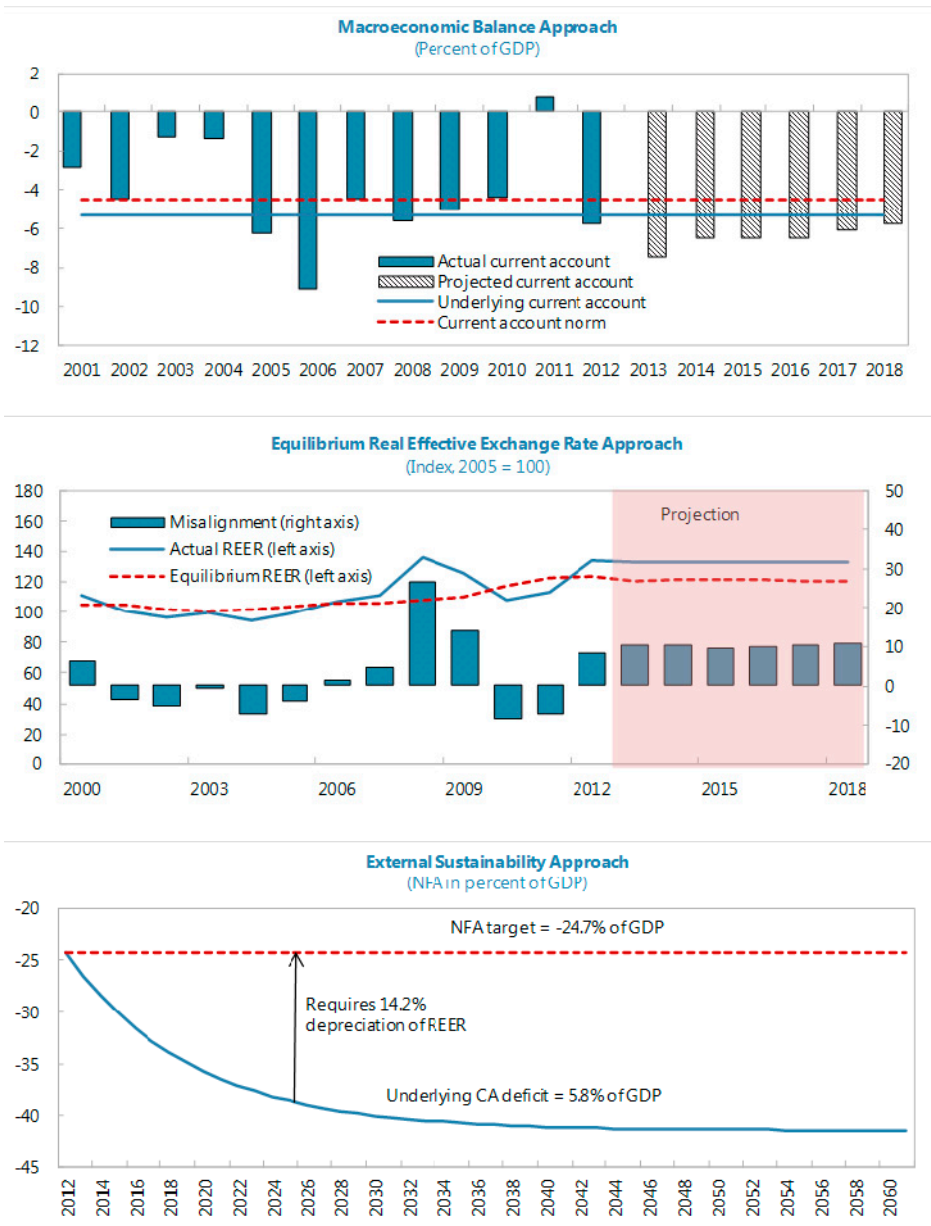
## Annex I. National Accounts Statistics Issues

- 1. Ethiopia's official national account statistics suffer from significant weaknesses. An IMF Statistics Department (STA) mission in March 2010 identified major compilation and estimation deficiencies and suggested corrective actions.** The authorities developed a national accounts improvement and capacity building action plan which they have been implementing.
- 2. During the 2012 Article IV consultation, it was agreed that completion of a new benchmark GDP for 2010/11 and implementation of the improved methodologies being supported by East AFRITAC (AFE) would help improve official statistics.** Since then, with the help of AFE, the authorities have made methodological improvements and published the 2011/12 national accounts based on the new benchmark which show a real GDP growth rate of 8½ percent, significantly lower than in recent years, reflecting in part lower growth in agricultural output.
- 3. The authorities need to continue to improve national account statistics and related capacity.** In consultation with STA, the mission decided to use the official historical figures with a notation regarding data weaknesses and possible overestimation of GDP growth rates. This approach is consistent with the general practice of reporting official historical data in other countries with national account data deficiencies. Staff will continue to have its own projections, but at the end of the fiscal year will adopt official statistics based on the national accounts outturns with the appropriate caveat. Authorities expressed their disagreement about putting a caveat on their statistics. Staff stressed the need to continue to improve national accounts data and the readiness of the Fund to offer further technical assistance.

## Annex II. Exchange Rate Assessment

1. **The assessment of the exchange rate in Ethiopia for the fiscal year 2012/13, based on the IMF's CGER methodology, suggested an overvaluation of the real effective exchange rate in the range of 10 to 14 percent, depending on the method applied.** The estimated misalignment has slightly narrowed since the 2012 Article IV consultation. The standard CGER methods are (i) the macroeconomic balance approach, (ii) the equilibrium REER approach, and (iii) the external sustainability approach.
2. **The macroeconomic balance approach indicates an overvaluation of 10 percent, because a REER depreciation of that proportion would align the current account with its equilibrium level.** The current account is expected to sustain a large but reducing deficit in the medium term. With an estimated current account deficit of 6.4 percent of GDP in 2012/13, the deficit is expected to shrink to 5.2 percent of GDP in the next five years. The norm current account balance is also negative (4.5 percent), supported in part by the large inflow of remittances and international development aid that is expected to continue in the medium term. Large level of imports is forecasted in the medium term, mostly on petroleum products and heavy construction equipment. A 10 percent depreciation of the REER is necessary to close the current account gap.
3. **The equilibrium real exchange rate approach shows an overvaluation of about 10 percent from the equilibrium REER derived from the medium-term macroeconomic fundamentals.** This result is predicated on highly volatile terms of trade, a stable level of remittances, and government expenditure partially financed by large external transfers.
4. **The external sustainability approach suggests an overvaluation of the REER of about 14 percent.** This approach calculates the current account balance that stabilizes the net foreign asset (NFA) position at a sustainable level. Nominal GDP growth is estimated at 14.9 percent, and the underlying current account deficit of 5.8 would result in a long-run NFA position of -41.6 percent of GDP. To sustain the NFA position at -24 percent (average of last five years), the current account deficit should be 3.1 percent of GDP, implying a depreciation of 13 percent in the REER.

**Figure II.1. Ethiopia: Exchange Rate Assessment**



Sources: Ethiopian authorities; and IMF staff calculations.

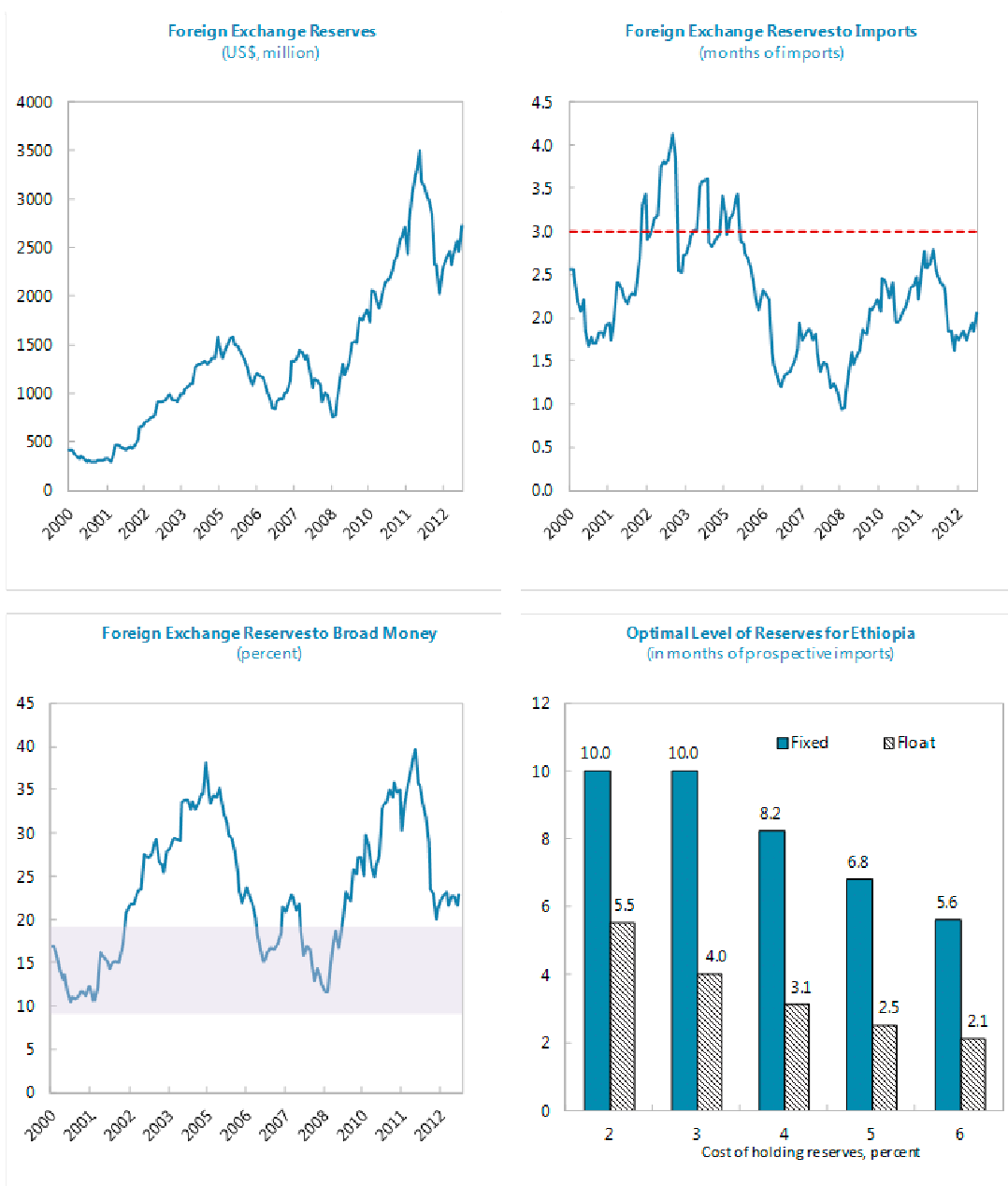
## Annex III. Reserve Adequacy Assessment

1. **Ethiopia is a low-income country with an agricultural commodity export oriented sector and a high dependency on imported fuel and capital goods.** The economy is exposed to potential terms-of-trade shocks and has a limited capacity to absorb them, given chronically low reserve coverage.
2. **In addition, Ethiopia receives a large volume of private transfers from Ethiopians leaving abroad.** These remittances averaged about US\$3 billion in the last three years, an amount close to the value of total exports during the same period. The large trade deficit is also partially offset with important official transfers that reached US\$1.7 billion in 2011/12.
3. **From September 2011 to May 2012, international reserves contracted by more than US\$1.5 billion as the government sold reserves in an attempt to control domestic liquidity.** Since then, reserves appear to be growing again.
4. **The reserve coverage has remained low in months of imports.** By June 2013 reserves could sustain only about two months of prospective imports. Given the relatively high level of imports expected in the coming years, further accumulation of reserves is needed to improve the coverage and have some buffer to respond to possible deterioration of the terms of trade.
5. **Reserves have stabilized in percent of broad money just above the 20 percent threshold.** Although there are no large capital flows in Ethiopia, low reserves in the context of a pegged exchange rate could add to the evidence of an inadequate reserves level.
6. **Reserve adequacy assessment based on Dabla-Norris and others (2011)<sup>1</sup> shows that for a country with a fixed exchange rate regime and assuming the cost of holding foreign reserves is set at 5 percent (mid-point in the range of the marginal product of capital in low-income countries), the optimal reserve coverage would be the equivalent of 6.8 months of imports.** The model evaluates various shocks in external demand, terms of trade, FDI, and aid flows for different cost levels of holding reserves. Remittances are not explicitly included in the calculation of the cost-benefit analysis, but a large and sustained inflow of foreign resources to Ethiopian households could imply lower reserve coverage for a given cost of holding those reserves.

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<sup>1</sup> Based on Dabla-Norris, Kim, and Shirono, 2011, "Optimal Precautionary Reserves for Low-Income Countries: A Cost-Benefit Analysis," IMF Working Paper 11/249.

**Figure III.1. Ethiopia: Reserves**



Sources: Ethiopian authorities; and IMF staff calculations.



# THE FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA

## STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION—DEBT SUSTAINABILITY ANALYSIS

August 29, 2013

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Prepared by the International Monetary Fund and the  
International Development Association

*Based on the Low-Income Country debt Sustainability Analysis (LIC DSA) framework, the updated DSA found that Ethiopia's risk of external debt distress remains low. The public DSA suggests Ethiopia's overall public sector debt dynamics are sustainable under the baseline scenario but vulnerable under several alternative scenarios. Public sector debt ratios are projected to decline in the medium and long term, starting from a relatively low level in 2013. An alternative scenario with a government primary deficit fixed at the 2012 level would have a detrimental impact on debt-to-GDP and debt-to-revenue ratios, suggesting that the government must develop a strategy to contain the primary deficit as it's already assumed in the baseline. Maintaining the growth of exports through diversification of the export sector, developing a medium-term debt strategy for the public sector, and limiting non-concessional borrowing remain crucial to maintaining a low risk of external debt distress.*

## BACKGROUND AND KEY FINDINGS

**1. The last Debt Sustainability Analysis (DSA), prepared in August 2012, concluded that Ethiopia was at a low risk of external debt distress.** Ethiopia reached the completion point under the Heavily Indebted Poor Countries (HIPC) Initiative in 2004 and benefited from debt relief under the Multilateral Debt Relief Initiative (MDRI) in 2006<sup>1</sup>. In 2011/12<sup>2</sup>, public and publicly guaranteed (PPG) external debt declined to 18.4 percent of GDP, more than 5 percentage points relative to the previous year.<sup>3</sup> High GDP growth and negative domestic real interest rates on public debt contributed to the decline.

**2. The previous DSA findings were robust to the inclusion of remittances and higher non-concessional loans as part of the assessment.** Last year's external DSA did not result in any breach of indicative thresholds with or without remittances and debt-to-exports ratios were about 20 percentage points better in the baseline with those private transfers. The assessment was made not taking into account remittances as recommended in the LIC DSA framework, with strong evidence of low external debt distress risks. An alternative scenario stretching the non-concessional borrowing capacity up to US\$1 billion a year confirmed the capacity of the country to absorb those resources with no harm to the external DSA.

**3. Ethiopia remains at low risk of external debt distress in 2013. The present value (PV) of PPG external debt is expected to increase slightly from 13.2 percent of GDP in 2011/12 to 14.4 percent of GDP in 2012/13.** The ratio of PV of PPG external debt to exports would go from 94.3 percent to 110.6 percent in the same period, as a result of the rapid buildup of external debt and low exports growth. The inclusion of workers' remittances significantly lowers the baseline average of the debt-to-exports ratios in the projection period (2012/13–2032/33) by 16 percentage points.<sup>4</sup> There is no breach of any indicative threshold in either case, excluding or including workers' remittances.

**4. The current DSA assumes a decline in the share of concessional loans, particularly from International Development Association (IDA), and higher nonconcessional external loan**

<sup>1</sup> While Ethiopia has received debt relief from most of its creditors, it has not been able to reach agreement with bilateral official creditors from Bulgaria, Libya, and FR Yugoslavia and commercial creditors from Italy, former Czechoslovakia, and FR Yugoslavia whose outstanding loans (US\$378.8 million) accounted for 7.0 percent of the debt stock in 2009/10. HIPC terms are assumed for these loans. Negotiations with Russia on outstanding loans (US\$161.6 million) are at an advanced stage, and debt service on these loans is excluded from this DSA.

<sup>2</sup> The Ethiopian fiscal year runs from July 8 to July 7.

<sup>3</sup> PPG debt includes not only federal and regional governments' debt, but also encompasses all major state-owned enterprises, except Ethiopian Airlines (EAL). EAL debt is excluded from PPG debt, because, although owned by the government, it is run on commercial terms. EAL enjoys managerial independence, borrows without any government guarantees, publishes annual audited reports and has a sizeable profit margin.

<sup>4</sup> Based on the 2012 Country Policy and Institutional Assessment (CPIA) score, Ethiopia is classified as a medium performer. The thresholds for the debt burden for medium performers are 150, 40, and 250 for the PV of debt to exports, GDP, and revenue, respectively; debt service thresholds are 20 and 30 percent of exports and revenue, respectively. In the scenarios that include workers' remittances, the corresponding threshold for PV of debt to exports and remittances is 120 percent (compared to 135 in the 2011 DSA) and is 16 percent for debt service to exports and remittances; the PV of debt to GDP and remittances is 36 percent.

**disbursements between 2013/14 and 2019/20.** An increase in projected commercial loan disbursements to finance large acquisitions of capital goods by state-owned enterprises is the largest contributor to the buildup of new debt in the medium term. New commercial loans will contribute to subsequent increases in the various debt ratios and a decline in the grant element on new borrowing throughout the projection periods. This DSA assumes disbursements just below US\$1 billion in nonconcessional loans a year in the next four years, with Ethiotel (the telecommunications company) taking US\$1 billion over four years. The DSA assumes that nonconcessional loan disbursements will remain at around US\$730 million on average over the projection period (2018–33). Over the time horizon of the DSA, 53 percent of new external loans are assumed to be concessional on average. Average maturity on all new external loans is assumed to be 26 years while new non-concessional loans are assumed to carry a maturity of 11–12 years. Average interest rates on new external loans are assumed at 2.3 percent over the horizon, and interest rates on new non-concessional loans are assumed to be in the 2–4 percent range.

**Text Table 1. Ethiopia: Comparison of PPG External Debt.  
Baseline Scenario**

	2012/13	2013/14	2014/15	2015/16	2016/17	2021/22	2031/32
	(Percent, unless otherwise indicated)						
	PV of Debt to Exports Ratio						
2013DSA	110.6	116.3	120.1	122.1	122.2	102.7	56.1
2012DSA	98.7	102.1	103.4	106.1	...	97.6	58.5
	PV of Debt to GDP Ratio						
2013DSA	14.4	16.3	17.4	18.5	19.1	17.7	10.5
2012DSA	14.3	15.4	16.0	17.1	...	16.2	9.7
	PV of Debt to Revenue Ratio						
2013DSA	100.7	127.3	131.0	139.7	144.6	132.8	77.9
2012DSA	111.2	119.2	123.1	129.5	...	118.5	74.4
	Debt Service to Exports Ratio						
2013DSA	5.8	6.4	7.2	7.1	7.4	8.5	4.9
2012DSA	5.7	6.4	7.3	7.3	...	8.3	5.4
<i>Memorandum items:</i>							
	Grant Element of New External Borrowing						
2013DSA	30.8	24.8	25.3	24.8	25.7	28.2	27.6
2012DSA	30.1	25.6	23.8	17.7	...	25.5	21.9
	New Commercial Loan Disbursements (billions of U.S. dollars)						
2013DSA	0.511	0.997	0.985	0.996	0.932	0.750	0.755
2012DSA	0.424	0.538	0.606	0.968	...	0.571	0.718
	Real GDP Growth (annual percent change)						
2013DSA	7.0	7.5	7.5	7.0	7.0	6.5	6.5
2012DSA	6.5	6.5	6.5	6.5	6.5	6.5	6.5
	Current Account Balance to GDP Ratio						
2013DSA	-6.4	-5.7	-6.0	-5.8	-5.6	-5.1	-4.2
2012DSA	-7.5	-6.2	-6.2	-6.3	...	-5.6	-5.2

Sources: Ethiopian authorities; IMF and World Bank staff estimates and projections.



**5. In April 2013, IDA authorized a US\$1 billion ceiling for Ethiopia for FY13 and, in principle, a similar ceiling for FY14 and FY15.** This implies that Ethiopia can borrow up to US\$1 billion per year from other creditors on non-concessional or commercial terms as long as these loans finance projects that are growth enhancing. According to the IDA Non-concessional Borrowing Policy, a loan counts at the point of signing the loan contract (regardless of the disbursement profile). The decision was informed by the 2012 DSA analysis, which demonstrates that such a ceiling is consistent with the maintenance of low risk of external debt distress. The 2013 DSA is consistent with the new ceiling.<sup>5</sup>

**6. Some of the large public investment projects by state-owned enterprises could pose risks to Ethiopia's public debt sustainability.** The state-owned power company, the Ethiopia Electricity Power Company, is undertaking several large investment projects. Most rely on external assistance and loans (including both concessional and nonconcessional) while the Renaissance Dam project, estimated by the authorities to cost 10 percent of 2012/13 GDP, is intended to be financed entirely domestically. The Ethiopian Railway Corporation recently signed contracts with Chinese and Turkish companies for projects whose total size is more than US\$3 billion, or 6 percent of 2012/13 GDP. The telecommunications company signed two agreements with Chinese providers for a total of US\$1 billion in equipment. It would be prudent for the authorities to formulate a medium-term debt management strategy and to start monitoring the overall debt (including external and domestic) of the consolidated public sector.

**7. Authorities requested the exclusion of the commercial external loans in the telecom sector from the DSA.** Ethiopian authorities agreed with the findings of the updated DSA, but requested the exclusion of the two specific loans that Ethiotel has signed with Chinese equipment suppliers for a total of US\$1 billion. The conditions of those loans are nonconcessional and the authorities explained that there is no government guarantee. The equipment has not been delivered and the process could take several years. Staff proposed to split the disbursements in the next four years to reflect the multiyear nature of the agreement and the time needed to properly commission the equipment. Authorities agreed on the proposed treatment and the inclusion of the loans under those conditions.

## MACROECONOMIC ASSUMPTIONS

**8. The medium-term macroeconomic outlook underlines an upward revision on output growth and slightly lower inflation compared to the assumptions of the 2012 DSA (Box 1).** Real GDP growth is forecasted at 7 percent in 2012/13 and 7.5 percent in the following two years, reflecting strong economic activity mainly led by public infrastructure investment. The projected long-run GDP growth rate is maintained at 6.5 percent.

**9. Export growth is projected to continue but at a slower pace than in the previous DSA, partly reflecting developments in commodity prices.** In the medium- to long-run, export growth would be supported by diversification of the export sector as emerging export industries expand, funded by greater inflows of foreign direct investment, and domestic investments to boost service exports including

<sup>5</sup> Some simulations implying slightly higher external non-concessional borrowing (above the US\$1 billion limit) produce debt trajectories that would lead to a downgrade in Ethiopia's risk of external debt distress.

electricity. Overall, exports of goods and services are projected to grow at 11.2 percent each year from 2013/14 to 2017/18 or 1.2 percentage points below the rate assumed in the 2012 DSA.

## EXTERNAL DEBT SUSTAINABILITY ANALYSIS

**10. Under the baseline scenario (not including remittances), the PPG external debt indicators will rise in the next several years, but will remain well under the relevant indicative thresholds (Figure 1).** The PV of PPG external debt in percent of GDP would slightly increase in 2012/13 to 14.4 percent and is projected to reach 19 percent by 2017/18, reflecting the assumed steady increase in new loan disbursements, and subsequently decline to about 10 percent in the long run. The PV of debt in percent of exports reached 110.6 percent in 2012/13; and despite continued strength in exports, it is projected to continue increasing, peaking at 124 percent in 2015/16. The debt service-to-exports ratio also remains well below the relevant threshold although it keeps rising to a peak of 12.5 percent in 2019/20, reflecting servicing of non-concessional loans by public enterprises.

### Box 1. Ethiopia: Macroeconomic Assumptions for the Baseline Scenario

Based on a domestic financing which is less compared to full financing of the Growth and Transformation Plan (GTP), real GDP growth is projected at 7 percent in 2012/13, 7.5 percent in the following two years, and to slightly tump down to 7 percent until 2017/18 and 6.5 percent during rest of the projection period.<sup>1</sup> This assessment contrasts with the government's growth ambitions in the GTP and reflects the still difficult business environment, given the limited space for private sector growth on account of crowding out by public sector borrowing. Inflation is projected to reach 7.4 percent by the end of 2012/13 and to stay at 8 percent in the long run. The primary balance of the public sector is projected to record a large deficit (averaging 5.7 percent of GDP in 2013–18) initially reflecting investment by public enterprises, and it is expected to remain about 4.2 percent in the long run.

The external current account deficit (before official transfers) is expected to improve slightly to 9.3 percent in 2013/14 after reaching 9.5 percent in 2012/13 and gradually to reduce to about 7 percent in the long-run.

Exports of goods and services are projected to grow by 15 percent in 2013/14, after an increase of 3.3 percent in 2012/13, and with an average growth of about 9.4 percent in the long run. A decline in commodity prices, especially in gold and coffee, largely offset gains in export volumes. Investments in targeted sectors that receive government support are expected to contribute to export growth, with export volume growth projected about 15.4 percent for 2013/14 and about the same growth rate in the next four years to just below 8 percent over the remaining DSA horizon. Imports of goods and services are projected to increase slightly above GDP as demand for imported capital goods is expected to grow fast during the GTP implementation. In the long run, imports are expected to grow in line with domestic output.

Workers' remittances have played a key role in supporting the balance of payments and in 2013/14 are expected to remain at 7 percent of GDP. High growth, economic stability and the return of growth in developed countries is expected to maintain remittances at around 5.7 percent of GDP in the long run.

Foreign direct investment (FDI) is projected at 2.8 percent of GDP in 2013/14 and will increase gradually to a long run yearly average of 4.5 on account of policies to promote greater private investment to sustain high growth.

<sup>1</sup>Domestic financing and prospective external inflows amount roughly to two third of full financing of the GTP.

**11. Under the historical scenario, the debt stock indicators would be lower than under the baseline scenario.** The scenario reflects significantly higher nominal GDP and export growth (than in the baseline) which works to drive the debt ratios down. It also reflects larger net debt creating flows (than in the baseline) which work to drive up the debt ratios. The dynamic path under the historical scenario is determined by these two offsetting forces.

**12. Without remittances, the terms-of-trade shock is the most extreme potential risk for the sustainability of the external debt.** Even under the possibility of a large deterioration in the terms-of-trade, no indicators would breach the indicative thresholds during the period covered by the DSA. The PV of PPG external debt to exports approached the threshold without reaching the 150 mark during 2017/18 through 2020/21, declining to less than 100 by 2032/33.

## PUBLIC DEBT SUSTAINABILITY ANALYSIS

**13. Under the baseline scenario and similar to the findings in the 2012 DSA, the total public sector debt-to-GDP ratio would rise sharply in the near term.** This reflects large domestic borrowing and continued accumulation of external PPG debt by public enterprises to implement infrastructure investment projects contemplated in the GTP. It is expected that after an initial period of high spending, total public sector expenditure would revert to a lower level in the long run.

**14. Debt stock related indicators grow steadily and peak in 2020/21 and debt service related indicators peak one year earlier.** All debt indicators decline gradually from the peak in the baseline scenario; this result depends on continuation of robust GDP growth, moderate public sector primary deficits, and most crucially the authorities' policy of keeping domestic interest rates low. Interest rates are assumed to remain in negative territory in real terms with inflation expected to stay at 8 percent in the long run.

**15. Public sector debt would grow in the long-run as a result of a permanent negative shock on GDP growth, but debt service-to-revenue could absorb this shock (Figure 2).** The scenario with unchanged primary balance from 2012/13 shows particularly sharp deterioration because of the unusually large primary deficit in that particular year, reflecting investment activities by public enterprises. The other two alternative scenarios (real GDP growth and primary balance at the historic average; permanently lower GDP growth) show trajectories with no important changes in the debt ratios during the DSA horizon.

**16. The baseline scenario understates the public debt burden for the economy because it reflects actual costs of borrowing by the public sectors, which are significantly lower than inflation.** Although inflation is projected to remain at a single-digit level, given the current policy of financing public investment at low costs, interest rates on public enterprise domestic borrowing would not be fully adjusted to a positive level in real terms. Ethiopia's relatively benign public sector debt outlook hinges strongly on the continuation of this current policy. If the actual cost of borrowing were to rise above inflation, the debt indicators would worsen or fiscal adjustment could be required to maintain fiscal sustainability.

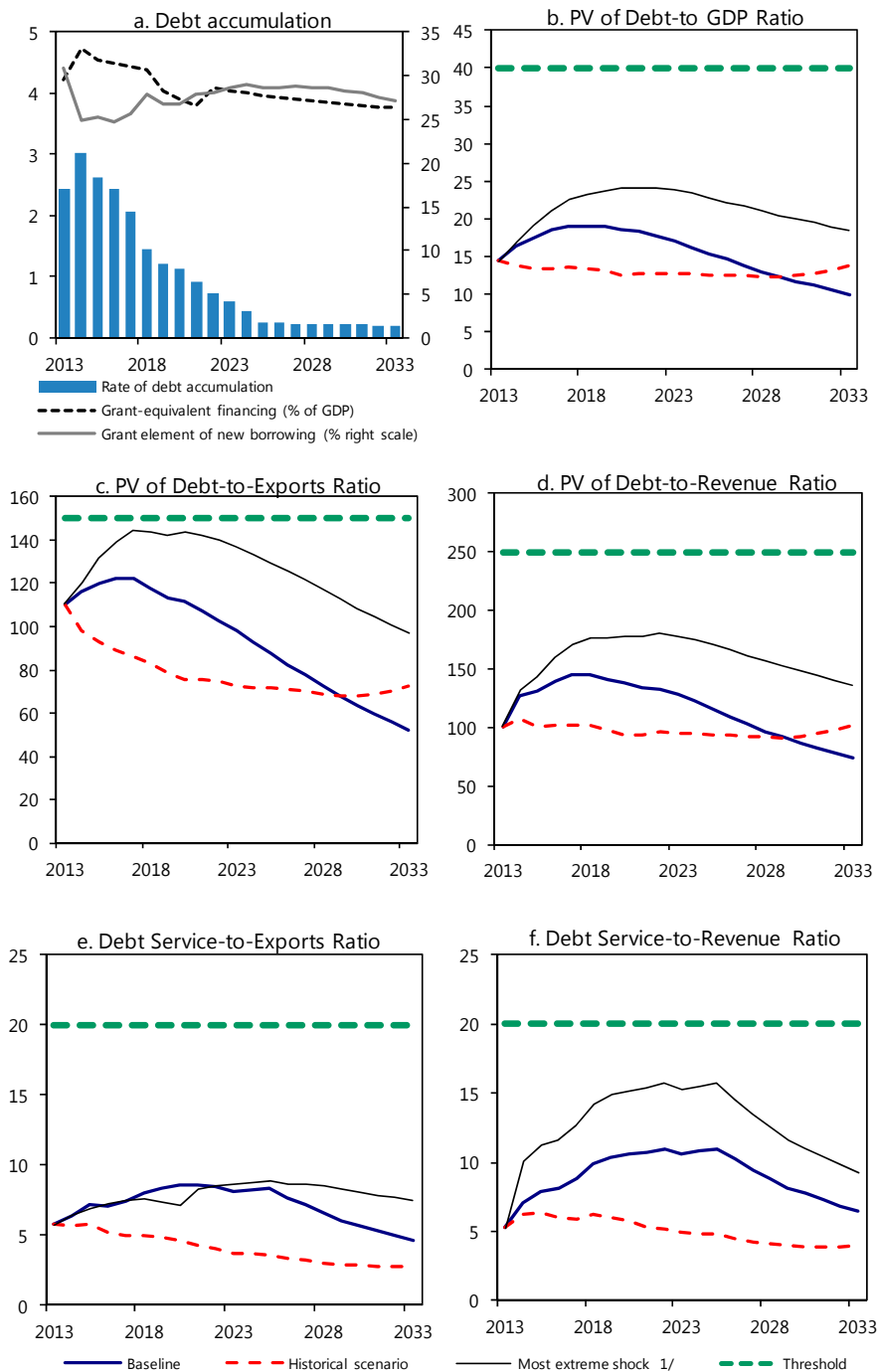
**17. This analysis which maintains a low risk of debt distress assumes disbursements of external borrowing significantly lower than required for the GTP.** The ongoing large public investment projects rely heavily on domestic financing and would lead to a large accumulation of public debt. Absent an appropriate pacing of the public investment projects in the GTP, the domestic financial sector could be squeezed. Monitoring the operations of the consolidated public sector including contingent liabilities arising from financial transactions among public entities is crucial.

## CONCLUSION

**18. The level of Ethiopia's external and public debt distress remains at a low risk rating.** The external debt ratios have risen rapidly in recent years, and this trend is projected to continue in the medium-term. The results suggest the importance for Ethiopia of monitoring debt closely and remaining vigilant regarding new debt accumulation, particularly with commercial loans. The financing plan underlying the GTP needs to take into account these results. Vulnerabilities identified in various sensitivity analyses are relevant for considering policies that would help maintain the low risk rating of external debt distress. Particular emphasis must be made on adequate concessionality of new external loans.

**19. Domestic borrowing by the public sector continues to increase.** The overall debt (including external and domestic) of the consolidated public sector must be monitored carefully. Adjustments to policies to ensure price stability, a competitive exchange rate, and greater private sector involvement in investment and trading activities would go a long way in enhancing Ethiopia's debt sustainability.

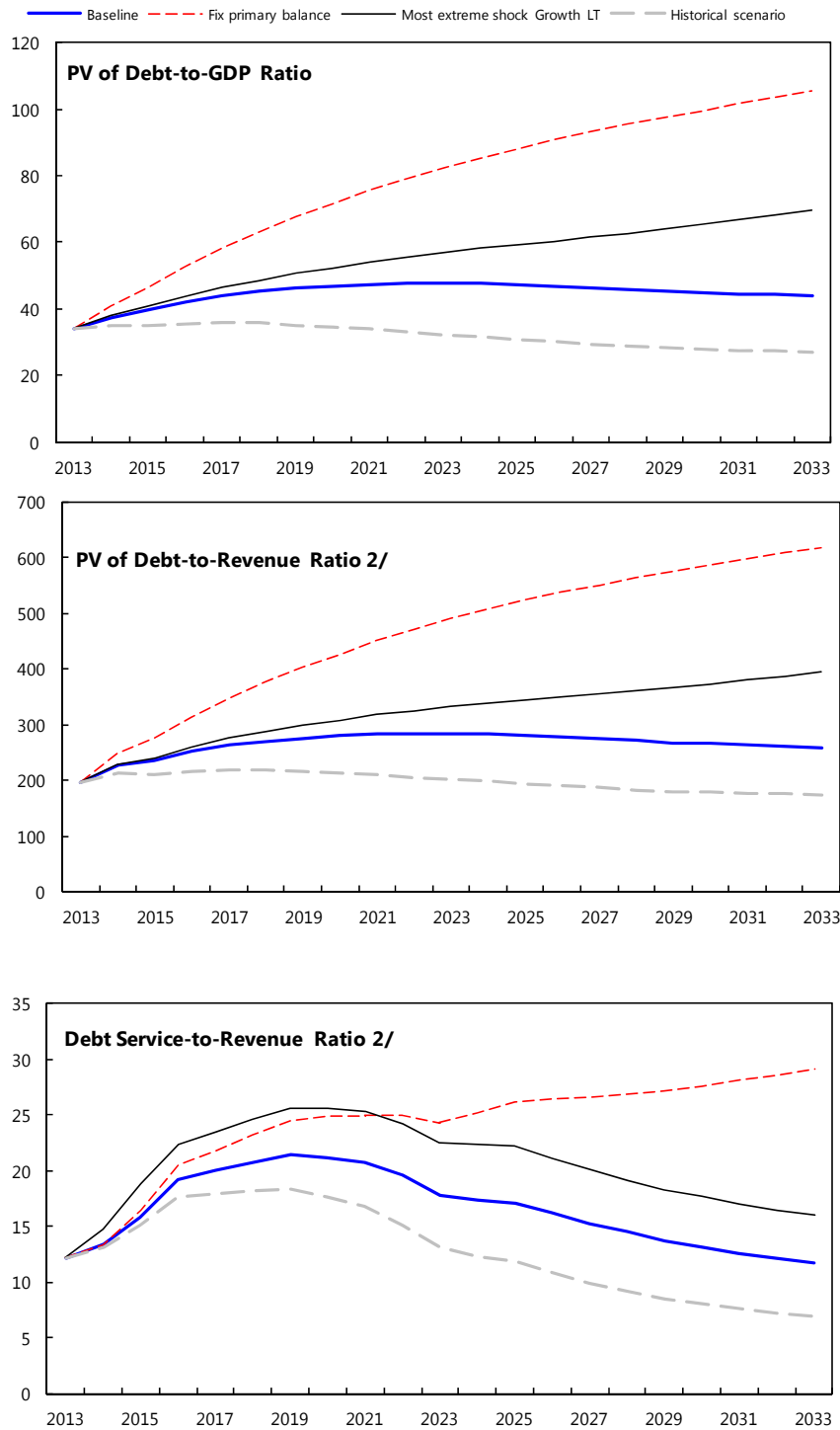
**Figure 1. Ethiopia: Indicators of Public and Publicly Guaranteed External Debt Under Alternatives Scenarios, 2013–33<sup>1</sup>**



Sources: Ethiopian authorities; IMF and World Bank staff estimates and projections.

<sup>1</sup> The most extreme stress test is the test that yields the highest ratio in 2033. In figure b. c. d. and e. it corresponds to a Terms shock; and in figure f. to a one-time depreciation shock.

**Figure 2. Ethiopia: indicators of Public Debt Under Alternative Scenarios, 2013–33<sup>1</sup>**



Sources: Ethiopian authorities; IMF and World Bank staff estimates and projections.

<sup>1</sup> The most extreme stress test is the test that yields the highest ratio in 2023.

<sup>2</sup> Revenue is defined inclusive of grants.

Table 1. Ethiopia: External Debt Sustainability Framework, Baseline Scenario, 2010–33<sup>1</sup>

	Actual											Historical <sup>6/</sup>		Projections						2013–2018			2019–2033			
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	Average	Standard Deviation	2013	2014	2015	2016	2017	2018	Average	2023	2033	Average			
<b>External debt (nominal) 1/</b>	<b>79.6</b>	<b>80.2</b>	<b>72.4</b>	<b>48.6</b>	<b>43.2</b>	<b>13.8</b>	<b>12.9</b>	<b>15.3</b>	<b>20.1</b>	<b>26.0</b>	<b>20.6</b>			<b>22.1</b>	<b>25.7</b>	<b>27.4</b>	<b>28.9</b>	<b>29.8</b>	<b>29.8</b>					<b>27.1</b>	<b>18.5</b>	
Of which: public and publicly guaranteed (PPG)	79.6	80.2	72.4	48.6	40.0	11.6	11.4	14.1	19.2	23.3	18.4			19.9	22.3	23.7	25.0	25.8	25.8					23.6	14.5	
Change in external debt	...	0.6	-7.8	-23.8	-5.4	-29.4	-0.9	2.3	4.8	5.9	-5.4			1.5	3.6	1.6	1.5	0.9	0.0					-0.8	-0.7	
Identified net debt-creating flows	...	-7.3	-12.2	-8.1	-2.3	-7.7	-1.1	0.1	2.1	-4.6	-2.7			2.6	1.3	1.1	0.6	0.1	-0.5					-1.0	-2.1	
<b>Non-interest current account deficit</b>	<b>3.6</b>	<b>0.7</b>	<b>0.6</b>	<b>5.8</b>	<b>9.0</b>	<b>4.3</b>	<b>5.6</b>	<b>5.0</b>	<b>3.9</b>	<b>0.5</b>	<b>6.4</b>			<b>4.2</b>	<b>2.8</b>	<b>6.2</b>	<b>5.3</b>	<b>5.5</b>	<b>5.2</b>	<b>5.0</b>	<b>4.6</b>			<b>4.2</b>	<b>3.4</b>	4.2
Deficit in balance of goods and services	14.1	14.2	14.2	20.6	22.9	19.5	19.8	18.4	19.6	15.1	18.2			16.7	16.0	15.7	15.2	14.6	13.8					13.4	12.6	
Exports	12.7	13.5	15.0	15.2	14.0	12.9	11.6	10.6	13.8	17.0	14.0			13.0	14.0	14.5	15.1	15.6	16.2					17.4	19.1	
Imports	26.9	27.7	29.1	35.8	36.9	32.4	31.4	29.0	33.3	32.1	32.2			29.7	30.0	30.2	30.3	30.3	30.0					30.8	31.7	
Net current transfers (negative = inflow)	-10.2	-13.7	-13.4	-14.5	-14.0	-15.0	-14.0	-13.4	-15.7	-14.7	-11.8			-14.0	-10.7	-10.3	-10.0	-9.6	-9.3					-9.2	-9.2	-9.1
Of which: official	-5.6	-7.1	-5.7	-6.1	-5.8	-6.2	-5.0	-4.9	-6.5	-5.9	-4.2			-3.1	-3.7	-3.6	-3.6	-3.6	-3.6					-3.5	-3.5	
Other current account flows (negative = net inflow)	-0.4	0.2	-0.1	-0.2	0.0	-0.2	-0.2	0.0	0.0	0.0	0.0			0.1	0.0	0.0	0.0	0.0	0.0					0.0	0.0	
<b>Net FDI (negative = inflow)</b>	<b>-1.3</b>	<b>-1.5</b>	<b>-1.5</b>	<b>-1.2</b>	<b>-2.4</b>	<b>-2.5</b>	<b>-3.1</b>	<b>-2.8</b>	<b>-3.3</b>	<b>-4.0</b>	<b>-2.5</b>			<b>-2.5</b>	<b>-2.8</b>	<b>-3.1</b>	<b>-3.4</b>	<b>-3.7</b>	<b>-3.8</b>					<b>-4.1</b>	<b>-4.5</b>	-4.3
<b>Endogenous debt dynamics 2/</b>	<b>...</b>	<b>-6.5</b>	<b>-11.3</b>	<b>-12.7</b>	<b>-8.9</b>	<b>-9.5</b>	<b>-3.6</b>	<b>-2.1</b>	<b>1.5</b>	<b>-1.1</b>	<b>-6.6</b>			<b>-1.1</b>	<b>-1.2</b>	<b>-1.3</b>	<b>-1.2</b>	<b>-1.3</b>	<b>-1.3</b>					<b>-1.2</b>	<b>-0.9</b>	
Contribution from nominal interest rate	...	0.6	0.7	0.5	0.2	0.2	0.1	0.1	0.2	0.2	0.2			0.2	0.4	0.5	0.6	0.6	0.7					0.5	0.2	
Contribution from real GDP growth	...	1.5	-8.0	-7.5	-4.6	-4.0	-1.1	-1.1	-1.8	-2.1	-1.6			-1.3	-1.6	-1.8	-1.8	-1.9	-1.9					-1.7	-1.2	
Contribution from price and exchange rate changes	...	-8.7	-4.0	-5.7	-4.6	-5.7	-2.5	-1.2	3.0	0.9	-5.1			...	...	...	...	...	...					...	...	
<b>Residual (3-4) 3/</b>	<b>...</b>	<b>7.9</b>	<b>4.3</b>	<b>-15.7</b>	<b>-3.1</b>	<b>-21.7</b>	<b>0.2</b>	<b>2.2</b>	<b>2.7</b>	<b>10.4</b>	<b>-2.7</b>			<b>-1.1</b>	<b>2.3</b>	<b>0.5</b>	<b>0.9</b>	<b>0.8</b>	<b>0.6</b>					<b>0.2</b>	<b>1.4</b>	
Of which: exceptional financing	...	0.0	0.0	0.0	-0.6	-0.6	-0.5	-0.4	-0.4	-0.3	-0.1			0.0	0.0	0.0	0.0	0.0	0.0					0.0	0.0	
PV of external debt 4/	...	...	...	...	...	...	...	...	...	...	15.4			16.6	19.8	21.1	22.4	23.1	23.0					20.6	14.1	
Percent of exports	...	...	...	...	...	...	...	...	...	...	110.1			127.8	140.6	145.7	147.9	147.7	142.3					118.4	73.7	
<b>PV of PPG external debt</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>13.2</b>			<b>14.4</b>	<b>16.3</b>	<b>17.4</b>	<b>18.5</b>	<b>19.1</b>	<b>19.0</b>					<b>17.0</b>	<b>10.0</b>	
<b>Percent of exports</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>94.3</b>			<b>110.6</b>	<b>116.3</b>	<b>120.1</b>	<b>122.1</b>	<b>122.2</b>	<b>117.7</b>					<b>97.9</b>	<b>52.3</b>	
<b>Percent of government revenues</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>95.9</b>			<b>100.7</b>	<b>127.3</b>	<b>131.0</b>	<b>139.7</b>	<b>144.6</b>	<b>144.8</b>					<b>127.7</b>	<b>73.9</b>	
<b>Debt service-to-exports ratio (percent)</b>	<b>53.0</b>	<b>16.8</b>	<b>10.7</b>	<b>8.9</b>	<b>8.0</b>	<b>7.3</b>	<b>2.9</b>	<b>2.4</b>	<b>3.2</b>	<b>4.3</b>	<b>6.6</b>			<b>8.1</b>	<b>8.4</b>	<b>10.0</b>	<b>10.3</b>	<b>10.9</b>	<b>11.6</b>					<b>10.6</b>	<b>4.6</b>	
<b>PPG debt service-to-exports ratio (percent)</b>	<b>53.0</b>	<b>16.8</b>	<b>10.7</b>	<b>8.8</b>	<b>7.2</b>	<b>5.0</b>	<b>1.3</b>	<b>1.3</b>	<b>2.2</b>	<b>2.9</b>	<b>4.9</b>			<b>5.8</b>	<b>6.4</b>	<b>7.2</b>	<b>7.1</b>	<b>7.4</b>	<b>8.0</b>					<b>8.2</b>	<b>4.6</b>	
<b>PPG debt service-to-revenue ratio (percent)</b>	<b>48.9</b>	<b>15.6</b>	<b>10.6</b>	<b>10.3</b>	<b>7.9</b>	<b>5.3</b>	<b>1.1</b>	<b>1.0</b>	<b>2.3</b>	<b>3.7</b>	<b>5.0</b>			<b>5.3</b>	<b>7.0</b>	<b>7.8</b>	<b>8.1</b>	<b>8.8</b>	<b>9.9</b>					<b>10.6</b>	<b>6.5</b>	
Total gross financing need (Billions of U.S. dollars)	...	...	...	...	1.2	0.5	0.7	0.8	0.3	-0.9	2.0			2.2	1.9	2.1	2.0	1.9	1.8					2.0	-0.5	
Non-interest current account deficit that stabilizes debt ratio	...	0.1	8.5	29.6	14.4	33.7	6.5	2.7	-0.9	-5.4	11.7			4.7	1.7	3.9	3.7	4.1	4.5					5.0	4.1	
<b>Key macroeconomic assumptions</b>																										
Real GDP growth (percent)	1.6	-2.1	11.7	12.6	11.5	11.8	11.2	10.0	10.6	11.4	8.5			9.7	4.3	7.0	7.5	7.0	7.0					7.2	6.5	6.5
GDP deflator in U.S. dollar terms (change in percent)	-6.1	12.2	5.3	8.6	10.4	15.3	22.5	9.9	-16.6	-4.1	24.7			8.8	12.1	4.0	-0.9	1.8	0.9					1.3	0.9	0.9
Effective interest rate (percent) 5/	1.2	0.8	1.1	0.9	0.6	0.5	1.2	0.9	1.1	1.1	1.2			0.9	0.2	1.3	1.8	2.0	2.2					2.0	2.0	1.7
Growth of exports of G&S (U.S. dollar terms, percent)	0.4	16.0	31.1	24.4	13.3	18.2	23.0	10.5	19.7	31.7	11.8			20.0	7.5	3.3	15.0	13.0	12.6					11.2	8.7	9.3
Growth of imports of G&S (U.S. dollar terms, percent)	7.1	13.2	23.8	50.3	27.0	13.0	32.1	11.6	6.1	2.9	35.9			21.6	15.0	2.8	7.5	10.2	8.3					7.3	8.2	7.3
Grant element of new public sector borrowing (percent)	...	...	...	...	...	...	...	...	...	...	...			...	...	...	...	...	...					...	...	
Government revenue (excluding grants, percent of GDP)	13.8	14.5	15.2	13.0	12.8	12.1	13.1	14.1	13.4	13.3	13.8			14.3	12.8	13.3	13.2	13.2	13.1					13.3	13.5	13.4
Aid flows (Billions of U.S. dollars) 7/	...	...	...	1.2	1.2	1.6	1.6	2.0	2.7	2.5	2.8			2.4	2.8	2.9	3.1	3.3	3.5					4.5	8.1	
Of which: grants	0.4	0.6	0.6	0.7	0.9	1.2	1.3	1.6	1.9	1.9	1.8			1.5	1.8	2.0	2.1	2.3	2.5					3.5	7.2	
Of which: concessional loans	...	...	...	0.5	0.4	0.4	0.3	0.4	0.8	0.6	1.0			0.9	1.0	1.0	1.0	1.0	1.0					1.0	1.0	
Grant-equivalent financing (percent of GDP) 8/	...	...	...	...	...	...	...	...	...	...	...			4.2	4.7	4.6	4.5	4.4	4.4					4.0	3.8	3.9
Grant-equivalent financing (percent of external financing) 8/	...	...	...	...	...	...	...	...	...	...	...			63.3	59.4	61.3	62.4	64.7	69.1					74.9	84.3	77.6
<b>Memorandum items:</b>																										
Nominal GDP (Billions of U.S. dollars)	7.7	8.5	10.0	12.2	15.0	19.4	26.4	31.9	29.4	31.4	42.5			47.3	50.4	55.1	59.6	64.3	69.5					99.6	204.5	
Nominal dollar GDP growth	...	9.8	17.6	22.3	23.2	28.9	36.2	20.9	-7.8	6.8	35.4			11.3	6.5	9.4	8.0	7.9	8.1					8.5	7.5	7.5
PV of PPG external debt (Billions of U.S. dollars)	...	...	...	...	...	...	...	...	...	...	5.5			6.5	8.0	9.3	10.6	11.9	12.8					16.4	19.8	
(PVt-PVt-1)/GDPt-1 (percent)	...	...	...	...	...	...	...	...	...	...	...			2.4	3.0	2.6	2.4	2.1	1.4					2.3	0.6	0.2
Gross workers' remittances (Billions of U.S. dollars)	0.2	0.2	0.2	0.4	0.4	1.2	1.8	1.8	1.8	1.9	1.9			2.1	2.1	2.2	2.3	2.3	2.4					3.2	3.2	
PV of PPG external debt (percent of GDP + remittances)	...	...	...	...	...	...	...	...	...	...	12.6			13.8	15.7	16.8	17.8	18.4	18.4					16.5	9.8	
PV of PPG external debt (percent of exports + remittances)	...	...	...	...	...	...	...	...	...	...	71.1			82.1	89.3	94.2	97.5	99.1	96.9					82.7	48.4	
Debt service of PPG external debt (percent of exports + remittances)	...	...	...	...	...	...	...	...	...	...	3.7			4.3	4.9	5.6	5.7	6.0	6.6					6.9	4.3	

Sources: Ethiopian authorities

**Table 2. Ethiopia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2013–33**

	Projections							2033
	2013	2014	2015	2016	2017	2018	2023	
<b>PV of Debt-to GDP Ratio</b>								
<b>Baseline</b>	14.4	16.3	17.4	18.5	19.1	19.0	<b>17.0</b>	10.0
<b>A. Alternative scenarios</b>								
A1. Key variables at their historical averages in 2013–2033 1/	14	14	13	13	13	13	<b>13</b>	14
A2. New public sector loans on less favorable terms in 2013–2033 2	14	17	19	21	23	23	<b>24</b>	18
<b>B. Bound tests</b>								
B1. Real GDP growth at historical average minus one standard deviation in 2014–2015	14	16	17	19	19	19	<b>17</b>	10
B2. Export value growth at historical average minus one standard deviation in 2014–2015 3/	14	16	17	18	19	19	<b>17</b>	10
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2014–2015	14	16	18	19	20	20	<b>18</b>	10
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014–2015 4/	14	15	15	16	17	17	<b>15</b>	9
B5. Combination of B1–B4 using one-half standard deviation shocks	14	13	11	12	13	13	<b>13</b>	8
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	14	23	24	26	26	26	<b>23</b>	14
<b>PV of Debt-to-Exports Ratio</b>								
<b>Baseline</b>	111	116	120	122	122	118	<b>98</b>	52
<b>A. Alternative scenarios</b>								
A1. Key variables at their historical averages in 2013–2033 1/	111	98	93	89	86	83	<b>73</b>	72
A2. New public sector loans on less favorable terms in 2013–2033 2	111	120	131	139	144	143	<b>137</b>	97
<b>B. Bound tests</b>								
B1. Real GDP growth at historical average minus one standard deviation in 2014–2015	111	112	116	118	118	113	<b>94</b>	50
B2. Export value growth at historical average minus one standard deviation in 2014–2015 3/	111	117	123	125	124	120	<b>99</b>	52
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2014–2015	111	112	116	118	118	113	<b>94</b>	50
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014–2015 4/	111	106	104	106	107	104	<b>87</b>	48
B5. Combination of B1–B4 using one-half standard deviation shocks	111	96	79	83	85	83	<b>73</b>	43
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	111	112	116	118	118	113	<b>94</b>	50
<b>PV of Debt-to-Revenue Ratio</b>								
<b>Baseline</b>	101	127	131	140	145	145	<b>128</b>	74
<b>A. Alternative scenarios</b>								
A1. Key variables at their historical averages in 2013–2033 1/	101	108	101	102	102	102	<b>95</b>	102
A2. New public sector loans on less favorable terms in 2013–2033 2	101	132	143	159	171	177	<b>178</b>	136
<b>B. Bound tests</b>								
B1. Real GDP growth at historical average minus one standard deviation in 2014–2015	101	125	132	140	145	145	<b>127</b>	73
B2. Export value growth at historical average minus one standard deviation in 2014–2015 3/	101	125	131	139	143	143	<b>125</b>	72
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2014–2015	101	126	137	145	150	151	<b>132</b>	76
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014–2015 4/	101	116	113	122	127	127	<b>114</b>	68
B5. Combination of B1–B4 using one-half standard deviation shocks	101	102	85	94	100	102	<b>94</b>	60
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	101	176	182	193	200	200	<b>176</b>	101



**Table 2. Ethiopia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2013–33 (concluded)  
(Percent)**

Debt Service-to-Exports Ratio								
<b>Baseline</b>	6	6	7	7	7	8	<b>8</b>	5
<b>A. Alternative scenarios</b>								
A1. Key variables at their historical averages in 2013–2033 1/	6	6	6	5	5	5	<b>4</b>	3
A2. New public sector loans on less favorable terms in 2013–2033 2	6	6	7	7	8	8	<b>9</b>	7
<b>B. Bound tests</b>								
B1. Real GDP growth at historical average minus one standard deviation in 2014–2015	6	6	7	7	7	8	<b>8</b>	5
B2. Export value growth at historical average minus one standard deviation in 2014–2015 3/	6	7	7	7	8	8	<b>9</b>	5
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2014–2015	6	6	7	7	7	8	<b>8</b>	5
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014–2015 4/	6	6	7	7	7	8	<b>8</b>	4
B5. Combination of B1–B4 using one-half standard deviation shocks	6	6	7	6	6	7	<b>6</b>	4
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	6	6	7	7	7	8	<b>8</b>	5
<b>Debt Service-to-Revenue Ratio</b>								
<b>Baseline</b>	5	7	8	8	9	10	<b>11</b>	6
<b>A. Alternative scenarios</b>								
A1. Key variables at their historical averages in 2013–2033 1/	5	6	6	6	6	6	<b>5</b>	4
A2. New public sector loans on less favorable terms in 2013–2033 2	5	7	8	8	9	9	<b>11</b>	11
<b>B. Bound tests</b>								
B1. Real GDP growth at historical average minus one standard deviation in 2014–2015	5	7	8	8	9	10	<b>11</b>	7
B2. Export value growth at historical average minus one standard deviation in 2014–2015 3/	5	7	8	8	9	10	<b>11</b>	7
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2014–2015	5	7	8	9	9	11	<b>11</b>	7
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014–2015 4/	5	7	8	8	8	10	<b>10</b>	6
B5. Combination of B1–B4 using one-half standard deviation shocks	5	7	7	7	8	9	<b>8</b>	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	5	10	11	12	13	14	<b>15</b>	9
<i>Memorandum item:</i>								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	20	20	20	20	20	20	<b>20</b>	20

Sources: Ethiopian authorities; IMF and World Bank staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline, while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

**Table 3. Ethiopia: Public Sector Debt Sustainability Framework, Baseline Scenario, 2010–33  
(Percent of GDP, unless otherwise indicated)**

	Actual			Average <sup>5/</sup>	Standard Deviation <sup>5/</sup>	Estimate				Projections				2019–33 Average	
	2010	2011	2012			2013	2014	2015	2016	2017	2018	2013–18 Average			2023
<b>Public sector debt 1/</b>	40.3	38.9	33.2			39.6	43.4	46.0	48.7	50.8	51.9		54.1	48.2	
Of which: foreign-currency denominated	19.2	23.3	18.4			19.9	22.3	23.7	25.0	25.8	25.8		23.6	14.5	
Change in public sector debt	4.0	-1.5	-5.6			6.4	3.8	2.6	2.7	2.1	1.1		-0.1	-0.6	
Identified debt-creating flows	-0.5	-3.6	-7.2			6.9	2.7	1.7	1.7	1.0	0.3		0.2	-0.3	
Primary deficit	1.0	2.5	3.7	3.3	1.7	9.9	5.5	5.4	5.1	4.5	4.2	5.7	4.3	3.9	4.2
Revenue and grants	19.9	19.2	18.0			17.4	16.5	16.9	16.8	16.8	16.8		16.8	17.0	
Of which: grants	6.5	5.9	4.2			3.1	3.7	3.6	3.6	3.6	3.6		3.5	3.5	
Primary (noninterest) expenditure	20.9	21.7	21.7			27.3	22.0	22.3	21.9	21.3	20.9		21.1	20.9	
Automatic debt dynamics	-1.4	-5.8	-10.6			-3.0	-2.7	-3.7	-3.4	-3.6	-3.8		-4.1	-4.3	
Contribution from interest rate/growth differential	-3.5	-6.8	-6.3			-2.8	-3.0	-3.6	-3.5	-3.7	-4.0		-4.3	-4.4	
Of which: contribution from average real interest rate	0.0	-2.6	-3.3			-0.6	-0.3	-0.6	-0.5	-0.5	-0.7		-1.0	-1.4	
Of which: contribution from real GDP growth	-3.5	-4.1	-3.1			-2.2	-2.7	-3.0	-3.0	-3.2	-3.3		-3.3	-3.0	
Contribution from real exchange rate depreciation	2.2	0.9	-4.3			-0.1	0.3	-0.1	0.1	0.2	0.2		...	...	
Other identified debt-creating flows	-0.2	-0.3	-0.4			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	-0.2	-0.3	-0.4			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	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 (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	4.5	2.2	1.6			-0.5	1.0	0.9	1.0	1.1	0.8		-0.3	-0.3	
<b>Other sustainability indicators</b>															
<b>PV of public sector debt</b>			28.1			34.1	37.4	39.8	42.2	44.1	45.2		47.6	43.8	
Of which: foreign-currency denominated			13.2			14.4	16.3	17.4	18.5	19.1	19.0		17.0	10.0	
Of which: external			13.2			14.4	16.3	17.4	18.5	19.1	19.0		17.0	10.0	
PV of contingent liabilities (not included in public sector debt)			...			...	...	...	...	...	...		...	...	
Gross financing need 2/	2.4	4.2	5.6			12.0	7.7	8.1	8.3	7.9	7.6		7.3	5.9	
PV of public sector debt-to-revenue and grants ratio (percent)	...	...	156.1			195.9	226.8	235.6	251.1	262.5	269.5		282.8	257.1	
PV of public sector debt-to-revenue ratio (percent)	...	...	203.7			238.8	291.3	298.9	319.6	334.3	343.8		357.0	323.6	
Of which: external 3/	...	...	95.9			100.7	127.3	131.0	139.7	144.6	144.8		127.7	73.9	
Debt service-to-revenue and grants ratio (percent) 4/	7.2	8.9	10.2			12.2	13.3	15.8	19.2	20.0	20.7		17.7	11.7	
Debt service-to-revenue ratio (percent) 4/	10.7	12.9	13.3			14.8	17.1	20.1	24.5	25.4	26.4		22.4	14.7	
Primary deficit that stabilizes the debt-to-GDP ratio	-2.9	3.9	9.4			3.5	1.7	2.7	2.4	2.4	3.0		4.4	4.5	
<b>Key macroeconomic and fiscal assumptions</b>															
Real GDP growth (percent)	10.6	11.4	8.5	9.7	4.3	7.0	7.5	7.5	7.0	7.0	7.0	7.2	6.5	6.5	6.5
Average nominal interest rate on forex debt (percent)	0.9	0.8	1.1	0.8	0.2	0.9	1.7	1.8	1.9	2.0	2.1	1.7	1.9	1.5	1.8
Average real interest rate on domestic debt (percent)	-0.1	-13.6	-21.3	-11.2	7.1	-4.2	-1.7	-3.4	-2.8	-2.9	-3.2	-3.0	-3.8	-4.3	-3.9
Real exchange rate depreciation (percent, + indicates depreciation)	16.9	5.4	-20.1	-4.8	10.4	-0.8	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, percent)	3.4	19.8	34.1	16.5	10.1	11.3	7.0	8.9	8.0	7.9	8.1	8.5	8.0	8.0	8.0
Growth of real primary spending (deflated by GDP deflator, percent)	0.1	0.2	0.1	0.1	0.1	0.3	-0.1	0.1	0.1	0.0	0.0	0.1	0.1	0.1	0.1
Grant element of new external borrowing (percent)	...	...	...	...	...	30.8	24.8	25.3	24.8	25.7	27.8	26.5	28.6	27.1	...

Sources: Ethiopian authorities; IMF and World Bank staff estimates and projections.

1/ Public sector debt covers general government and selected nonfinancial public enterprises. Gross debt is used.

2/ 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.

3/ Revenue excluding grants.

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

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

**Table 4. Ethiopia: Sensitivity Analysis for Key Indicators of Public Debt, 2013–33  
(Percent)**

	Projections							
	2013	2014	2015	2016	2017	2018	2023	2033
<b>PV of Debt-to-GDP Ratio</b>								
<b>Baseline</b>	34	37	40	42	44	45	48	44
<b>A. Alternative scenarios</b>								
A1. Real GDP growth and primary balance are at historical averages	34	35	35	36	36	36	32	27
A2. Primary balance is unchanged from 2013	34	41	47	53	58	63	82	105
A3. Permanently lower GDP growth 1/	34	38	41	44	47	49	57	70
<b>B. Bound tests</b>								
B1. Real GDP growth is at historical average minus one standard deviation in 2014–2015	34	38	42	45	47	49	53	51
B2. Primary balance is at historical average minus one standard deviation in 2014–2015	34	37	39	42	43	45	47	43
B3. Combination of B1-B2 using one-half standard deviation shocks	34	36	38	40	42	43	46	43
B4. One-time 30 percent real depreciation in 2014	34	43	45	47	49	50	52	50
B5. 10 percent of GDP increase in other debt-creating flows in 2014	34	45	47	49	51	52	53	47
<b>PV of Debt-to-Revenue Ratio 2/</b>								
<b>Baseline</b>	196	227	236	251	263	270	283	257
<b>A. Alternative scenarios</b>								
A1. Real GDP growth and primary balance are at historical averages	196	213	210	215	218	219	201	174
A2. Primary balance is unchanged from 2013	196	248	276	312	346	377	489	618
A3. Permanently lower GDP growth 1/	196	229	240	260	275	287	331	394
<b>B. Bound tests</b>								
B1. Real GDP growth is at historical average minus one standard deviation in 2014–2015	196	231	246	265	278	288	311	298
B2. Primary balance is at historical average minus one standard deviation in 2014–2015	196	224	231	247	259	266	280	255
B3. Combination of B1-B2 using one-half standard deviation shocks	196	220	224	239	251	258	273	250
B4. One-time 30 percent real depreciation in 2014	196	264	268	281	291	297	312	292
B5. 10 percent of GDP increase in other debt-creating flows in 2014	196	274	280	294	303	309	315	277
<b>Debt Service-to-Revenue Ratio 2/</b>								
<b>Baseline</b>	12	13	16	19	20	21	18	12
<b>A. Alternative scenarios</b>								
A1. Real GDP growth and primary balance are at historical averages	12	13	15	18	18	18	13	7
A2. Primary balance is unchanged from 2013	12	13	16	21	22	23	24	29
A3. Permanently lower GDP growth 1/	12	13	16	20	21	22	20	17
<b>B. Bound tests</b>								
B1. Real GDP growth is at historical average minus one standard deviation in 2014–2015	12	14	16	20	21	22	19	14
B2. Primary balance is at historical average minus one standard deviation in 2014–2015	12	13	16	19	20	21	18	12
B3. Combination of B1-B2 using one-half standard deviation shocks	12	13	16	19	20	20	17	11
B4. One-time 30 percent real depreciation in 2014	12	15	19	22	23	25	22	16
B5. 10 percent of GDP increase in other debt-creating flows in 2014	12	13	17	21	21	22	20	13
Sources: Ethiopian authorities; IMF and World Bank staff estimates and projections.								
1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.								
2/ Revenue is defined inclusive of grants.								



# THE FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA

## STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

August 29, 2013

Prepared By

African Department (In consultation with other departments)

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## FUND RELATIONS

**Membership Status:** Joined: December 27, 1945

[Article XIV](#)

<b>General Resources Account:</b>	<b>SDR Million</b>	<b>%Quota</b>
Quota	133.70	100.00
Fund holdings of currency	126.20	94.39
Reserve Tranche Position	7.51	5.62
Lending to the Fund		
Holdings Exchange Rate		

<b>SDR Department:</b>	<b>SDR Million</b>	<b>%Allocation</b>
Net cumulative allocation	127.93	100.00
Holdings	97.25	76.02

<b>Outstanding Purchases and Loans:</b>	<b>SDR Million</b>	<b>%Quota</b>
ESF Arrangement	153.76	115.00
ESF RAC Loan	33.43	25.00

### **Latest Financial Arrangements:**

<u>Type</u>	<u>Date of Arrangement</u>	<u>Expiration Date</u>	<u>Amount Approved (SDR Million)</u>	<u>Amount Drawn (SDR Million)</u>
ESF	Aug 26, 2009	Nov 22, 2010	153.76	153.76
ECF <sup>1/</sup>	Mar 22, 2001	Oct 31, 2004	100.28	100.28
ECF <sup>1/</sup>	Oct 11, 1996	Oct 22, 1999	88.47	29.49

<sup>1/</sup> Formerly PRGF.

### **Projected Payments to Fund <sup>2/</sup>**

**(SDR Million; based on existing use of resources and present holdings of SDRs):**

	<u>Forthcoming</u>				
	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
Principal		3.34	25.40	37.44	37.44
Charges/Interest	0.01	0.03	0.45	0.38	0.28
<b>Total</b>	0.01	3.37	25.86	37.81	37.72

<sup>2/</sup> When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

### **Implementation of HIPC Initiative:**

Enhanced

- I. Commitment of HIPC assistance  
Decision point date

[Framework](#)  
November 2001

Assistance committed	
by all creditors (US\$ Million) <sup>1/</sup>	1,982.20
<i>of which:</i> IMF assistance (US\$ million)	60.85
(SDR equivalent in millions)	45.12
Completion point date	April 2004
<b>II. Disbursement of IMF assistance (SDR Million)</b>	
Assistance disbursed to the member	45.12
Interim assistance	10.28
Completion point balance	34.84
Additional disbursement of interest income <sup>2/</sup>	1.54
<b>Total disbursements</b>	<b>46.66</b>

<sup>1/</sup> Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts cannot be added.

<sup>2/</sup> Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

#### **Implementation of Multilateral Debt Relief Initiative (MDRI):**

I. MDRI-eligible debt (SDR Million) <sup>1/</sup>	112.07
Financed by: MDRI Trust	79.66
Remaining HIPC resources	32.41
II. Debt Relief by Facility (SDR Million)	

#### Eligible Debt

<u>Delivery Date</u>	<u>GRA</u>	<u>PRGT</u>	<u>Total</u>
January 2006	N/A	112.07	112.07

<sup>1/</sup> The MDRI provides 100 percent debt relief to eligible member countries that qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 that remains outstanding at the time the member qualifies for such debt relief.

### **Safeguard Assessment**

An update safeguards assessment of the National Bank of Ethiopia (NBE) was completed in December 2009 in connection with Ethiopia's ESF-RAC approved on January 23, 2009. The assessment found that, since the previous assessment in 2001, the NBE has implemented some improvements to the safeguards framework but that several initiatives were a work-in-progress and substantial gaps remained. Financial transparency has improved through the publication of independently audited financial statements, and internal audit capacity has been strengthened. In response to the assessment's recommendations, action has been taken to commence Audit Committee (AC) oversight, and introduce controls and independent reviews over program data

reporting to the Fund. The authorities are also in the process of addressing remaining safeguards issues relating to enhancing AC oversight of the external audit mechanism, further strengthening of reserve management capacity, and introducing bank-wide risk management practices. Going forward, the NBE Law will need to be strengthened with regard to independence of the central bank and the potential scope for unlimited financing of the government.

### **Exchange Rate Arrangement**

The de facto exchange rate regime is classified as a crawl-like arrangement. The authorities describe their exchange rate regime as a managed float with no predetermined path for the exchange rate. The pace of the depreciation, however, has been stable. The NBE supplies foreign exchange to the market based on plans established at the beginning of each fiscal year that takes into account estimates of likely supply and demand. The transaction-weighted average interbank market exchange rate on July 31, 2013, was Br 18.90 = US\$1.

Ethiopia currently maintains four restrictions on the payments and transfers for current international transactions, which relate to: (i) the tax certification requirement for repatriation of dividend and other investment income; (ii) restrictions on repayment of legal external loans and supplies and foreign partner credits; (iii) rules for issuance of import permits by commercial banks; and (iv) the requirement to provide a clearance certificate from NBE to obtain import permits. These restrictions are inconsistent with Article VIII, Section 2(a), of the IMF's Articles of Agreement and remain unapproved.

The staff is continuing to assess whether a general finance and economic cooperation agreement signed between the government of Ethiopia and China in 2006 gives rise to exchange restrictions under Article VIII.

### **Article IV Consultation**

Ethiopia is on the standard 12-month consultation cycle, in accordance with the Decision on Article IV Consultation Cycles (Decision No. 14747-(10/96), 9/28/2010). The last consultation was concluded on September, 2012.

**Technical Assistance (2007–present)**

<b>Department</b>	<b>Purpose</b>	<b>Time of Delivery</b>
MCM	Bank supervision	July 2007
MCM	Monetary operations	July 2007
MCM	Payment system	July 2007
AFE	Customs administration	October 2007
FAD	Public expenditure management	December 2007
AFE	Program budgeting	December 2007
AFE	Macro-fiscal	January 2008
AFE	Program budgeting	January 2008
AFE	Banking supervision	February 2008
AFE	Consumer price index	March 2008
MCM	Islamic banking regulation	April 2009
AFE	Banking supervision	June 2009
AFE	Program budgeting chart of accounts	July 2009
FAD	Revenue administration	September 2009
FAD	Program budgeting	November 2009
FAD	Tax policy	December 2009
AFE	Cash management and treasury single account	February 2010
AFE	Price statistics	February 2010
AFE	Risk-based supervision	May 2010
AFE	Medium-Term Expenditure Framework	August 2010
AFE	Stress testing	November 2010
FAD	Tax administration	December 2010
AFE	Cash management	February 2011
STA	Balance of payments statistics	March 2011
AFE	National accounts statistics	March 2011
FAD	Tax incentives, tax expenditures, and transfer pricing	December 2011
AFE	Payment system	December 2011
AFE	National Accounts Statistics	March 2012
FAD	Reform review and monitoring on tax policy	March 2013
FAD	Program-based budgeting	March-April 2013
AFE	Solvency framework for insurers	May 2013

**Resident Representative**

The IMF has had a resident representative office in Addis Ababa since 1993. The current Resident Representative, Mr. Jan Mikkelsen, took up the post in January 2012.



## JOINT MANAGEMENT ACTION PLAN, JULY 2013- AUGUST 2014

Title	Products	Provisional and actual timing of missions	Expected and actual delivery date
<b>A. Mutual information on relevant work program</b>			
The World Bank work program in the next 12 months	<b>Economic policy analysis and advice</b> <ul style="list-style-type: none"> <li>Ethiopia Economic Update (bi-annual)</li> <li>Public Expenditure Review</li> <li>Policy dialogue on economic reform issues</li> <li>Poverty assessment</li> <li>Poverty mapping</li> </ul>	July 2013–June 2014 July 2013–June 2014 July 2013–June 2014 July 2013–June 2014 July 2013–June 2014	Q4 2013, Q2 2014 Q2 2014 ongoing Q2 2014 Q3 2013
	<b>Technical Assistance</b> <ul style="list-style-type: none"> <li>Capacity Building of the Central Statistical Agency</li> <li>Staff turnover study</li> <li>Public financial management</li> </ul>	July 2013–June 2014 July 2013–June 2014 July 2013–June 2014 July 2013–June 2014	ongoing (until 2016) Q2 2014 ongoing
The Fund work program in the next 12 months	<b>Macroeconomic policy analysis and advice</b> <ul style="list-style-type: none"> <li>Article IV consultation</li> </ul>	May 2014	June 2014
	<b>Technical assistance</b> <ul style="list-style-type: none"> <li>PFM</li> <li>Statistical capacity (national accounts, CPI)</li> <li>Tax administration</li> </ul>	Ongoing Ongoing July 2012–June 2015	
<b>B. Requests for work program inputs</b>			
Fund request to Bank	<ul style="list-style-type: none"> <li>Periodic update on progress on the financial sector capacity building project and social sector projects including poverty related work.</li> <li>Macroeconomic and financial data to be shared regularly.</li> </ul>	Ongoing	
Bank request to Fund	<ul style="list-style-type: none"> <li>Periodic update on all TA activities.</li> <li>Macroeconomic and financial data to be shared regularly.</li> </ul>	Ongoing	
<b>C. Agreement on joint products and missions</b>			
Joint products in the next 12 months	Debt sustainability analysis		July 2014

## STATISTICAL ISSUES

### I. Assessment of Data Adequacy for Surveillance

**General:** Data provided to the Fund are broadly adequate for surveillance purposes, albeit with some shortcomings. Despite recent progress, there are some shortcomings in financial, real, fiscal, and balance of payments statistics.

**National Accounts:** Shortcomings in the source data and compilation practices affect the accuracy and reliability of the statistics. The GDP estimates are heavily dependent on benchmark data that may not reflect current economic activity. Further, the techniques used to compile the estimates for construction, distribution, and some other services activities do not conform to international best practice. While some progress has been made in compiling estimates of GDP by final expenditure, there remain substantial shortcomings, particularly in the estimation of private consumption and fixed capital formation. The statistical discrepancies between the estimates by expenditure categories and output remain large.

**Government finance statistics:** Despite recent improvements, general government fiscal statistics continue to be affected by shortcomings. Timely data on the consolidated operations of local governments is unavailable. Significant discrepancies between data on the domestic financing of the budget deficit and the monetary accounts continue to complicate assessment of fiscal developments.

**Monetary statistics:** Monetary statistics are broadly adequate for analytical purposes, although there is a need for the NBE to resume data submissions based on the SRF and IMD framework. For policy purposes, however, ensuring data collection and reporting in a timely manner continues to be critical.

**Financial statistics:** The staff does not have access to sufficient data to assess the soundness of the banking sector.

**Balance of payments:** Balance of payments data require improvements in coverage, valuation, timing, and classification of current account transactions. Financial and capital account transactions are also incompletely covered and data on FDI could to be better reconciled with alternative sources. Improvements in balance of payments compilation could most appropriately be pursued in the context of adopting the sixth edition of the *Balance of Payments and International Investment Position Manual*.

### II. Data Standards and Quality

Ethiopia participates in the General Data Dissemination System (GDDS) and metadata were partially updated in early 2008. Ethiopia participates in the GDDS project for capacity building in statistics in Anglophone Africa (2006–09) including socio-demographic, macro-economic and financial statistics. No Report on the Observance of Standards and Codes has been completed.

## TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE

(As of July 31, 2013)

	Date of Latest Observation	Date Received	Frequency of Data	Frequency of Reporting	Frequency of Publication
Exchange rates	July 2013	July, 2012	D	D	D
International reserve assets and reserve liabilities of the monetary authorities <sup>1/</sup>	May 2013	June 2012	M	M	M
Reserve/base money	May 2013	June 2013	M	M	M
Broad money	April 2012	June 2013	M	M	M
Central bank balance sheet	April 2012	June 2013	M	M	M
Consolidated balance sheet of the banking system <sup>2/</sup>	....	....	NA	NA	NA
Interest rates <sup>3/</sup>	April 2012	June 2013	M	M	M
Consumer Price Index	June 2012	July 2013	M	M	M
Revenue, expenditure, balance, and composition of financing <sup>4/</sup> – general government <sup>5/</sup>	December 2012	May 2013	Q	Q	Q
Revenue, expenditure, balance, and composition of financing <sup>4/</sup> – central government	July 2013	April 2013	M	M	NA
Stocks of central government and central government-guaranteed debt <sup>6/</sup>	2011/12	June 2013	A	On mission	A
External current account balance	March 2013	June 2013	Q	Q	Q
Exports and imports of goods and services	April 2013	June 2013	M	Q	Q
GDP/GNP	2011/12	January 2013	A	A	A
Gross external debt	2011/12	May 2013	A	On mission	A
International investment position	...	...	NA	NA	NA

1/ Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

2/ The authorities provide some balance sheet items but not comprehensive enough for proper financial stability analysis.

3/ Both market-based and officially determined, including discount rates, money market rates, and rates on treasury bills, notes, and bonds.

4/ Foreign, domestic bank, and domestic nonbank financing.

5/ The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

6/ Including currency and maturity composition.



INTERNATIONAL MONETARY FUND



Press Release No. 13/407  
FOR IMMEDIATE RELEASE  
October 17, 2013

International Monetary Fund  
Washington, D.C. 20431 USA

### **IMF Executive Board Concludes 2013 Article IV Consultation with the Federal Democratic Republic of Ethiopia**

On September 18, 2013, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Federal Democratic Republic of Ethiopia.<sup>1</sup>

Recent macroeconomic developments are encouraging, with a significant deceleration in inflation and continued robust economic growth. Despite significant decline in coffee prices and supply bottlenecks, growth remains robust, supported by better agriculture output and construction and other services activities. Inflation declined from the peak of 40 percent in July 2011 to around 7 percent in June 2013. This has significantly eased the extent to which real interest rates were negative. Pressures resulting in foreign exchange shortages in the wake of the passing away of Prime Minister Meles have eased.

Fiscal policy at the general government level remains prudent, with cautious execution of the government budget. Overall revenue-to-GDP ratio is estimated to fall from 14 percent in 2011/12 to 13.2 percent in 2012/13. Reflecting the strong pro-poor focus, the ratio of poverty-reducing expenditure to GDP is being maintained and non-priority expenditure will likely be compressed in 2012/13. The government budget deficit, including grants, is estimated to be 2.8 percent of GDP.

Overall fiscal stance for the consolidated public sector (including public enterprises) is likely considerably more expansionary. While appropriately consolidated data on the overall public sector finances are not available, external financing of public enterprises in 2012/13 and the monetary survey suggest that overall public sector (including public enterprises) borrowing exceeded 9 percent of GDP in 2012/13.

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<sup>1</sup> Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: <http://www.imf.org/external/np/sec/misc/qualifiers.htm>.

Although the monetary stance remains generally tight to keep inflation in single digits, recent developments point to some relaxation. Base money contracted by 4 percent in 2011/12, but by end-May 2013 expanded by 18 percent at an annual rate. The authorities adjusted slightly the base money target for the year to 13 percent from 12.2 percent. Achieving the 13 percent target implies a very tight monetary policy for the remainder of the fiscal year. The reserve requirement ratio has been further lowered recently (March 2013) from 10 percent to 5 percent, following an earlier (January 2012) lowering by 5 percentage points, and the National Bank of Ethiopia (NBE) sterilized the resulting liquidity injection through the sale of certificate deposits. Broad money growth remains on the high side and was 28 percent in 2012/13.

The external current account deficit widened slightly to US\$3 billion in 2012/13 from US\$2.8 billion in 2011/12, reflecting a weaker trade balance, although it improved as a ratio of GDP from 6.6 percent to 6.4 percent. Export performance suffered from a decline in prices and weak external demand conditions, growing only 3.2 percent (in nominal terms), while continued infrastructure and industrial investment and higher fuel importation contributed to an increase in imports by 6.3 percent. Transfers brought in a net inflow of around US\$5 billion due to a surge in net private transfers that more than offset a decline in official transfers. Increased loan disbursements to the central government and public enterprises yielded a capital account surplus of US\$3.4 billion. The NBE's gross international reserves declined slightly to US\$2.2 billion (1.8 months of imports) at the end of 2012/13 from US\$2.3 billion (1.9 months of imports) at the end of 2011/12.

Foreign exchange supply came under pressure in the first half of 2012/13. The passing of Prime Minister Meles created uncertainty and excess demand in the foreign exchange market which was also reflected in a widening of the premium in the parallel market. Since its previous peak in October 2008, the Real Effective Exchange Rate (REER) reached the highest level in November 2012, although this has started to turn around with the recent decline in inflation.

### **Executive Board Assessment**

Executive Directors commended the authorities for the Federal Democratic Republic of Ethiopia's strong growth performance and impressive progress in decreasing poverty and inequality under the Growth and Transformation Plan (GTP). Prudent macroeconomic management has ensured a significant deceleration in inflation. Going forward, Directors agreed that the Federal Democratic Republic of Ethiopia's public-sector-led strategy needs to be recalibrated, with greater participation by the private sector to sustain robust and inclusive growth and mitigate vulnerabilities. They emphasized the importance of policies to maintain fiscal sustainability, preserve low inflation, rebuild external buffers, and improve financial intermediation and the business environment.

Directors welcomed the authorities' prudent budgetary stance, but underscored the need to gain a fuller picture of public enterprises' finances and to pace public investments appropriately. Sustaining pro-poor expenditures will require increased domestic revenue, and Directors therefore encouraged the authorities to continue the momentum of revenue administration and tax policy reforms. Further public financial management reforms as well as a medium-term debt management strategy would also help maintain fiscal sustainability and achieve the fiscal objectives under the GTP.

Directors agreed that a continued cautious monetary stance is warranted to preserve low inflation. They underscored the importance of improving the efficiency and flexibility of monetary policy instruments, including through greater flexibility of nominal interest rates and the development of market-based liquidity management. Directors called for better coordination between exchange rate and monetary policies and for greater exchange rate flexibility to help reconstitute foreign exchange reserves, strengthen competitiveness, and eliminate the spread between the parallel and official rates.

Directors noted that the banking sector remains well-capitalized and profitable. They stressed the need to carefully monitor concentration of large exposures to single entities, and for strengthened capacity to ensure effective financial sector supervision and regulation. Directors encouraged policies to improve the private sector's access to finance and promote financial inclusion. In particular, phasing out the directive requiring commercial banks to hold low-yield central bank bills would facilitate financial deepening. They also encouraged the authorities to address the remaining deficiencies in the Anti-Money Laundering/Combating the Financing of Terrorism regime.

Directors underscored the transformational power of the private sector, which can be further harnessed to generate employment and sustain development. Accordingly, they advised the authorities to enhance competitiveness and attract Foreign Direct Investment by improving the business climate and fostering competition.

Directors acknowledged recent improvements in GDP statistics. They encouraged the authorities to make further efforts to improve data quality, particularly financial sector, fiscal and balance-of-payments statistics, with support from the International Monetary Fund technical assistance.

Ethiopia: Selected Economic and Financial Indicators, 2010/11–2012/13 <sup>1</sup>

	2010/11	2011/12	2012/13 Est.
	(Annual percentage change)		
National income and prices			
GDP at constant prices (at factor cost)	11.4	8.5	7.0
Consumer prices (period average)	20.0	34.2	11.3
Consumer prices (end period)	18.1	34.1	13.5
External sector			
Exports, (In U.S. dollars, f.o.b.)	37.1	14.8	3.2
Imports, (In U.S. dollars, c.i.f.)	-0.2	34.0	6.3
Export volume	8.9	-0.4	14.0
Import volume	-3.8	25.9	6.8
Terms of trade (deterioration - )	23.5	8.2	-10.3
	(Percent of beginning-period stock of broad money, unless otherwise indicated)		
Money and credit			
Net foreign assets	29.1	-12.7	2.2
Net domestic assets	10.1	43.0	26.4
Net claims on the government	-2.9	-7.0	3.2
Net claims on public enterprises	25.1	28.5	20.2
Net claims on private sector	9.8	13.2	4.4
Broad money	39.2	30.3	28.5
Velocity (GDP/broad money)	3.49	3.90	3.62
	(In percent of GDP, unless otherwise indicated)		
Financial balances			
Gross domestic saving	12.8	16.5	15.9
Government saving	4.3	5.7	4.9
Private saving	8.5	10.8	11.0
Gross domestic investment	27.2	34.6	32.6
Public investment	19.6	26.5	24.3
Private investment	7.5	8.1	8.3
Resource gap	-14.4	-18.1	-16.7
External current account balance, including official transfers	-0.7	-6.6	-6.4
Government finances			
Revenue	13.7	14.0	13.2
External grants	3.3	1.7	2.0
Expenditure and net lending	18.5	16.9	18.0
Fiscal balance, excluding grants (cash basis)	-4.9	-2.9	-4.8
Fiscal balance, including grants (cash basis)	-1.6	-1.2	-2.8
Total financing	1.6	1.2	2.8
External financing	1.5	0.9	1.3
Domestic financing (not including privatization)	0.0	0.5	1.5
Public debt <sup>2</sup>	37.8	32.8	38.6
Domestic debt	15.6	14.9	19.7
External debt (including to IMF)	22.2	17.9	18.9
Present value of external public and publicly guaranteed (PPG) debt-to-exports ratio (including to Fund) <sup>2</sup>	103.7	104.5	122.1
External PPG debt-service-to-exports ratio <sup>3</sup>	2.9	4.9	5.8
Overall balance of payments (in millions of U.S. dollars)	1446	-1067	189
Gross official reserves (in millions of U.S. dollars)	3,044	2,262	2,218
(in months of imports of goods and nonfactor services of following year)	2.7	1.9	1.8
GDP at current market prices (in billions of birr)	506.1	736.6	877.5

Sources: Ethiopian authorities; and IMF staff estimates and projections.

<sup>1</sup> Data pertain to the Ethiopian fiscal year from July 8 to July 7.

<sup>2</sup> Including debt of major public enterprises.

<sup>3</sup> After enhanced HIPC and MDRI relief.

**STATEMENT BY MR. SAHO, EXECUTIVE DIRECTOR FOR  
THE FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA  
SEPTEMBER 18, 2013**

The Ethiopian economy has performed remarkably well in the past decade. GDP growth has averaged over 11 percent, resulting in a significant drop in poverty. The realization of the macroeconomic objectives of the Growth and Transformation Plan (GTP) is anchored under three pillars: inclusive growth; public investment and structural transformation; prudent fiscal and monetary management. Overall, the income gap has narrowed significantly, economic wellbeing has risen substantially and the Gini index now stands at 33.6.

My Ethiopian authorities appreciate the discussions they had with International Monetary Fund (IMF) staff during the 2013 Article IV consultation. They value the exchange of views on key policy issues aimed at supporting the continued implementation of the GTP, while addressing any potential risks and challenges. My authorities remain confident that by persevering with the current macroeconomic framework, they stand a good chance of mitigating risks associated with a renewed slowdown in the global economic recovery. While they consider the quality of staff policy advice as useful, nevertheless, they do not share some of the conclusions reached by staff as expressed below.

**I. BACKGROUND**

The Government of Ethiopia has been working for the past seven years establishing the protection of basic services program in collaboration with the World Bank (WB), the African Development Bank, European Union and other development partners, which are active in the country. The program aims at sustaining basic services such as water, health, roads and agricultural extension development projects in all regions of the country. Since the inception of the program, Ethiopia has made impressive progress in ensuring rapid and quality basic services for the majority of the population and these efforts are expected to help and support Ethiopia meet the Millennium Development Goals (MDGs).

In addition, the government has critically evaluated both external and internal conditions in setting the growth targets in the GTP, which is mainly driven by the agriculture sector. Through significant investment in agriculture, my authorities aim to modernize the sector and insulate it from recurring drought shocks. Spending priorities remain geared towards the poor and there is substantial investment in public infrastructure.

The high growth of the last several years has been accompanied by a halving of the proportion of the population living below the poverty line, from 60.5 percent in 1995 to 30.7 percent in 2011. Other indicators of living standards, such as literacy rate, labor participation rates have also shown significant improvements. However, the significant progress towards the MDGs has so far failed to generate adequate employment opportunities, particularly for the youth. As a result my authorities are focused on reducing unemployment in the urban and rural areas. To this end, the five-year GTP, which aims to foster high and



broad-based growth, is expected to expand employment opportunities by emphasizing the development of small and medium-scale industries.

My authorities are committed to enhance the participation of the private sector in growing the economy. Cognizant of the role of the private sector as a key player in the development process, the government continues to formulate policies to ensure that the private sector emerges as a central player in the future development of the country. The currently high infrastructure developments and service delivery improvement by the government is geared towards opening opportunities and creating an enabling environment for the active participation of the private sector.

## **II. MACROECONOMIC DEVELOPMENTS AND OUTLOOK**

The growth momentum continues albeit at a slower rate. GDP is estimated at 8.5 percent for 2011/12, lower than the expected 11 percent due to poor performance in agriculture. My authorities expect growth to rebound to 11.3 percent in 2012/13 as the agriculture sector recovers. The tight monetary policy stance, aided by slowdown in food and fuel price inflation, saw consumer price inflation decelerating to 7 percent year-on-year in August 2013. Food price inflation eased to 3.8 percent in August, down from 5.8 percent in July, while non-food inflation rate edged higher to 10.8 percent from 10.5 percent in July.

Vigorous policy implementation by my authorities has enabled Ethiopia to make significant advances in meeting the key challenge of low international reserves while sustaining the high growth rate and development momentum. Nevertheless, going forward my authorities will continue to adjust their policies, including the growth in reserve money to ensure macroeconomic stability. My authorities recognize that inflation, despite the significant decline recently, remains a concern as it could quickly pose a challenge to their plan to sustain the current real growth momentum.

The government's determination to hold down prices was further reflected in its prudent fiscal policy focusing on strengthening domestic resources and reducing domestic borrowing. Fiscal policy remains geared towards maintaining the level of spending on the key MDGs clusters and infrastructure while conforming to the overall macroeconomic framework. To protect spending in priority areas, my authorities will continue to strengthen domestic and concessional resource mobilization in the medium term. They are committed to improving domestic revenue mobilization and are appreciative of the continued IMF technical assistance (TA) in this area. Given the overall resource limitations, my authorities intend to facilitate greater participation of the private sector and mobilize a modest level of non-concessional financing while remaining vigilant of the contingent liabilities and debt sustainability implications and strengthening their debt management strategy. The joint debt sustainability analysis undertaken by the IMF and WB staffs reaffirms that the level of debt distress will not worsen. My authorities also recognize the important role played by the public enterprises, particularly in the improvement of infrastructure critical to socio-economic development.

### **III. DATA ISSUES**

The authorities have noted the need to further improve the quality and reliability of the macroeconomic data. However, they note that the revised lower GDP number for 2011/12 was primarily due to the less than expected growth in agriculture (4.9 percent), in contrast to growth in the previous years (7.6 percent in 2009/10 and 9.0 percent in 2010/11) rather than the change in methodology following TA on national accounts from the IMF. In fact the March 2010 IMF Statistics Department mission's report states that, "some of the weakness noted .... are not unique to Ethiopia. In fact, the compilation system compares quite favorably with the system of other countries in the region..." is implying that the weaknesses are not unique to Ethiopia and that the country is relatively well positioned in terms of the quality of statistics in SSA. My authorities agree on the need expressed in the staff report for continued improvement of National Accounts Statistics (NAS) compilation methodology and have started implementation of NAS improvement and capacity building action plan to identify weaknesses and incorporate improvements in the compilation process on an ongoing basis.

In an effort to improve the national accounts statistics, my authorities have recruited a resident international expert for one year to help improve estimation methodology and build the capacity of NAS compilers. In addition, they have benefited from the expertise of an IMF East AFRITAC expert to further improve the methodology. Going forward, they expect TA from IMF East AFRITAC to improve GDP - Expenditure estimation would help further and express their commitment to keep on improving NAS compilation on an ongoing basis.

### **IV. AML/CFT**

With regard to AML/CFT, Ethiopia has recently taken significant steps towards improving the AML/CTF regime, including enacting a law that criminalizes money laundering and the financing of terrorism. The authorities are addressing the deficiencies in their action plan vis-à-vis international standards with the help of consultants from the WB. They expect the Financial Action Task Force to review and remove Ethiopia from the list of jurisdictions with strategic AML/CFT deficiencies.

### **V. CONCLUSION**

My authorities will continue to focus on sustaining macroeconomic stability, enhancing domestic resource mobilization, promoting broad-based and pro-poor growth, and increasing investment in infrastructure, primary sectors and core MDG clusters. They intend to be vigilant and continue adjusting their economic policies and programs in the near term to meet the emerging challenges and maintain macroeconomic stability while at the same time maintaining their focus on the long-term development objectives of poverty reduction, sustaining the growth momentum and closing the infrastructure gap in line with the GTP. Going forward, they will continue to consult with the IMF and seek the support of development partners in order to achieve Ethiopia's development goals.