Ethiopia
Macroeconomic Handbook 2020

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Macroeconomic Handbook 2020

Macro Research Ethiopia

As 2020 unfolds, Ethiopia's political calendar is bringing an uncertain and unsettled environment to the economic outlook for the coming year. Amid this state of affairs, we decided to take stock of the many positive developments and hopeful trends emerging in Ethiopia's macroeconomic environment at the start of the year. While recognizing key risks, this note focuses on the wide range of recent reforms and upcoming initiatives whose significance is often fast forgotten or inadequately appreciated. Beyond highlighting what we see as the economy's bright spots, we present also our latest Quarterly Macroeconomic Review and our economic forecasts—covering the real, monetary, fiscal, and external sectors—for 2020 and 2021.

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1. **A Major Threshold Crossed**: Ethiopia's per capita income passes $1,000 this year.
2. **Development Policy**: Not all State and not all Market… as it should be.
3. **Macroeconomic Policy**: Now more disciplined, more coherent, and more transparent.
4. **Government and State Enterprise Finances**: Putting a proper price on borrowed money.
5. **Investment in the economy**: Some sub-components are stalling but still high levels overall.
6. **Credit to the Private Sector**: At record levels—and the types and terms are improving.
7. **Multilateral and Bilateral Partners**: Ethiopia is now on top of most priority lists.
8. **Privatization**: Inflows will start in 2020, and should exceed $5 billion within three years.
9. **Exchange Rate and FX Supplies**: A realistic rate for the Birr not yet in place, but is on the horizon.
10. **Financial Sector Reforms** : A slow start so far, but prospects look good for 2020 and 2021.

Ethiopia Macroeconomic Handbook 2020—EXECUTIVE SUMMARY

1. A Major Threshold Crossed: Ethiopia's per capita income has just crossed $1,000 this year, based on an expected US dollar GDP of $109.5bn for FY 2019-20 (3,422bn in Birr terms) and a population count—per official statistics—of just above 100 million. In PPP terms, average incomes have reached $2,750 per capita. With the rise in incomes, total consumer spending ($66bn) is now fourth highest in absolute terms in Sub-Saharan Africa. And focusing just on urban consumers, their aggregate spending is near Birr 450bn ($16bn), by our estimates, which is propelling demand for fast-moving consumer goods, housing, transport, and a range of domestic services. Taking a cross-country perspective and reviewing the record of other countries that crossed $1,000 in per capita income (this occurred just 19 years ago in China, 13 years ago in India/Vietnam, and 7 years ago in Bangladesh/Kenya), we see that growth can continue at its recent pace as long as it is supported by high investment, and that Ethiopia could reach a $2,000 per capita income (~$5,100 per capita in PPP terms) within the space of seven years.

2. Development Policy: Current economic reforms are being viewed by some as a major shift towards neo-liberal, free-market policies and yet by others as still reflecting state-led and state-dominated policies. Neither perspective fully captures the reality, in our view, and policies seem to us to be moving (appropriately) towards a mixed and pragmatic approach that seeks to put in place both a strong state and a strong private sector. We think the economy will—for the foreseeable future—show four main economic actors each having over-sized roles in their specific spheres: government and state enterprises continuing to deliver most public goods; a dominant state bank providing the lion's share of credit (though increasingly serving private sector clients and doing so alongside a growing pool of private banks); a growing domestic private sector—both SMEs and corporates—active primarily in agriculture, trading, services, and construction; and a foreign private sector increasingly dominant in large-scale manufacturing, industrial exports, mining, and specialized agricultural and agro-processing ventures.

3. Macroeconomic Policy: With a well-articulated 'Homegrown Economic Reform Plan' in place alongside the support of an IMF financing arrangement, macroeconomic policies in 2020 will be the most disciplined, coherent, and transparent seen in years. The recent start of WTO entry negotiations—and an expected accession next year—will further help put in place rules-based and predictable economic and financial policies. On macro policies, tighter discipline is evident from stricter financial controls now governing not just the government but also—as important—the central bank and state enterprises. More coordination is being seen with tighter fiscal policies, monetary restraint, and a faster pace of exchange rate adjustment all working in parallel to (temporarily) restrain aggregate demand—while being supplemented with structural and sector-specific reforms to boost longer-term supply responses. And in terms of transparency, a range of economic policy commitments are being disclosed for greater awareness by the public, private sector, and foreign investors (per, for example, the 23 specific actions laid out in the Finance Minister and Governor's recent Memorandum of Economic and Financial Policies).

4. Government and State Enterprise Finances: For the first time in decades, the Government is moving away from funding itself almost exclusively via cheap and 'captive' sources and beginning to borrow at rates that better reflect the true cost of credit. Market-based T-Bills launched at end-2019 have—in just three months—already provided nearly Birr 3bn in funding (from private banks) and interest rates have moved upwards to 7-8 percent (similar to savings deposits) versus the rates of 1-2 percent prevalent before. While this move is of course more costly for government, the greater resort to market-based T-Bills will help impose a hard budget constraint and is significant in laying the foundation for the establishment of broader (private) debt and capital markets.

5. Investment in the economy: Despite a slowdown in some sub-components, investment remains at a high 35 percent of GDP per official FY 2018-19 data. The recent slowdown in FDI—per BOP data—has not brought down overall investment levels given the still limited share of FDI in total investment (~10 percent) and an offset provided from domestic private investors. Seen from a five-year perspective, two positive trend lines remain in place: there is a rising share of *private* investment and an increasing reliance on *domestic savings*. Looking ahead, FDI should recover in 2021 (given privatization inflows and assuming a stable political transition) and will also likely show an increasingly broadening base in terms of targeted sectors (thanks to the opening of previously restricted sectors).

6. Credit to the private sector: Loans provided to the private sector passed Birr 320bn last year—a historic high in nominal terms and the highest share relative to GDP seen in five years. The recent decision to end NBE Bills should boost credit supplies to the private sector even further. Credit to the private sector is not just growing in size, but also improving in the types and terms of loans becoming available.

7. Multilateral and Bilateral Partners: Reflecting a range of internal reforms, Ethiopia's engagement with a wide range of official multilateral and bilateral partners is currently at its closest level seen in many years. The enhanced support of official external partners will add up to around $4bn, or 4% of GDP, annually if including grants, low-interest loans, and debt rescheduling. Such official external support is supplemented by large private sector inflows including remittances from the diaspora (~$6bn annually) and foreign investment (~$3-$4bn). Taken together, these external financing flows are making possible investment levels (~35% of GDP) that are well beyond available domestic savings (24% of GDP).

8. Privatization: Though almost two years have passed since the announcement of the recent round of privatization, 2020 should be the first year that sales transactions take place and fx inflows of as much as $5bn-$7bn are possible over the course of three years, in our view. Fx inflows from privatization may not all be available for government use (as some portion may be used to repay external debt), but this will still improve the country's net external position and enable the concerned enterprises to return to financial health. Beyond just the financial gains involved, privatization should—with the right safeguards—bring positive spillovers to the operating environment of technology dependent businesses and of a range of domestic services such as logistics and distribution.

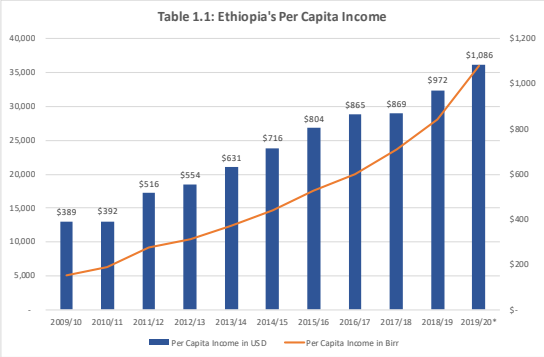
9. Exchange Rate and Fx Supplies: The faster pace of exchange rate adjustment put in place since end-2019 is a very positive step that signals a clear intention to address Ethiopia's long-standing fx challenges. With this change, the gap between the official and parallel market rate has fallen, though it remains substantial (around 25 percent). Somewhat unexpectedly, the IMF program has not been used as a framework to make a more immediate adjustment of the Birr towards its market rate, but it is still possible that meaningful exchange rate reform could be forthcoming in the near-term since a roadmap to review and revise fx policies is promised by April 2020.

10. Financial Sector Reforms: Reforms enacted over the past year are beginning to address many of the past bottlenecks seen in the financial sector—including its small overall size relative to the economy (just ~33% GDP), its lopsided allocation of credit (two-thirds going to the public sector), and its limited menu of service offerings suited to the needs of local borrowers (in terms of cost, collateral, instruments, and maturity). While still in the early stages, reforms to date are helping boost private credit supply, reduce borrowing costs, and ease collateral requirements. Looking ahead, 2021 should mark the start of some limited private debt and equity markets as well as the emergence of new financial institutions (including non-banks) specialized in fin-tech offerings, Islamic banking, leasing, SME financing, mortgage loans, and agricultural credit—all of which should gradually broaden the volume, mix, instruments, pricing, and terms of funding available within Ethiopia's fast-expanding financial sector.

1. **A Major Threshold Crossed**: **Ethiopia's per capita income passes $1,000 this year.**

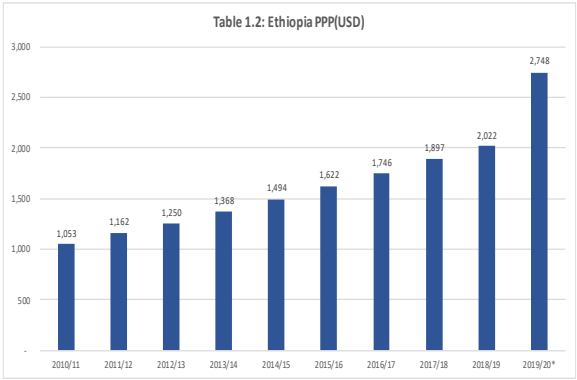
Ethiopia's per capita income has crossed $1,000 as of early 2020, based on this year's expected US dollar GDP of $109.5bn (3,422bn in Birr terms) and a population count—per official statistics—of just above 100 million (Table 1.1). Accounting for the lower average cost of goods in Ethiopia compared to other countries, incomes on a Purchasing Power Parity (PPP) basis are—by our estimates—$2,748 per capita this year (Table 1.2). The doubling of per capita income to $1,000 has taken almost eight years, given that Ethiopia's per capita income was $554 as recently as 2012-13.

Table 1.1: Ethiopia's Per Capita Income: A Ten-Year Overview



Source: NBE for historical data, and Cepheus Research for FY2019-20 USD GDP projection. Population figure is 100,802,000 for 2020, based on official CSA projections under the Medium-Case Population Growth Scenario (See ICPS document on CSA website) Given USD GDP projected, the $1,000 per capita threshold is crossed even if Ethiopia's population is as high as 109.5mn in 2020.

Table 1.2: Ethiopia Per Capita Income in Purchasing Power Parity PPP Terms, (USD)



Source: IMF WEO and Cepheus Research for FY2019-20 projection

Focusing just on urban Ethiopia, median per capita incomes are roughly two-and-a-half times the nation-wide average or near $2,500 per year by our estimate (Table 1.3). In PPP terms, average urban incomes would be closer to $6,400 per year or $530 per month. This average urban per capita figure is more representative of the income of the roughly 20 percent of the population (around 20 million people), now living in urban areas per national statistics.

Table 1.3 Urban Income Indicators--Representative Salaries for Positions with Large Employment in Urban Areas

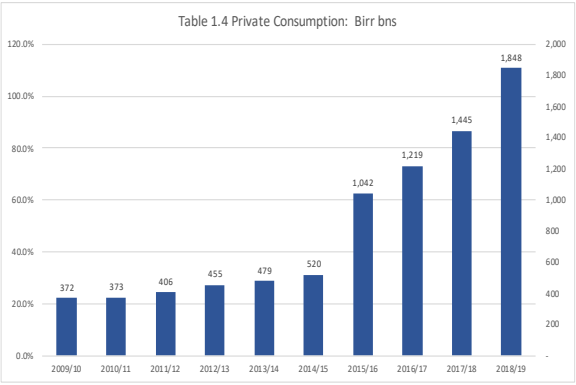
	Ten Common Jobs with High Employee Numbers	Birr/month	Birr/Year		USD/Year		USD/Year in PPP terms
1	Security guards	1,500	18,000	$	563	$	1,423
2	Daily laborers	2,600	31,200	$	975	$	2,467
3	Retail workers	3,000	36,000	$	1,125	$	2,846
4	Police force members	4,000	48,000	$	1,500	$	3,795
5	Teachers at public schools	4,500	54,000	$	1,688	$	4,269
6	Civil servants--front line staff	5,000	60,000	$	1,875	$	4,744
7	Nurses and health workers	6,000	72,000	$	2,250	$	5,693
8	Bank Clerks	9,500	114,000	$	3,563	$	9,013
9	Office workers	11,000	132,000	$	4,125	$	10,436
10	Senior professionals	20,000	240,000	$	7,500	$	18,975
	Average of the ten *common* urban job positions:	**6,710**	**80,520**	**$**	**2,516**	**$**	**6,366**

Source: Cepheus market review of average salaries for occupations with large urban employment; inputs provided by Premier HR and Investment Consultants.

Reflecting many consecutive years of rising nominal incomes, the aggregate value of private sector consumption in the economy passed Birr 1,848bn ($66bn) last year (Table 1.4).

This figure reflects—and is derived from—total national disposable income reaching Birr 2,924 billion in 2018-19 (GDP of Birr 2,696bn plus transfers from abroad of Birr 240bn), of which Birr 949bn went into investment, Birr 247bn represented government consumption, and the residual Birr 1,848bn (nearly 70 percent of GDP) was private sector consumption (Table 1.5). At roughly $66bn in dollar terms, the size of private sector consumption in Ethiopia ranks fourth place in sub-Saharan African, behind only the levels seen in Nigeria, South Africa, and Kenya (Table 1.6). This figure effectively represents the aggregate purchasing power of private households on an annual basis, and is a close proxy of total consumer spending in the economy.

Table 1.4 Private Consumption(Birr bns)



Source: MoFEC

Table 1.5: GDP and Private Consumption Data, FY 2018-19:

	Birr billions	% GDP
Gross Domestic Product	**2,696**	**100.0%**
Plus: Net income from abroad	(13)	-0.5%
Gross National Product	**2,683**	**99.5%**
Plus: Transfers from abroad	240	8.9%
Gross Disposable income	**2,923**	**108.4%**
Of which, spent on:		
Investment (gross capital formation)	949	35.2%
Government Consumption	247	9.2%
Private Consumption	1,848	68.5%

Source: MoFEC

Table 1.6: GDP Level and Private Consumption share in Top 10 Sub-Saharan African Economies by GDP

Ranked by private consumption in USD terms

	Country	GDP in USD billions	Private Cons-to-GDP	USD value of Private Consumption
1	Nigeria	445.0	76.6%	$ 340.9
2	South Africa	371.0	58.8%	$ 218.1
3	Kenya	99.0	81.0%	$ 80.1
4	**Ethiopia**	**96.0**	**68.5%**	**$ 65.8**
5	Angola	92.0	57.1%	$ 52.5
6	Ghana	68.0	72.0%	$ 49.0
7	Tanzania	61.0	59.4%	$ 36.2
8	DR Congo	48.0	71.6%	$ 34.4
9	Cameron	39.0	81.6%	$ 31.8
10	Cote d'ivoire	45.0	55.6%	$ 25.0

Source: MOFEC (for Ethiopian GDP and private consumption share data) and CEIC (for all other countries)

With respect to just the urban component of private sector consumption, we estimate that the aggregate spending of urban consumers is now close to Birr 450bn ($16bn) per year. This estimate reflects an average of two approaches, namely: (1) taking a 23 percent of total nation-wide private consumption (slightly above the urban population share), and (2) multiplying average estimated urban per capita incomes with the urban population figure. The average of the two approaches yields a figure of around Birr 450bn ($16bn). In terms of the breakdown of this figure for urban purchasing power, the composition of the consumer price index (meant to represent the consumption patterns of the average urban citizen) offers reasonably good guidance as to the broad categories of private expenditure—indicating, for example, that the typical urban Ethiopian spends 41 percent of his/her income on food, 23 percent for home rent/expenses, 6 percent for transport, 6 percent for clothing/footwear, 5 percent for communications, and around 2 percent each for categories such as education, medical care, and beverages. On this basis, we can estimate that, of the Birr 450bn in urban purchasing power, roughly Birr 186bn ($6.6bn) was spent on food items, Birr 105bn ($3.7bn) on home rent and furnishings, Birr 26bn ($1bn) on transport services, Birr 26bn ($0.9bn) on clothing and footwear amounts of near Birr 9bn ($0.3bn) each on education and medical care education. A tabulation of these estimated urban consumption aggregates—and implied market size—for the over two dozen main goods and services that make up the CPI index is provided below (Table 1.7).

Table 1.7 Urban Consumption Estimates for 2018-19

Category	Weight	Brr mns		USD mns
Total Urban Consumption Estimate	**...**	**456,809**	**$**	**16,245**
Food	**40.8%**	**186,185**	**$**	**6,621**
Cereals (teff, wheat, maize, etc.)	9.1%	41,429	$	1,473
Meat	7.0%	31,986	$	1,137
Vegetables, leaves, roots and tubers	4.3%	19,535	$	695
Oils and fats(including edible oil)	3.7%	17,103	$	608
Peas and Lentils	3.7%	17,023	$	605
Salt and Spices	2.2%	10,173	$	362
Bread	2.0%	9,265	$	329
Injera	1.9%	8,570	$	305
Milk and eggs	1.8%	8,121	$	289
Sugar	0.9%	4,137	$	147
Chicken	0.9%	4,044	$	144
Pasta & Macaroni	0.9%	4,021	$	143
Potatoes, other tubers and Stems	0.8%	3,752	$	133
Pulses and beans	0.6%	2,901	$	103
Fruits	0.4%	1,994	$	71
Cereals preparation (wheat flour)	0.4%	1,917	$	68
Fish	0.0%	213	$	8
Beverages	**2.4%**	**11,074**	**$**	**394**
Coffee and Tea	1.6%	7,442	$	265
Mineral water	0.8%	3,632	$	129
Alcoholic beverages and tobacco	**1.4%**	6,389	$	227
Alcoholic beverages	1.1%	5,094	$	181
Chat	0.2%	1,028	$	37
Cigarettes and Tobacco	0.1%	267	$	10
Clothing and foot wear	**5.6%**	**25,605**	**$**	**911**
Clothing	3.8%	17,265	$	614
Food wear	1.8%	8,340	$	297
Home related & furnishing	**23.0%**	**104,900**	**$**	**3,730**
Rent	10.0%	45,551	$	1,620
Household furnishing	6.6%	30,119	$	1,071
Solid fuels(Charcoal, candles etc.)	3.2%	14,550	$	517
Electricity	1.8%	8,005	$	285
Water Charges	0.6%	2,842	$	101
maintenance	0.6%	2,619	$	93
Kerosene	0.3%	1,214	$	43
Services	**26.9%**	**122,657**	**$**	**4,362**
Restaurants	7.5%	34,332	$	1,221
Transport	5.7%	26,136	$	929
Communication	5.4%	24,761	$	881
Miscellaneous	3.7%	16,862	$	600
Medical care	2.0%	9,227	$	328
Education	1.5%	7,035	$	250
Entertainment	0.9%	4,305	$	153

Source: Cepheus Research estimates. Total urban consumption expenditure based on average of two approaches: (1) Urban share taken as 22% of national private consumption, and (2) estimated urban income from wage and non-wage sources multiplied by urban population. Breakdown of spending items is based on the composition of CPI index for Addis Abeba.

Crossing $1,000 in per capita income: what do other country experiences tell us?

Ethiopia's timing—how far behind? Looking at the timing of when some comparator countries crossed $1,000 in per capita income, one finds that this occurred in 1977 for a country such as South Korea that showed one of the fastest and sustained growth records in recent history. However, for many other countries (including potential economic 'models' for Ethiopia), the $1,000 threshold was crossed not that long ago: it occurred in 2001 in China, in 2007 in Vietnam and India, in 2011 in Kenya, and in 2013 in Bangladesh. Indeed, based only on this (simplistic) metric, Ethiopia is just 19 years behind China, 13 years behind both Vietnam and India, 9 years behind Kenya, and 7 years behind Bangladesh (Table 1.8).

Table 1.8: Year when Per Capita Income of $1,000 was reached:

	Year when country crossed $1,000 per capita income	No of Years Ethiopia is behind other countries
Ethiopia	2020	...
South Korea	1977	43
Morocco	1988	32
Indonesia	1995	25
Egypt	1995	25
China	2001	19
Philippines	2002	18
Vietnam	2007	13
India	2007	13
Kenya	2011	9
Bangladesh	2013	7

Source: IMF WEO data and Cepheus Research compilation

Cross-country comparisons—macro conditions after crossing $1,000: Comparing key macro conditions of comparator countries in the five years before and after crossing $1,000, we note that growth rates often remained roughly unchanged (growth was 6.4/6.0 percent in the five years before/after for the comparator countries), investment rates tend to rise relative to GDP (by about 4 percentage points of GDP), inflation rates drop somewhat (towards 7 percent—though they were already low to begin with in other countries), export levels jump by a few percentage points of GDP (to 32 percent of GDP) and the structure of the economy moves markedly away from agriculture and towards services (Table 1.9). Though these need not be seen as deterministic outcomes, if Ethiopia were to follow these patterns, we can anticipate continued strong growth supported by high investment, lower inflation, a rising export-to-GDP share, and a structural shift in the sectoral make-up the economy.

Table 1.9: Macro Conditions Before and After Reaching a Per Capita Income of $1,000

	Five Years BEFORE Reaching $1,000 Per Capita Income										
	Ethiopia	China	Vietnam	South Korea	Indonesia	Bangladesh	Morocco	Egypt	India	Philippines	Kenya
Growth (Percent)	9.3	9.1	7.1	10.5	8.5	5.9	4.6	3.6	7.1	3.0	5.1
Inflation (Percent)	10.0	5.1	6.1	16.0	7.0	8.0	7.6	14.1	4.4	6.0	12.7
Investment/GDP (Percent)	37.4	37.0	34.5	27.3	39.1	26.9	28.1	22.5	34.0	21.5	19.8
Exports of goods & services-$bn	6.38	150.14	31.00	9.34	87.88	22.16	3.36	11.16	123.87	30.56	7.53
Exports/GDP (Percent)	9.1	18.4	60.5	22.2	24.5	18.1	23.7	24.9	17.6	47.3	21.7
Ext Debt/GDP (Percent)	20.8	14.8	35.3	-	-	23.3	94.0	73.4	17.9	71.0	23.2
Agriculture/GDP (Percent)	37.5	18.0	21.1	24.4	6.5	16.9	13.1	16.5	18.3	15.2	22.3
Services/GDP (Percent)	21.1	35.6	39.9	40.7	48.4	53.2	47.0	47.9	44.4	51.1	49.6
Industry/GDP (Percent)	42.3	46.4	39.0	26.4	35.7	25.1	29.4	30.5	29.0	33.7	18.9
	Five Years AFTER Reaching $1,000 Per Capita Income										
	Ethiopia	China	Vietnam	South Korea	Indonesia	Bangladesh	Morocco	Egypt	India	Philippines	Kenya
Growth (Percent)	...	9.80	5.79	6.63	5.66	6.98	2.13	5.70	6.03	5.66	5.48
Inflation (Percent)	...	1.34	13.36	18.00	3.99	5.99	5.79	4.29	9.88	4.40	6.97
Investment/GDP (Percent)	...	39.68	33.27	34.36	33.75	29.77	28.57	19.67	39.22	20.30	20.75
Exports of goods & services-$bn	...	456.06	88.47	20.79	166.26	37.81	5.96	14.62	360.84	36.73	10.79
Exports/GDP (Percent)	...	26.97	72.87	26.83	32.64	16.56	22.73	17.41	23.19	46.34	18.27
Ext Debt/GDP (Percent)	...	12.76	35.13	-	-	18.63	74.85	37.30	19.04	57.08	27.67
Agriculture/GDP (Percent)	...	12.84	19.35	16.24	4.41	14.13	14.81	15.84	16.92	12.71	28.27
Services/GDP (Percent)	...	41.60	39.38	41.94	51.37	53.49	45.61	47.65	45.73	53.55	47.03
Industry/GDP (Percent)	...	45.56	34.48	30.83	34.50	27.36	26.76	29.26	30.51	33.74	17.85

Source: World Development Indicators and Cepheus Research Compilation

Cross-country comparisons—how fast to even higher incomes? Looking at the income record of comparator countries once they crossed $1,000 in per capita income reveals that they doubled average incomes—to $2,000—in an average of 10 years (Table 1.10). Were this to serve as a benchmark, we should expect Ethiopia to see a doubling of per capita income to $2,000 in ten years, or by 2029-30. However, as Ethiopia is currently growing roughly one-and-a-half times the average growth of the comparable countries when they reached $1,000 in per capita income (9 percent vs 6 percent), Ethiopia could reach $2,000 at an even faster pace. Indeed, under a set of some plausible macro assumptions—growth of 7.5 percent, inflation near 8 percent, annual Birr depreciation of 5 percent, and population growth of around 2 percent each year—Ethiopia will reach a $2,000 per capita income as soon as 2027.

Table 1.10: Country Experiences in Moving From Per Capita Income of $1,000 to $2,000

	Year PCI of $1,000 reached	Year PCI of $2,000 reached	Number of Years Taken
1 Morocco	1988	2005	17
2 Egypt	1995	2008	13
3 Indonesia	1995	2008	13
4 Philippines	2002	2010	8
5 Vietnam	2007	2014	7
6 China	2001	2006	5
7 South Korea	1977	1983	6
8 Bangladesh	2013	...	...
9 India	2007	....	...
10 Kenya	2011	....	...
		Average number of years taken:	**9.9**

Source: WDI and Cepheus Research for compilation

2. **Development Policy**: **Not all State and not all Market… as it should be.**

Development policy: The overall direction of Ethiopia's recent economic policies are being viewed, on the one hand, as a major shift towards neoliberal, free-market policies and, on the other hand, as a continuation of long-standing state-led and state-dominated policies. Neither view fully captures the reality, in our judgement, and policies are instead actually moving towards a mixed and pragmatic approach that seeks to put in place both a strong state and a strong private sector—each with its particular division of labour and spheres of greater dominance. Our tabulation of reforms undertaken over the past two years reinforces this view and points to the fact that development policy is—precisely as it should be—neither 'all state' nor 'all market'(Table 2.1).

In terms of the move towards more liberal economic policies, there is certainly no shortage of recent reforms to show that Ethiopia is moving towards more market-based systems with greater private sector participation. The clearest manifestation of this can be seen in the large privatization program targeting the country's largest state enterprises; the launch of Public-Private Partnerships to help fund many public sector projects; the substantial reform of Investment laws to allow deeper private and foreign investment; and the wide range of initiatives to improve the ease of doing business. We are also likely to see even further efforts to engage private investors in major sector-specific projects across the agricultural, manufacturing, and mining segments of the economy.

Table 2.1: Policies and Reforms aimed at Building a Strong Private Sector

	Strengthening the Private Sector: Examples from Recent Reforms and Policies
Real Economy	1 Part privatization of four big state enterprises (telecom, power, logistics, airlines)
	2 Full privatization of other state enterprises (sugar plants, railways, ind parks, toll roads, smaller firms)
	3 Public-private partnerships being put in place for 17 public projects (14 in energy, 3 in transport)
	4 Public-private partnerships being put in place 8 solar projects to generate over 10,000 MW
	4 Opening of telecom sector to additional two new licensees/operators
	5 Opening of logistics sector to part foreign ownership (two large global firms already entered via joint ventures)
	6 Relaxation of investment law to negative list basis (i.e., all sectors presumed open unless otherwise restricted)
	7 Upper limits on foreign share-holdings expected to be raised in areas where joint ventures are required; this is expected to allow more foreign investment in several service sectors and professional firms once upcoming Investment Regulations are passed
	8 Reforms to improve the ease of doing business (86 measures targeted, 10 ministries, 14 laws amended/revised)
	8 Industry: Generous rental rates offered in state-build and administered industrial parks
	9 Mining: Reforms have introduced more flexible fx account rules for mining and oil/gas firms
	10 Agriculture: Large commercial farms (under potential PPPs) planned for major crops and using irrigation systems, and incentive to modernize farming (such as tax free imports of farm machinery) also put in place
Fiscal policy	1 Generous tax incentives and allowances still in place for a range of investment activities
	2 Low-cost energy still in place for private industries and businesses
	3 Still large resort to private contractors and suppliers for road, energy, other public works
Financial policy	1 Limits being put in place on scope of government and SOE borrowing, enabling more funding for private sector. Borrowing limits being placed on SOEs by the Public Enterprise Holding and Administration Agency (PEHAA) to sharply reduce their net domestic borrowing over the coming three years.
	2 Removal of NBE Bill purchase requirements allows private bank to boost lending to the private sector
	3 Relaxation in rules on foreign borrowing for private firms (60-40 ratio for debt-equity now allowed)
	4 Foreign entry into leasing business allowed, to help provide such financing facilities to SMEs and corporates
	5 Relaxation in rules governing collateral requirements to allow a wide range of movable collateral
	6 Ethiopia signs "New York Convention" that make international arbitration awards henceforth enforceable in Ethiopia, thus strengthening private foreign investor protections in Ethiopia

Source: Cepheus Research compilation, based on policy announcements, press statements, and IMF Staff Report

At the same time, it is erroneous to think that the role of government (or the 'developmental state' depending on one's terminology) is withering away; to the contrary, there are equally significant initiatives being put in place to build-up and strengthen the state (Table 2.2)**.** For perspective, it is worth remembering that the state remains the nominal owner of all land in the country (the largest source of wealth by any measure); is the single largest investor in the economy (with a yearly capital expenditure budget of Birr 174bn or $5bn per year); is the largest wage employer in the economy; is the main provider of social services to the bulk of the population (education, health, and safety nets); and is also the largest financier in the economy (thanks to a state bank whose deposits—near Birr 560bn at end-2019—are roughly twice the amount of taxes collected last year). Even with privatization, the state will continue to maintain majority equity stakes and oversight roles in the country's largest airline, power supplier, shipping/logistics operator, and telecom provider. Looking ahead, the state will have command of an even greater pool of resources as it boosts revenue (from Birr 311bn to Birr 972bn—or 11.5 to 14.7 percent of GDP—over the coming five years) and as the main state bank expands its nation-wide reach (especially to the un-banked). And finally, even within what are clearly private sector spaces, the regulatory role of the state will remain substantial as it sets the 'rules-of-the-game' in areas such as business operating requirements, competition policies, taxation, banking, and much more.

Table 2.2: Policies and Reforms indicative of a Strong and Activist State

Strengthening the State: Examples from Recent Reforms and Policies		
Real Economy and Sector-Specific Policies	1	Land ownership remains in state hands, but offered with user rights (in agriculture) and long-term leases (in urban areas)
	2	Large land allocations at state discretion (e.g. for industrial parks, urban expansion, commercial farms)
	3	State dominant in public infrastructure goods provision, most notably roads, railways, power, water, sanitation
	4	State remains largest single employer (1.6mn civil servants, public school teachers, health/agriculture extension workers)
	5	State is largest educator (public schools and 50-plus universities) and largest health-care provider (public clinics/hospitals)
	6	State to remain in position of influence/ownership even with part privatized SOEs
	7	State retains nearly 20 other large SOEs other than the big four enterprises (telecom, airlines, logistics, energy)
	8	State is (de facto) largest housing developer, with plans to spend Birr 56bn for 500,000 new units in coming years
Fiscal Policies	1	Large boost planned to state tax collections from 12 to 15 percent of GDP in five years (from Birr 311bn to Birr 972bn)
	2	New revenue boosting measures will bring changes to current VAT, excise, and income tax regimes, and will potentially also include a new property tax, inheritance tax, 'chat excise tax', and motor vehicle circulation tax
	3	Corresponding growth in expenditure envisaged from 15 to 17 percent of GDP in four years
	4	Public investment to continue at near 10 percent of GDP for the coming years
Financial Policies	1	State bank still dominates financial sector with two-thirds of financial system assets
	2	Financial sector remains heavily regulated, e.g., for foreign exchange and foreign borrowing,
	3	Financial sector remains (mostly) closed to foreign ownership and participation
Overarching Growth Policies	1	*Job Creation* : Government is taking a pro-active, coordinating role to increase private sector job creation via a Job Creation Commission focused on: adopting 'job-rich' economic policies, addressing labor market gaps, and supporting sectors with high job-creation potential
	2	*Agriculture* : Government is the primary actor and implementer for many past and recent initiatives in this area, including for example, efforts to improve seed varieties, increase fertilizer usage, expand irrigation, broaden commercialization, encourage clustering, and put in place irrigation-based low-land commercial farms
	3	*Industry* : Government remains a major coordinator of industrial policies and acts as the administrator of Ethiopia's industrial parks--setting leasing rates, operating terms and conditions. Taxation, regulation, and competition policy also heavily set by state.
	3	*Services* : Though most services activities are in private hands (retail, trading, hotels, restaurants, transport), the Government plays a lead role in setting the 'rules of the game' via sector-specific regulatory and competition policies.
	5	*Social Safety Nets and Social Protection* : Government is still taking an active role to ensure social safety nets, including through cash transfers under the Productive Safety Net Program (considered 'the largest social protection system in Sub-Saharan Africa'), via a new Urban Safety Net Program, and through a public expenditure policies that still allocate a sizeable share of the budget to 'poverty-reducing expenditures'. Funding under the PSNP to be indexed to food inflation to protect its real value for the coming years.

Source: Cepheus Research compilation, based on policy announcements, press statements, and IMF Staff Report

The combination of efforts to build a strong private sector alongside a strong state is not—as some might see it—a sign of muddled or incoherent policy or somehow a risk to future growth. Indeed, the parallel strengthening of key state capacities/institutions alongside efforts to significantly expand the private sector are—as policy makers see it—positive and mutually reinforcing initiatives. Given this policy direction, the outlook for state-market (government-private sector) relations over the coming years points to the likely co-existence of: (1) an increasingly strengthening government and state enterprise sector still dominating public goods provision (though supplemented, on the margins, by private entrants in areas such as power generation, health, and education); (2) the state bank still delivering the majority of credit and fx provision (but increasingly serving private sector clients and doing so alongside a growing pool of private banks); (3) the domestic private business sector—including both SMEs and corporates—still remaining dominant players in agriculture, trading, services, and construction; and finally, (4) the foreign private sector increasingly dominating more specialized sub-sets of the modern economy such as large-scale manufacturing, industrial/mining exports, and knowledge-intensive agricultural and agro-processing ventures (Table 2.3). This policy mix certainly need not be seen as an impediment to growth and can indeed yield positive growth and developmental outcomes for many years if, for example, the East Asian development records—and most notably the Chinese and Vietnamese cases—are any guide.

Table 2.3: Dominant Economic Actors: Expected Roles and Spheres of Influence in Ethiopia's Emerging Economy

Government and SOEs	State Banks	Domestic Private Sector	Foreign Investors
Dominant role in…	***Dominant role in…***	***Dominant role in…***	***Dominant role in…***
--Infrastructure (roads, power)	--Loans to state enterprises	--Services	--Large-scale manufacturing
--Basic health	--Loans to private corporates	--Retail, trade, distribution	--Mining
--Basic education	--Purchase of Govt Bills/Bonds	--Construction	--Oil and Gas
--Defense and security	--Purchase of SOE Bills/Bonds	--Basic manufacturing	--Big-ticket construction
--Partial ownership in Big SOEs		--Small & Medium-Size Firms	--Specialized agriculture
--Few productive activities		--Artisinal/informal firms	--Specialized agro-processing
But supplemented by…	***But supplemented by…***	***But supplemented by…***	***But supplemented by…***
--Private PPP providers	--Private banks	--FDI in allowed areas above	--Domestic private sector in…
--Private health/educ providers	--Other private financial firms		…some limited areas above
	--Foreign loan/equity providers		

Source: Cepheus Research compilation

3. **Macroeconomic Policy**: **Now more disciplined, more coherent, and more transparent.**

With a well-articulated Homegrown Economic Reform Plan (HGER) in place as well as the support of an IMF financing arrangement, macroeconomic policies in 2020 are set to be the most disciplined, coherent, and transparent seen in years. The HGER Program provides a roadmap of the Government's intentions across a range of macroeconomic, structural, and sector-specific policies. The HGER does not provide a quantitative set of targets or goalposts, but it does lay out the broad framework on what policy initiatives should be expected for the coming years. More precisely, it proposes: (1) *macro policy reforms* (strengthening public finances, correcting fx imbalances, controlling inflation, safeguarding financial stability, and developing capital/financial markets to foster financial inclusion); (2) *structural policy reforms* (streamlining business regulations, improving governance at public institutions, power sector reforms, telecom reforms, export market access, improving logistics, and improving competitiveness in domestic goods/services markets); and (3) *sector-specific policy reforms* (agriculture, manufacturing, mining, tourism, and ICT).(Table 3.1)

Table 3.1 Ethiopia's Home-Grown Economic Reform: A Snapshot of Key Goals and Reform Priorities

MACROECONOMIC Goals & Reforms	STRUCTURAL Goals & Reforms	SECTOR-SPECIFIC Goals & Reforms
1 Strengthen Public Finances	1 Streamline regulations	1 Agriculture modernization
2 Correct FX Imbalances	2 Improve governance at SOEs	2 Manufacturing expansion
3 Control Inflation	3 Improve power sector	3 Mining development
4 Safeguard Financial Stability	4 Improve telecome sector	4 Tourism development
5 Develop capital markets and improve financial inclusion	5 Improve export market access, via WTO and Regional Agreements	5 IT and Creative Industries development
	6 Improve logistics sector	
	7 Improve competitiveness in domestic goods and services markets	

Source: "Ethiopia's Home-Grown Economic Reforms" document from Prime Minister's Office website (www.pmo.gov.et).

Following on the HGER, the Government has set out a more quantified and specific set of policy commitments under the framework of an IMF supported macroeconomic program. These macroeconomic reform plans are disclosed in detailed policy statements by the Finance Minister and Central Bank Governor in a "Memorandum of Economic and Financial Policies", or MEFP (see IMF Staff report, pages 53-72). Most notably, to address current macro challenges, money supply growth will be limited to tackle inflation, borrowing limits will apply to the government's use of commercial bank or central bank funds, and state enterprises will face tighter budget caps—all while ensuring still-high social sector spending for which minimum levels are targeted. The specific *quantitative* targets set out in the MEFP cover ten areas of macroeconomic policy, as tabulated below (Table 3.2):

Table 3.2 Macro Policy Commitments: Quantitative Targets Set out in the "Memorandum of Economic and Financial Policies" of the Minister of Finance and Central Bank Governor

Monetary policy		
1	**Money supply:**	Growth in reserve money limited to 12.5 percent (up Birr 25bn) for the year to June 2020
2	**Central bank loans to Gov't:**	To be capped at no more than Birr 19.5bn for the year; it is also envisaged that NBE advances to the Government will be discontinued by the end of the program (2023)
3	**Central bank forex reserves**:	To be maintained at roughly their end-June 2019 levels of $3.4bn.
Fiscal policy		
4	**Government borrowing**:	To be capped at no more than Birr 67bn for the year to June 2020
5	**Foreign borrowing**:	No high-interest rate external loans to be contracted for the year.
6	**Arrears on foreign loans**:	Zero arrears accumulation on external principal and interest payments.
7	**State enterprise borrowing:**	SOE borrowing from domestic banks to be limited to Birr 74bn for the year.
8	**Tax collections**:	Target of Birr 244.8 bn to be collected by June 2020.
9	**Govt's Foreign Borrowing:**	Government borrowing from abroad to be limited to $1.8bn for the year.
10	**Social Spending**:	Social safety net cash transfers to be kept at a minimum of Birr 11bn for the year, while overall poverty-reducing spending to rise from 4.5 to 5.0 percent of GDP over 3 years

Source: IMF Program Staff Report, January 2020, MEFP pages 51-72. Available on the IMF website at www.imf.org

Other macroeconomic policy commitments include *non-quantitative* measures and address a range of structural reform priorities of the Government. These cover fiscal, state enterprise, capital market, and financial sector issues, and are presented below (Table 3.3):

Table 3.3 Macro Policy Commitments: Structural Reforms set out in the "Memorandum of Economic and Financial Policies" of the Minister of Finance and Central Bank Governor

Fiscal structural reforms		
1	**Tax incentives policies**	An end to most new tax incentives to be put in place (prior action)
2	**Supplementary Budget**	Passage of a Supplementary Budget to account for new fiscal resources and associated spending
3	**New Excise tax regime**	Adoption of new excise tax regime
4	**Fiscal measures**	Passage of 2020-21 Budget to include tax/expenditure measures of 1% of GDP to limit deficit
5	**NBE financing to DBE**	NBE financing of DBE to end by June 2020
6	**Study of Past Tax Incentives**	Study to make assessment of past tax incentives by June 2020
7	**Stock-taking of govt arrears**	Study to compile/review any payment arrears Govt may owe to goods and services providers
8	**Study of Energy Subsidies**	Study to quantify all subsidies on energy products to be completed by Sept 2020
Capital markets structural reforms		
9	**Marketable T-Bills**	Launch of a market-based primary T-Bill auction (prior action)
State Enterprise structural reforms		
10	**SOE Audits**	Financial audits of 20 large SOEs to be finalized by February 2020 by PEHAA
11	**Release of CBE, DBE audits**	Financial audits of DBE and CBE to be released by June 2020
12	**Asset Quality Review of CBE**	Asset Quality Review of CBE financials to be completed by April 2021
FX market structural reforms		
13	**Foreign exchange market reform**	A roadmap to be prepared (by April 2020) to deepen fx market and move towards a more flexible rate by the end of program.

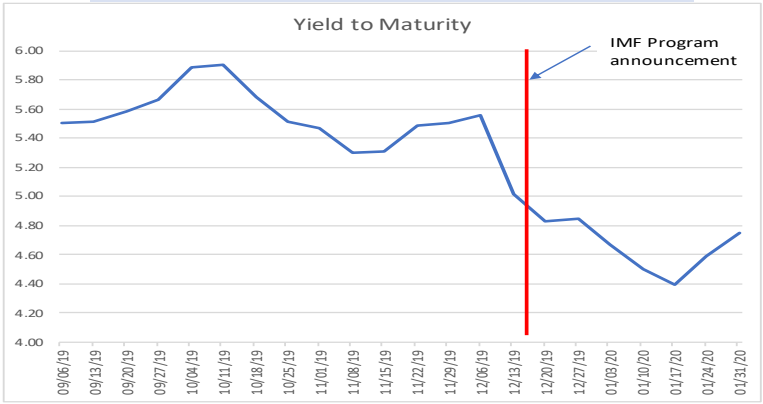
Source: IMF Program Staff Report, January 2020, MEFP pages 51-72. Available on the IMF website at www.imf.org

Beyond just the macroeconomic arena, Ethiopia's resumption of WTO negotiations will further reinforce the pursuit of predictable and rules-based economic and financial policies. The resumption

of Ethiopia's accession talks with the WTO started at end-January 2020 (after an eight-year pause) and, based on the Government's announced intentions, the aim is to "bring Ethiopia into the WTO within the shortest possible period, ideally not later than the end of 2021." WTO entry will modernize and institutionalize Ethiopia's practices, laws, regulations on a range of trade and investment related matters—addressing issues such as export and import rules, market access, and competition policies. We note that Ethiopia's entry is in many ways long overdue (it is one of only 23 countries still outside the WTO, given the body's 164 current members) and that its entry into the WTO would be coming soon after crossing a $1,000 per capita income threshold. This, incidentally, is a path followed by many other countries who leveraged WTO entry to boost FDI, export, and growth trends: WTO entry took place in the year 2000 for China, 2007 for Vietnam, 1995 for Indonesia, and 1995 for Egypt—all around the same year of crossing the $1,000 per capita income threshold.

External investor reaction to the government's recent macroeconomic policy program has so far been quite positive and should continue to be so with strong execution of on-going reforms. Multilateral and bilateral support will, no doubt, be strengthened as macroeconomic policies are now better anchored and give greater assurances that a sustainable set of policies has been laid for Ethiopia's long-term growth. Indeed, as part of the IMF program, an early and upfront vote of confidence was already provided by bilateral partners, who offered a debt re-profiling to cover upcoming debt service dues of around $600mn per year that would have otherwise been payable in each of the coming three years. With respect to private investors, yields on Ethiopia's sole Eurobond issue have fallen since the announcement of the IMF program (though broader emerging market factors were also at play), with effective interest rate now below 4.8 percent as of January 2020 and the lowest ever seen since the bond's issuance in 2014 (Table 3.4). Commentary from the few emerging market investment firms that cover Ethiopia has been clearly positive, with Renaissance Capital for example remarking in a research note that: "With a new focus on cheap external financing, plus more equity and foreign investment, and a track record of policy delivery, we think [Ethiopia] is setting itself up to be one of Africa's most successful economies in the first half of the 21st century."

Table 3.4 Euro Bond Yield

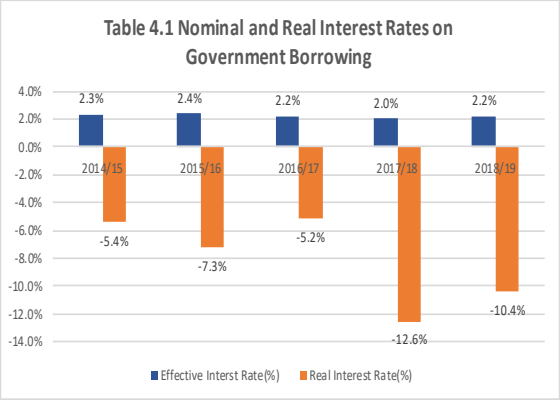


Source: FactSet

4. **Government and State Enterprise Finances**: **Putting a proper price on borrowed money.**

For the first time in decades, the Government is moving away from cheap and 'captive' financing sources and beginning to borrow at rates that better reflect the true cost of credit. The Government's domestic debt—which reached Birr 362bn (13 percent of GDP) as of June 2019—has been covered in recent years by borrowing at very low interest rates from the NBE, from commercial banks, and from the public pension funds. Interest rates on such borrowing ranged from zero to five percent—with an effective average interest rate of just 2 percent on all Government domestic debt (Table 4.1). With inflation rates averaging above 10 percent during this period, real borrowing rates were clearly negative—benefitting government for its wide range of activities, but in the process of hurting savers, the central bank, and the long-term asset value of public pension funds.

Table 4.1: Ethiopa Domestic Interest Rates (Effective) in Percent



Source: MoFEC Debt Bulletin

In similar fashion, state enterprises have benefited from unusually large credits offered at unusually low rates, mainly from the CBE. The domestic debt stock of state enterprises currently stands at around Birr 411 bn (15 percent of GDP), mostly reflecting bonds issued to the state bank. The borrowing was at slightly higher rates than those of Government, with MOFEC debt data showing that state enterprises enjoyed an average effective interest rate of 5.2 percent on all domestic debt (Table 4.2). Per the disclosures in CBE's publicly released 2016-17 annual report, interest rates for Ethiopian Electric Power, Ethiopian Electric Utility, and Ethiopian Railway Corporation were generally set at the savings rate plus 1 percent, which translated into effective rates (given deposit rates at the time) of around 6 percent.

Table 4.2: State Enterprise Bonds (Birr bns)

State Enterprise Domestic Debt	
By borrower	**411.2**
EEP bonds	*172.5*
ERC bonds	*18.9*
Sugar Corporation	*95.7*
Others	*124.1*
By lender/instrument	**411.2**
CBE Bonds	*300.8*
CBE long term loans	107.6
CBE short term loans	2.0
DBE long term loans	0.8
Effective interest rate estimates	
Interest paid 2018-19	19.48
Year average debt stock	375.14
Effective Interest rate	5.2%

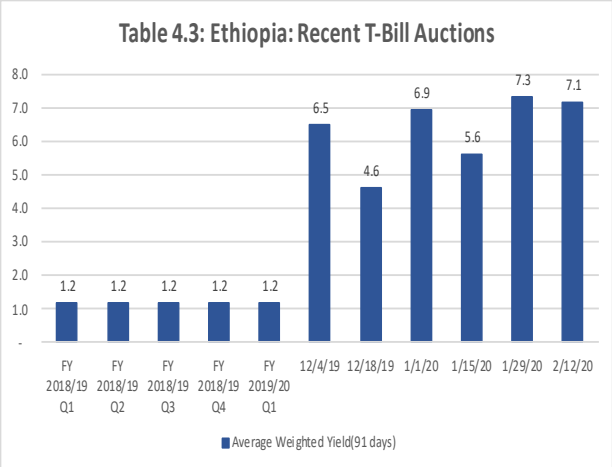
Source: MoFEC and Cepheus Research estimation

These past policies have helped finance major national projects but at the same time resulted in several adverse impacts and distortions. As highlighted in the HERP, negative real interest rates and overvalued exchange rates both provided easy access to financial resources for the public sector, but at the cost of limiting returns to savers, shrinking funds available for the private sector, and contributing to external imbalances through high levels of public sector imports. Moreover, as noted in a recent paper on Ethiopia's experience with such policies of 'financial repression', other additional distortions

that built up included, for example, significant maturity mismatches for the state bank (as it relied on private sector deposits but gave out long-term loans and bonds), and perverse incentives for state enterprises (who were not encouraged to improve performance or repay loans given accommodative policies of capitalizing interest on past due debt).[1]

Recognizing these past distortions, the need to move at least partly towards market-based borrowing arrangements has been prioritized by policy makers, and the very first steps in that direction were taken with the launch of Market-Based Treasury Bill auctions at end-2019. Commercial banks have been the sole participants at the auctions so far and have begun to make their own interest rate bids/offers for the issued debt. With six treasury bill auctions having taken place as of mid-February, the interest rates have risen from 2 percent to as high as 8 percent—thus beginning to reflect market rates even if they remain negative in real terms (due to temporarily high inflation at present) (Table 4.3). Bid-cover ratios have been at least 100 percent for all auctions (meaning that all supply was taken up by participants), despite the fact that banks have temporarily been short of liquidity in the last few months. (Table 4.4).

Table 4.3: Ethiopia: Recent Treasury Bill Auctions



Source: NBE

[1] See World Bank Policy Research Working Paper No 9082 on "Exiting Financial Repression: The Case of Ethiopia" by Jean-Pierre Chaffour and Muluneh Ayalew.

Table 4.4: Market-Based T-Bill Auctions Conducted in the Past Three Months

	Treasury-Bill Auction Dates						
T-Bills of 28 Days Mauturity	4-Dec	18-Dec	1-Jan	15-Jan	29-Jan	12-Feb	*Cumulative*
Bids Offered, Birr mns	250	200	100	100	100	100	*850*
Bids Received, Birr mns	239	240	80	100	100	100	*859*
Bids Accepted, Birr mns	226	200	80	100	100	100	*806*
Bid-cover ratio, %	106%	120%	100%	100%	100%	100%	
Cut-off price, Birr cents	99.00	99.60	99.10	99.53	99.50	99.46	
Cut-off yield, %*	13.17%	5.24%	11.84%	6.16%	6.55%	7.08%	
Weighted average Price	99.42	99.60	99.33	99.53	99.50	99.46	
Weighted average Yield	7.65%	5.24%	8.79%	6.16%	6.55%	7.08%	
T-Bills of 91 Days Mauturity	4-Dec	18-Dec	1-Jan	15-Jan	29-Jan	12-Feb	*Cumulative*
Bids Offered, Birr mns	250	300	400	400	400	400	*2,150*
Bids Received, Birr mns	200	420	492	560	494	560	*2,726*
Bids Accepted, Birr mns	190	300	400	400	400	400	*2,090*
Bid-to-cover ratio, %	105%	140%	123%	140%	124%	140%	
Cut-off price, Birr cents	98.00	98.86	97.50	98.62	98.00	98.25	
Cut-off yield, %*	8.19%	4.63%	10.29%	5.61%	8.19%	7.14%	
Weighted average Price	98.41	98.86	98.30	98.62	98.21	98.25	
Weighted average Yield	6.47%	4.63%	6.94%	5.61%	7.32%	7.14%	

Source: National Bank of Ethiopia website
*T-Bills do not offer any coupouns but are redeemed at par face value, i.e., a 91-Day T-Bll bought at 98 cents yeilds 1 Birr after 91 days
The yield is roughly equal to the annualized interest rate at the offered price: Y= (100-Price)*(365/28) for 28-Day T-Bills,
or Y= (100-Price)*365/91) for 91-Day T-Bills.

The move away from cheap credit is still in its early stages, but is significant nonetheless given the government's willingness to: (1) put in place a (self-imposed) hard budget constraint and (2) begin to set the foundations for other debt markets. A higher cost of government borrowing is to be expected for future years and there will thus be a greater burden on the budget to cover debt service dues; this is, however, moving towards the norm seen in most other countries (Table 4.5) and has its own positive features as it forces the government to recognize the opportunity cost of its borrowing. Moreover, as parallel measures are being taken to boost government resources via revenue mobilization and additional external financing, the need for increased borrowing (and thus higher borrowing costs) should itself be more limited than before. For state enterprises, the harder budget constraint implied from recent policy commitments implies a need to improve their own internally generated financial resources (by charging more realistic prices, expanding their services, reducing losses, or streamlining costs)

Table 4.5: Domestic Government Treasury Bills: Ethiopia vs Other African Countries

	Interest Rate on Govt Three-Month Treasury Bills	Inflation, year-average	Real rate of Return
Ethiopia (Last 5 Years Average)	2.2%	10.1%	-7.8%
Ethiopia (Latest T-Bill Auction)	7.1%	12.6%	-5.4%
South Africa	6.5%	5.2%	1.3%
Kenya	6.6%	5.7%	0.9%
Nigeria	14.0%	14.3%	-0.3%
Zambia	13.0%	9.9%	3.1%
Egypt	14.0%	8.0%	6.0%
Angola	15.5%	15.0%	0.5%
Ghana	16.5%	7.5%	9.0%
Average, excl Ethiopia:	*12.3%*	*9.4%*	*2.9%*

Source: NBE for Ethiopia data. Renaissance Capital for other countries. Data are for end-2019 or early 2020.

5. **Investment in the economy**: **Some sub-components are stalling but still high levels overall.**

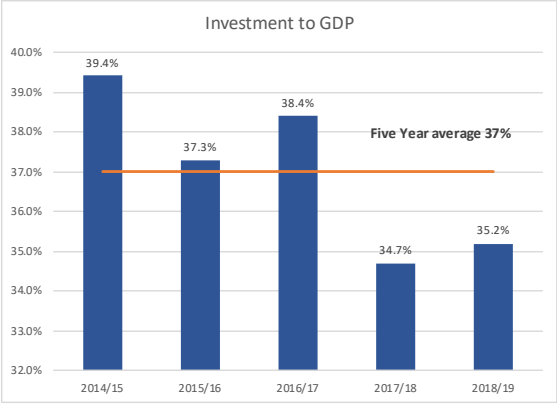
Despite a slowdown in some sub-components, investment remains at a high 35 percent of GDP per official FY 2018-19 data. The overall investment rate remains one of the highest rates in Africa (actually the highest if excluding mining economies) and also one of the highest on a global basis (Table 5.1). Relative to the investment rates seen in recent years, there is a modest slowdown (investment rates averaged 37 percent of GDP between 2014-15 to 2018-19) (Table 5.1B), but this primarily reflects a fall in public sector investment while private sector investment held up relatively well. Still-high overall investment levels provide strong assurances that Ethiopia's growth momentum can be sustained.

Table 5.1A: Total Investment-to-GDP Ratio, 2018

	Total Inv/GDP
Sub-Saharan Africa	
Mozambique*	49.2
Zambia*	42.2
Niger*	40.2
Ethiopia	35.2
Tanzania	33.1
Cameroon	32.6
Ghana	28.1
Cote d'ivoire	26.2
Angola	21.4
Kenya	19.9
South Africa	18.2
DRC	15.3
Nigeria	14.0
Others	
Bhutan	63.7
Nepal	51.8
Algeria	48.9
Panama	44.5
China	44.2
Mongolia	42.2
Uzbekistan	41.0
Mauritania	40.7
SSA Average	**28.4**
World Average	**24.0**

Source: World Bank
** Figures for Mozambique, Zambia, and Niger are partly inflated by recent large mining investments*

Table 5.1B: Ethiopia Total Investment to GDP ratio



Source: MoFEC

Table 5.2: Investment Levels in FY 2018-19 and 2019-20

FY 2018-19 ESTIMATES	Birr (bns)	% of Total	% of GDP
Total Investment-Birr bns	**948.9**	**100.0%**	**35.2%**
Public Sector investment	**296.6**	**31.3%**	**11.0%**
Government	174.9	18.4%	6.5%
State Enterprises	121.6	12.8%	4.5%
Private Sector investment	**652.5**	**68.8%**	**24.2%**
Domestic private investors	565.3	59.6%	21.0%
Foreign direct investment	87.2	9.2%	3.2%

FY 2019-20 OUTLOOK	Birr (bns)	% of Total	% of GDP
Total Investment-Birr bns	**1,144**	**100.0%**	**34.0%**
Public Sector investment	**370**	**32.4%**	**11.0%**
Government	219	19.1%	6.5%
State Enterprises	151	13.2%	4.5%
Private Sector investment	**774**	**67.6%**	**23.0%**
Domestic private investors	655	57.3%	19.5%
Foreign direct investment	119	10.4%	3.5%

Source: For 2018-19, MOFEC investment data, budget capital spending data, and NBE.
For 2019-20, Cepheus estimates based on total investment, budget capex and FDI outlook.
Public vs Private Investment breakdown is taken from IMF Staff Report data.

Seen from a five-year perspective, two notable trends with respect to investment are the rising share of *private* investment and an increasing reliance on *domestic* savings. For 2018-19**,** public sector investment is 11 percent of GDP, per IMF data on the public vs private sub-components, while private sector investment is more than double that amount at 24.2 percent of GDP (Table 5.2). Private investment has risen from 8.5 to 24.2 percent of GDP over the past ten years. Of the 24 percent of GDP in private investment in 2018-19, most of it (Birr 565bn, or around 60 percent of total investment) reflected investment by domestic businesses while around Birr 87bn (~$3bn or 10 percent of total investment) constituted foreign direct investment.

The current slowdown in FDI—per balance of payments data—has not brought down overall investment levels given the still limited share of FDI in total investment. For last year, for example, even as FDI inflows fell somewhat from the previous year (from $3.7bn to $3.1bn, or 4.4 to 3.1 percent of GDP), this was offset by domestic private investment given that total private investment rose from 22 to 24 percent of GDP between 2017-18 and 2018-19. The recent rise of the private investment to GDP ratio means Ethiopia has among the highest such ratios across the ten largest Sub-Saharan African countries (Table 5.3)

Table 5.3: Private Investment-to-GDP Ratio in the Ten Largest Sub-Saharan African Countries

1	Tanzania	25%
2	Angola	24%
3	Ethiopia	22%
4	Cameroon	21%
5	Cote d'ivoire	16%
6	Ghana	14%
7	Nigeria	14%
8	South Africa	14%
9	Kenya	13%
10	DR Congo	10%

Source: IMF Article IV Staff Reports and WDI

Regarding investment flows by economic sector, we estimate that investment continues to be dominated by construction activity, roadbuilding, and manufacturing investments in new industries. Within the public sector, the bulk of government capital investment is flowing into road-building (Birr 47bn), irrigation (Birr 14bn), agriculture (Birr 12bn), and construction works for government buildings such as ministry/region/woreda offices, universities, schools, and health facilities. Within domestic private sector investment, most investment is likely to be flowing into construction related businesses including commercial real estate, residences, and to a lesser extent in capital goods imports for basic manufacturing facilities. For FDI, most of the investment is the counterpart of new capital equipment imports brought in by foreign companies well as construction activities they undertake either as greenfields or for expanding existing facilities.

Looking ahead, prospective FDI is likely to flow into a wider base of sectors as previously restricted areas open up with changes in investment regulations. The state enterprises being privatized are clearly one area that will see significant FDI inflows—thus implying large flows to telecoms, sugar industries, industrial parks, and power plants (as IPPs or PPPs). Logistics is already attracting FDI inflows and should continue to do so. Other areas being given high government support and likely to figure prominently in upcoming FDI inflows (besides manufacturing) include: mining developments; real estate; and commercial farm/irrigation ventures. Within services, the recent relaxation of investment regulations opens the way for enhanced inflows into areas such as domestic air and public transport, professional service firms, advertising, and media services.

6. **Credit to the Private Sector**: **At record levels—and the types and terms are improving.**

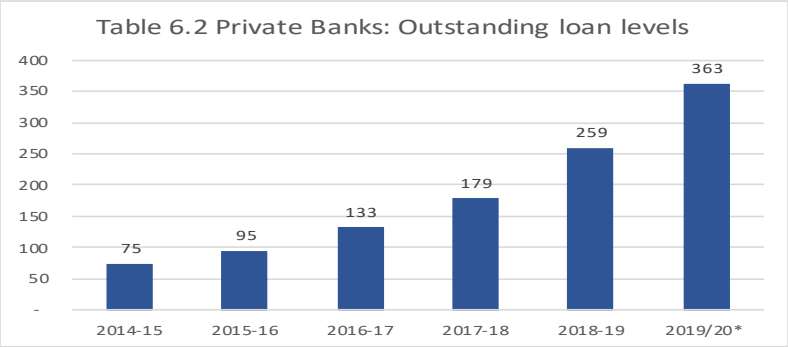
Loans to the private sector passed Birr 320bn last year—a historic high in nominal terms and the highest share (relative to GDP) in five years (Table 6.1 and 6.2). Growth in lending by private banks is up around 44 percent as of end-2019, and is one of the highest growth rates seen in many years. While the recent progress is of course very positive, it remains the case that credit to the private sector is still only about one-third of overall credit, and is a much smaller share of the economy (12 percent of GDP) than that seen in many peer countries.

6.1 Credit to the Private Sector: Levels, % GDP, % of Total

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Credit to Private Sector (Birr mns)	92	120	147	197	241	325	423
Credit to Private Sector (% of GDP)	13.5%	16.0%	9.5%	10.7%	11.0%	12.1%	12.4%
Share of Total Credit (%)	30.6%	32.5%	31.6%	32.6%	30.8%	33.2%	36.0%
Nominal GDP	682	753	1,541	1,833	2,200	2,696	3,422
Total Domestic Credit	300	371	465	604	785	978	1,174

Source: IMF Staff Report, Monetary Survey. Cepheus Research for 2019-20 projections

Table 6.2: Private Banks: Outstanding Loan Levels

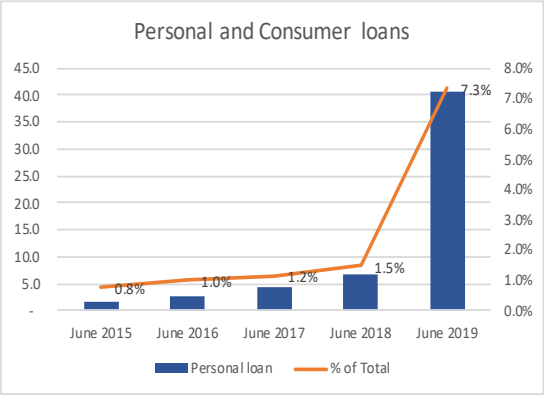


Source: Bank's Annual Reports: Cepheus Research for 2019/20 projections

Looking ahead, the decision to end NBE Bills represents a major policy change that promises to boost credit to the private sector. NBE Bills reached close to Birr 95bn (nearly a quarter of private bank deposits) as of end-2019, and this stock of funds will thus soon make its way back to the private sector. Considering the maturity profile of the NBE Bills (their five-year duration means roughly one-fifth of the total will return to the banks each year) and given the amounts that private banks would have had to buy had the NBE Bills policy stayed in place, the total extra resources becoming available to the private sector is on the order of Birr 25-30 billion per year. This represents about a quarter of last year's *incremental* lending increase (which rose from Birr 179 to 250bn) and is thus a material addition to the supply of private sector credit for the banking system as a whole.

Credit to the private sector is not just growing in size, but also improving in the types and terms of loans becoming available. The market is beginning to provide a greater range of credit facilities better suited to borrowers' needs—including SME loans, consumer loans, loans with looser collateral requirements (including moveable property or on a non-secured basis), and longer-maturity loans. One small but notable example is the sharp rise in offerings of personal and consumer loans this past year to meet the demands ofa growing base of salaried and middle-income clients (Table 6.3). But other features of private sector credit are beginning to change as well, as summarized in Table 6.4, thanks to growing competition among banks, new strategy plans being deployed at most banks with the help of global consulting forms, and the need to address changing market conditions and dynamics.

Table 6.3 Personal loan share



Source: NBE

Table 6.4: Credit to the Private Sector-- Emerging Trends and Directions

Banks are lowering interest rates follwing NBE bills removal

- Awash Bank has reduced rates by up to 4.5 percent depending on the sector
- United Bank has lowered rates by up to 4.5 percent depending on the sector
- Bank of Abyssinia has reduced rates by up to 6 percent in certain cases
- Most other private banks are likely to follow suit in reducing lending rates, given the direction taken by the Top 3 market leaders and the attendant competitive pressures

Dedicated focus on SMEs, consumer/personal loans, and specialized loan types:

- CBE has opened a dedicated unit to serve and lend to SMEs
- Many private banks are separating units that serve large/corporate clients vs those serving SMEs, Medium-Sized firms, and Consumer/Household borrowers
- Some private banks have already set aside dedicated pool of funds specifically for small or medium-sized borrowers, and this trend is ikely to broaden within the banking industry.
- Virtually all banks have started consumer loans offering home, auto, personal loans targeted at varied clients such as salaried workers, diaspora, NGO/International Organization employees, etc
- Close to a dozen banks are under formation, with the aim of providing specialized lending services, such as Islamic Banking, residential and commercial mortgages, consumer banking, and agriculture.

Source: Bank press statements and press reports

7. **Multilateral and Bilateral Partners**: **Ethiopia is now on top of most priority lists.**

Following Ethiopia's extensive internal reforms over the past two years, its engagement with a wide range of international partners is currently at its closest level seen in many years. The closer cooperation and engagement is becoming evident across: (1) multilateral and bilateral institutions; (2) donors, lenders, and investors; and (3) debt as well as equity providers.

The current year's budget is one indication of an already closer re-engagement with many donors and lenders. Total external support includes 33 donors anticipated to provide $1.2bn in budgetary grants and 13 lenders expected to provide $1.4bn in low-interest budgetary loans (Table 7.1).

Table 7.1 External Budgetary Support for FY 2019-20

Ranked from highest to lowest

	Birr mns	USD mns		Birr mns	USD mns
Total Budgetary Grants, Birr mns	**36,820.6**	**$ 1,235**	**Total Budgetary Loans**	**40,296.8**	**$ 1,352**
Multilateral grants	**31,752.3**	**$ 1,065**	**Multilateral loans**	**31,873.8**	**$ 1,069**
World Bank--IDA [for PBS program]	14,870.1	$ 499	IDA--World Bank [for PBS program]	19,925.9	$ 668
Global Fund	4,006.6	$ 134	IDA--World Bank	7,131.3	$ 239
Global Alliance for Vaccines Initiative /GAVI/	2,951.3	$ 99	African Development Bank	1,919.2	$ 64
Others	2,203.8	$ 74	World Bank	1,684.0	$ 56
European Union [for PBS program]	1,939.1	$ 65	Intl Fund for Agricultural Devpt	610.5	$ 20
African Development Bank [for PBS program]	1,189.6	$ 40	Arab Bank for Africa Devpt	602.9	$ 20
United Nations Children's Fund	920.9	$ 31			
Pool Fund for MDGs	807.7	$ 27			
International Devpt Association (World Bank)	803.2	$ 27			
European Union	416.9	$ 14			
World Bank	336.7	$ 11			
World Food Program	287.2	$ 10			
African Development Fund	278.2	$ 9			
International Fund for Agricultural Devpt	253.5	$ 9			
European Development Fund	161.0	$ 5			
Global Environment Facility	135.8	$ 5			
African Development Bank	133.7	$ 4			
Center for Diseases Control	22.5	$ 1			
United Nations Fund for Population Activity	16.3	$ 1			
United Nations Development Program	11.5	$ 0			
World Health Organization	6.8	$ 0			
Bilateral Grants	**5,068.3**	**$ 170**	**Bilateral loans**	**8,423.0**	**$ 283**
UK-Dept for International Development	1,888.6	$ 63	China EXIM Bank	2,624.6	$ 88
US Agency for International Development	1,676.8	$ 56	Others	2,611.8	$ 88
Canadian International Development Agency	330.3	$ 11	China	1,541.8	$ 52
Netherlands (KNCB)	273.2	$ 9	KOICA (Korea)	1,010.7	$ 34
Ireland	195.3	$ 7	Saudi Fund	559.9	$ 19
Germany (KFW & GTZ)	187.5	$ 6	Italy	56.6	$ 2
Italy	168.4	$ 6	Kuwait Fund (KFAED)	17.6	$ 1
Others	113.6	$ 4			
Danish Intl Development Agency (DANIDA)	71.8	$ 2			
Finland (DIDC)	70.5	$ 2			
Sweden (SIDA)	70.1	$ 2			
Spain	15.7	$ 1			
China	6.5	$ 0			

Source: Federal Budget Document of June 2019 for Fiscal Year 2019-20 Budget: Revenue, Grants and Loans Table
These figures only cover Budget grants and would not include funds provided to non-budgetary activities (e.g. direct humanitarian assistance)
Donors are also providing substantial emergency humanitarian assistance, with funding from the US ($379mn), UK ($74mn), EU ($48mn), Germany ($30mn), Sweden ($22mn), Korea ($13mn), Canada ($13mn), and amounts below $10mn from several others. Data from UN OCHA Feb 10 , 2020 Ethiopia Humanitarian Bulletin

Looking ahead, the commitment of most multilateral institutions towards Ethiopia is likely to be the strongest it has been in decades. The World Bank, the United Nations, the IFC, the IMF, the African Development Bank, the European Investment Bank, the Trade and Development Bank, the

International Fund for Agricultural Development, have for example already boosted their support or indicated their intention to substantially raise their financial support in the coming years. Such support will take place through varied instruments that will include grants (IDA, UN agencies), low-cost, long-term loans (IDA, AfDB, IFAD), foreign exchange and macro policy support (IMF), and direct equity, lending, or trade finance support to the private sector (IFC, AfDB, TDB, and others) (Table 7.2).

At the same time, many national governments and their development agencies are also continuing or deepening their engagements—and in many cases working with both the public and private sectors. Three large donors to Ethiopia—DFID, USAID, and the European Union—are long-standing partners who have provided humanitarian, social sector, and private sector support and continue to have active programs in Ethiopia that will likely be sustained or increased in the coming years. Private sector focused bilateral agencies are also expected to show a deeper engagement, including: the CDC of the UK; the Millennium Challenge Corporation and Development Finance Corporation (formerly OPIC) of the US; Proparco of France; and Scandinavian groups such as Norway's Norfund, Sweden's Swedfund, and Finland's Finnfund. The Governments of rest of the G7—Germany, Italy, Canada and Japan—have in recent bilateral forums also indicated a strong readiness and willingness to provide both public sector and private sector support, as have governments or affiliates in China, Saudi Arabia and UAE. Additional or on-going support is also expected from private groups and foundations, such as the Gates Foundation, the Soros Foundation, the Mastercard Foundation, and others with initiatives focused on public health, education, financial inclusion, entrepreneurship, SMEs, and job creation.

Table 7.2 Ethiopia: Recent and Prospective Financial Support from Official Multilateral and Bilateral Partners*

Multilateral institutions	
World Bank	Development Policy Credit addressing Growth and Competitiveness Reforms ($1.2bn) Other large financing programs cover: Enhancing Public Services and Social Safety Nets; Urban Development; Water and Sanitation; Electrification; Rural Development; Transport; Job creation; Renewable energy; Local Government capacity building; and support for industrial parks
International Monetary Fund	Balance of payments support of $2.9bn over three years for macro/structural reforms
International Finance Corporation	Providing financing directly to Ethiopian private businesses and private equity groups Also providing financing to Ethiopian banks via trade finance lines
African Development Bank	Providing budgetary loans and grants focused on infrastructure projects
Trade and Development Bank	Providing financing directly to Ethiopian private businesses
European Investment Bank	Recent support has included funding for Job Compact, SMEs, entrepreneurship programs, and solar Also providing financing directly to Ethiopian businesses and private equity
European Union	Recent pledges to support transport, logistics, health, elections, and business climate reforms
Intl Fund for Agricultural Devpt	Providing financing for agricultural projects and climate resiliency initiatives
World Trade Organization	Expedited accession planned to the WTO, and engagements to this end initiated in January 2020
Bilateral Partners	
UK-DFID	Large multi-year programs are providing budgetary and non-budgetary support, including in areas such as health, education, humanitarian support, social services, and private sector growth
USAID	Large multi-year programs are providing budgetary and non-budgetary support, including in areas such as food security, democracy and governance, economic growth and trade, and social services
US-MCC	As entrant to 'Threshold Program', support expected for reforms that boost growth and investment
US-DFC	Significant financing, up to $5bn over next few years, planned for private sector from ex-OPIC DFI
Canada	Providing financing via CIDA for programs focused on human development, governance, and growth
Italy	Providing financing for projects focused on agriculture, infrastructure, and rural development
France	Providing financing for budget support, education, economic agencies and (via AFD) for power grid
Germany	Providing financing direct budgetary support and projects implemented under KFW and GTZ
China	Providing financing for mainly infrastructure public sector projects (via EXIM and other banks)
Korea	Providing financing for electricity, irrigation, and rural development projects (via EXIM Bank of Korea)
Saudi Arabia	Providing financing to infrastructure and energy projects and in reprofiling fuel import dues
United Arab Emirates	Provided support to central bank reserves, and recently to multiple sector-specific investment projects

Source: Websites of respective agencies and press reports. This is a selective tabulation of major official partners and not meant to be an exhaustive listing.
** This tabulates official sector support (i.e. public sector lenders and donors) as opposed to foreign direct investors or private foundations and donors.*

The enhanced support of external partners is significant as external savings will remain critical for Ethiopia to maintain still high investment rates in the economy. Moreover, beyond just focusing the public sector, funding is now also flowing directly to the private sector in the forms of both debt and equity. With domestic savings rates at around 24 percent of GDP, the needed pool of external resources (savings) to meet the 35 percent investment to GDP ratio is on the order of 10 percent of GDP each year. The enhanced support of official external partners—adding up to as much as $4bn, or 4% of GDP, annually if including grants, low-interest loans, and debt rescheduling (Table 7.3)—is thus significant in that respect. Such official external support is supplemented by large private sector inflows including remittances from the diaspora (~$6bn annually) and foreign investment (~$3-$4bn). Taken together, these external financing flows are making possible investment levels that are well beyond available domestic savings and thus contributing to faster growth and developmental outcomes than would have otherwise been the case.

TABLE 7.3: Official Financing Flows Under the Government-IMF Macroeconomic Program

Projected Official financing flows for the coming four years:

Type of inflow	2019-20	2020-21	2021-22	2022-23	Total
Official grants	$ 1,374	$ 1,278	$ 1,161	$ 1,330	**$ 5,143**
Official loans to Govt, excl IMF	$ 1,331	$ 1,375	$ 1,414	$ 1,357	**$ 5,477**
IMF loans	$ 619	$ 804	$ 990	$ 495	**$ 2,908**
Debt service rescheduling	$ 156	$ 634	$ 637	$ 606	**$ 2,033**
Additional donor funding	$ 220	$ 175	$ 700	$ 825	**$ 1,920**
Total Official flows to Govt:	$ 3,700	$ 4,266	$ 4,902	$ 4,613	**$ 17,481**
In percent of GDP:	3.4%	3.7%	3.9%	3.3%	...

Comparisons of Projected Inflows for Next Four Years and Actual Inflows of Past Four Years

	Actual over Past 4 Yrs	Planned over Next 4 Yrs
Grants:	$ 6,198	$ 5,143
Grants plus additional donor funding:	$ 6,198	$ 7,063
Loans to Govt:	$ 6,601	$ 5,477
Loans to Govt, plus IMF loans:	$ 6,601	$ 8,385

Source: IMF Staff Report (Table 6 on Gross Financing) and Cepheus Research compilation. SOE external loans excluded.

8. Privatization: Inflows will start in 2020, and should exceed $5 billion within three years.

Though almost two years have passed since the announcement of the recent round of privatization, 2020 should be the first year that sales transactions take place. Per the Government's Memorandum of Financial and Economic Policies, privatization initiatives are currently most heavily focused on six main sectors: (1) telecommunications, (2) logistics; (3) railways; (4) industrial parks; (5) sugar; and (6) energy. Sectoral studies for all of these sectors (except industrial parks) are reported to be completed, with these assessments laying out the plans for the privatization strategy in each of the six sectors. For context, a listing of the 23 largest state enterprises, as well as their available financial indicators, are summarized below (Table 8.1 and 8.2).

Table 8.1: Ethiopia's Major State-Owned Enterprises (SOEs)

Listing of 23 SOEs Administered by PEHAA*

Profitable SOEs: 18 Enterprises

Manufacturers

1 Chemicals Industry Corporation
2 Sugar Corporation
3 Berhanena Selam Printing Enterprise
4 National Alcohol and Liquor Factory

Service Providers

5 Ethio Telecom
6 Ethiopian Airlines Group
7 Ethiopian Shipping and Logistics Enterprise
8 Ethiopian Postal Service Enterprise
9 Ethiopian Tourism Organization
10 Filuwha Spa Enterprise
11 Ghion Hotels Enterprise
12 Ethiopian Hotels S. C. (Hilton Hotel)

Trading Companies

13 Ethiopian Agricultural Businesses Corporation
14 Ethiopian Trading Businesses Corporation

Financial Institutions

15 Commercial Bank of Ethiopia
16 Ethiopian Insurance Corporation

Construction Sector

17 Ethiopian Constructon Design and Supervision Works Corporation
18 Ethiopian Construction Works Corporation

Loss-making SOEs: 5 Enterprises

19 Development Bank of Ethiopia
20 Metal and Engineering Corporation
21 Ethiopian Mining, Petroleum and Biofuels Corporation
22 Ethiopian Pulp and Paper Share Company
23 Shebelle Transport Share Company

Source: PEHAA Public Press Briefing Note, September 2019 and Reporter Newspaper
** Public Enterprise Holding and Administration Agency (formerly Ministry of Public Enterprises)*
Financial performance refers to 2018-19 fiscal year.

Table 8.2: Selected Indicators for Ethiopia's 23 Largest SOEs

Income Indicators in Birr billions

Company	Revenue	Profits	Profit Margin
1 Ethiopian Airlines Group	114.0	8.9	7.8%
2 Commercial Bank of Ethiopia	53.6	17.9	33.4%
3 Ethio Telecom	36.0	24.9	69.2%
4 Eth Shipping & Logistics Enterprise	18.7	2.0	10.6%
5 All Other SOEs (19 Companies)	35.7	(1.4)	...
Of which: 14 profitable	...	2.5	...
Of which: 5 loss-making	...	(3.9)	...
TOTAL FOR 23 LARGE SOEs:	**258.0**	**52.3**	**20.3%**

Income Indicators in USD billions

Company	Revenue	Profits	Profit Margin
1 Ethiopian Airlines Group	$ 4.1	$ 0.3	7.8%
2 Commercial Bank of Ethiopia	$ 1.9	$ 0.6	33.4%
3 Ethio Telecom	$ 1.3	$ 0.9	69.2%
4 Eth Shipping & Logistics Enterprise	$ 0.7	$ 0.1	10.6%
5 All Other SOEs (19 Companies)	$ 1.3	$ (0.0)	...
Of which: 14 profitable		$ 0.1	...
Of which: 5 loss-making		$ (0.1)	...
TOTAL FOR 23 LARGE SOEs:	**$ 9.2**	**$ 1.9**	**20.3%**

Foreign exchange revenues, USD bns

Company	FX Revenue
1 Ethiopian Airlines Group	$ 4.000
2 Ethio Telecom	$ 0.086
3 All Others	$ 0.063
TOTAL FOR 23 LARGE SOEs:	**$ 4.149**

Employment

Employment: All 23 Large SOEs	
Permanent	139,194
Temporary	16,812
Contract	14,786
Total	**170,792**

Source: PEHAA Public Press Briefing Note, September 2019. Data is for 2018-19 fiscal year

Based on plans announced so far, our rough estimates suggest that privatization related fx inflows could reach $5-$7bn over the coming three years (Table 8.3). These estimates are based on four main privatization prospects, namely: a part privatization of Ethio telecom and Ethiopian Shipping and Logistics Service Enterprise, the issuance of two new telecom licenses, and the sale of at least half of the remaining state enterprise stock (including sugar companies, industrial parks and other assets). Notably excluded is the part privatization of Ethiopian Airlines (which does not appear to be a near-term prospect) and the privatization of the electric power company (whose large debt liabilities and financial challenges are likely to first require an extensive period of rehabilitation under state hands). These estimates are based on valuations seen in a sample of comparable emerging and frontier

markets—which show a Price-to-Earnings ratio of around 11x on average for telecom companies and around 9x for other companies (Table 8.4). On these valuation multiples (and an admittedly simplified estimation), total privatization receipts could fall within a range of $5.2 to $10.5bn, taking the 25th and 75th percentiles as the applicable range, for a median value of $7.8bn.[2]

Table 8.3: Prospective Privatizations: An Estimate of the Range of Possible Valuations

	Company	Revenue (USD mn)	Earnings (USD mn)	Comparator P/E Multiples			Implied Valuation for planned stakes		
				Low-end	High-end	Mid-point	Low-end	High-end	**Mid-point**
1	Ethio Telecom	$ 1,312	$ 394	7.6	15.2	11.3	$ 2,875	$ 5,730	**$ 4,302**
2	First Telecom licensee	…	…	7.6	15.2	11.3	$ 719	$ 1,433	**$ 1,076**
3	Second Telecom licensee	…	…	7.6	15.2	11.3	$ 719	$ 1,433	**$ 1,076**
4	Eth Shipping and Logistics	$ 665	$ 70	6.0	11.7	9.3	$ 404	$ 788	**$ 596**
5	Other SOEs (excludes EAL, EEP)	*$ 635*	*$ 90*	6.0	11.7	9.3	$ 535	$ 1,044	**$ 790**
							$ 5,252	$ 10,427	**$ 7,839**

Source: Revenue and earnings data from PEHAA Public Press Briefing Note, September 2019. P/E Multiples from Factset data and Renaissance Capital.
*Privatization of two large state enterprises, Ethiopian Airlines and Ethiopia Electric Power, is **not** assumed in the above estimation exercise.*
For Ethio Telecom and ESLE, a 49% equity offer assumed; for two new telecom licensees, an eventual 25% (each) market share guides estimation.
For "Other SOEs" this excludes EAL and EEP.

Table 8.4: Valuations for Telecom Companies and Broader Equity Markets

	TELECOM COMPANIES Company	Valuation: P/E ratio		Market Capitalization (USD mns)
1	Safaricom Kenya	15.5	$	11,540
2	Vodafone Tanzania	14.8	$	832
3	MTN Ghana	…	$	1,562
4	MTN Nigeria	10.5	$	6,681
5	MTN South Africa	11.4	$	11,054
6	Vodacon South Africa	11.3	$	14,144
7	Telkom South Africa	7.4	$	1,505
8	Telecom Egypt	4.4	$	1,082
9	Turk Telecom	7.8	$	4,234
10	Etisalat UAE	15.5	$	38,594
	25th percentile:	***7.6***	***$***	***1,399***
	Median:	***11.3***	***$***	***5,458***
	75th percentile	***15.2***	***$***	***12,191***

	OVERALL STOCK MARKETS Country	Valuation: P/E ratio		Market Capitalization (USD mns)
1	Kenya (MSCI)	12.1	$	14,981
2	Tanzania (DARSDSEI)	5.6	$	3,940
3	Ghana (GGSECI)	3.9	$	3,599
4	Nigeria (MSCI)	6.1	$	23,486
5	South Africa (MSCI)	11.5	$	356,837
6	Egypt (MSCI)	9.0	$	10,658
7	Morocco (MSCI)	18.9	$	47,414
8	Turkey (MSCI)	6.2	$	68,326
9	UAE (MSCI)	9.5	$	137,466
10	Bangladesh (DSE)	11.0	$	46,000
	25th percentile:	***6.0***	$	8,979
	Median:	***9.3***	$	34,743
	75th percentile	***11.7***	$	85,611

Source: Factset data and Renaissance Capital

[2] These valuation estimates are only illustrative, of course, and will depend on the specific regulatory and operating conditions laid out at the time of privatization.

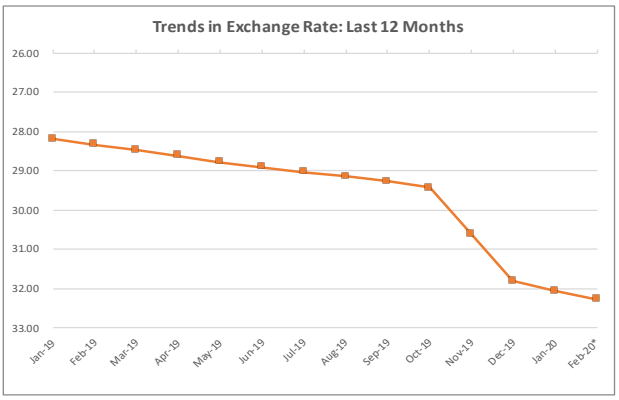
Fx inflows from privatization may not all be available for government use (as some portion may be used to repay debt or recapitalize capital), but this will still improve the country's net external position. Any gross privatization receipts could, in principle, be utilized to: (1) recapitalize the existing companies; (2) to settle the company's outstanding foreign/domestic debt; (3) or be transferred to the central government to be used for fiscal resources. Depending on which of these options, or combination of options, is selected the net impact in terms of resources made available to the government is unclear. Under either of the scenarios, the overall economy will of course be a beneficiary of the gross inflow of funds, but the ultimate beneficiaries could be the state enterprises themselves (if used for recapitalization), past lenders (if used for debt repayment), or the general population (if directed towards higher budgetary spending).

Beyond solely the financial gains involved, **privatization should deliver positive spillovers to the wider economy**. Given the firms targeted for privatization, it is reasonable to expect a major improvement in the operating environment of telcom-dependent businesses and manufacturers, exporters, importers and other users of logistics and distribution services. The impacts could also be particularly notable with respect to the growth of fin-tech services (regulations permitting) and other tech-based start-ups and 'digital disruptors' seeking to address market needs in transport, health, education, entertainment or other areas.

9. Exchange Rate and FX Supplies: A realistic rate for the Birr not yet in place, but is on the horizon.

The faster rate of exchange rate adjustment put in place since end-2019 has been a very positive step and signals a move to address Ethiopia's long-standing fx challenges. The accelerated pace of adjustment has been evident since November 2019, and the annual depreciation rate has been moved from around 6 percent in mid-2019, to a pace that is now closer to 15 percent on annual basis as of February 2020 (Table 9.1).

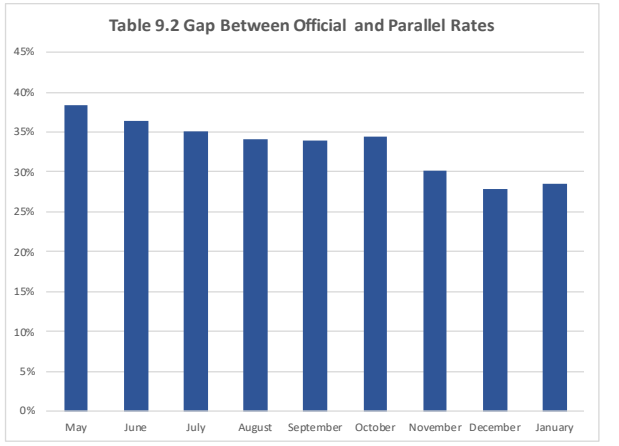
Table 9.1 Recent Trends in Exchange Rate



Source: CBE website FX Rates

Though the gap between the official and parallel market rate has fallen somewhat, it remains substantial. The gap between the two rates is down from a peak of 38 percent in mid 2019 to about 25 percent as of early 2020 (Table 9.2). On a positive note, the parallel rate appears to have stabilized in the past few months. At the same time, that the gap is currently on the order of 20-25 percent reveals an official exchange rate that is not yet reflective of its proper market rate. The size of the gap is—incidentally—roughly in line with the IMF's estimated over-valuation (23-25 percent per the IMF Staff Report, though these estimates are seen to have high degrees of uncertainty).

Table 9.2 Gap between parallel and official market



Source: Cepheus Research

With respect to policy initiatives focused on addressing the Birr's misalignment and improving fx conditions, several planned measures have been highlighted in the Homegrown Economic Reform Plan. These include: increased privatization and low-cost borrowing; an improved remittance strategy; stronger efforts to boost diaspora savings; promoting exports/tourism/FDI; easing controls on fx sales to private importers'; and improving "the management and functioning of the fx market based on further study."

More recently, as part of the Government's IMF-supported macro program, there is a clear statement that moving towards a market-reflecting exchange rate is a policy priority; however, the timing of such a move is not immediate but rather seen as a medium-term objective. Based on the contents of the IMF program, the 'transition to a market-clearing exchange rate' is envisaged 'by the end of the program' which implies an approximate timing towards the end of 2023. A quicker correction of the Birr rate to its market determined rate (as done for T-Bill rates) might have been expected, but this has not been the approach adopted. Moreover, while the NBE bills removal ended private banks from allocating 27 percent of their funds to government bills, the 30 percent surrender requirement faced by private banks on the fx collected from their clients remains in place, reducing by that magnitude the volume of foreign exchange they can make available to the private sector.

While changes to the fx regime have thus been limited so far, it is nonetheless still possible that meaningful exchange rate reform could be forthcoming in the near-term. Per the IMF program, the Government will soon be finalizing (by April 2020) "a roadmap to deepen the fx market and move towards a more flexible exchange rate by the end of the program." If substantive reform measures are put in place as part of that roadmap and review, a move towards a quicker rate adjustment might thus be forthcoming, which would help reduce and remove foreign exchange shortages at a much faster schedule than currently envisaged.

10. **Financial Sector Reforms** : **A slow start so far, but prospects look good for 2020 and 2021.**

Reforms enacted over the past year are beginning to address many of the past problems seen in the financial sector—including its small overall size relative to the economy (just ~33% GDP), its lopsided distribution of credit (two-thirds to the public sector), and its limited set of offerings that tailored to the needs of local businesses, SMEs, and households (in terms of cost, instruments, maturity, and collateral requirements).

Specific measures enacted over the past two years are helping to boost private credit supply, reduce borrowing costs, and loosen collateral and other regulatory requirements (Table 10.1). Among the most notable reforms: (1) market-based securities have been introduced; (2) NBE Bill purchase requirements imposed on private banks have been discontinued; (3) certain segments of the financial sector—such as leasing—have been opened to foreign investors; (4) collateral requirements have been eased (e.g., movable collateral registry); and (5) diaspora investment into banking shares has been allowed.

Table 10.1 Financial Sector--Recent Reforms

Areas of Reform	
1 **Debt Markets**	Market-based Treasury Bills introduced
2 **NBE Bills**	Removal of mandatory purchase of NBE Bills equal to 27% of new lending
3 **Leasing**	Leasing business opened to foreign investors
4 **Collateral requirements**	Movable collateral register ratified to allow broader range of collateral including items such as machinery, transport equipment, and livestock
5 **Islamic banking**	Sector opened to banks to be established focused explicitly on Islamic banking
6 **IFRS Reporting**	IFRS 9 transition became mandatory in 2018-19, helping improve private bank's transparency and financial disclosure practices
7 **Diaspora involvement**	Diaspora investment in Ethiopian bank shares permitted
8 **Anti-Money Laundering**	AML and CFT reforms by NBE and banks have removed Ethiopia from FATF grey list as of October 2019; this could improve scope for Ethiopian banks to broaden their future correspondent banking relationships.

Source: NBE announcements, press reports, and IMF Staff Report (Memorandum of Economic and Financial Policies).

Additional financial sector reforms have been promised publicly or are to be expected in the near term. These cover areas such as: (1) debt and capital markets; (2) deposit insurance; (3) modernizing monetary policy tools; (4) improving the operations of state banks; (5) financial inclusion policies; and (6) digital banking initiatives (Table 10.2).

Table 10.2 Financial Sector--Prospective and Anticipated Reforms

Areas of Reform	
1 **Foreign exchange policies**	NBE is undertaking a study to 'review all existing FX regulations and restrictions and adopt a roadmap to develop the FX market and guide the move towards a more market-clearing exchange rate system by the end of the program' Potential consideration may be given to formalizing parts of parallel fx markets
2 **Deposit insurance**	Deposit insurance scheme to be introduced to strengthen financial stability
3 **Monetary policy tools**	NBE to strengthen its monetary policy framework, including consideration (in the near-term) of deposit auctions to absorb liquidity when needed and, in the longer-term, developing a market for government securities with market-based interest rates (i.e., open market operations of government securities, such as the new Market-Based T-Bills whose stock will grow steadily over time).
4 **Secondary Markets**	Market to trade T-Bills expected to be established--to promote liquidity in the market and enable primary buyers to dispose T-Bills without holding them to maturity
5 **DBE Operations**	New operating approaches to be considered for DBE, including identifying a suitable funding, business, and pricing model
6 **NBE Operations**	Medium-term plans include 'operational independence for NBE and accountability for price stability'
7 **Financial Safety Net & Crisis Management**	A framework to be put in place on a liquidity assistance framework and a bank resolution framework should such circumstances arise.
8 **Consumer protection**	A financial consumer protection framework under drafting and to be put in place
9 **Financial Education**	A financial education strategy being finalized to broaden financial inclusion
10 **Risk-sharing schemes**	To incentivize lending to particular areas, such as for SMEs and agriculture sector, the set up of risk-sharing schemes (such as partial guarantee funds) is under consideration
11 **Basic 'no-frills' accounts**	To broaden financial inclusion and reach under-served populations, a Directive is under preparation for banks to offer basic, 'no-frills' accounts (which will also have simplified Know-Your-Customer requirements)
12 **Digital banking**	Government to deepen efforts to accommodate digital payments for Government-to-Person (G2P) payments and for Person-to-Government payments (P2G)

Source: NBE announcements, press reports, and IMF Staff Report (Memorandum of Economic and Financial Policies).

Looking ahead, we think that—after a period mostly preparatory work this year—2021 is likely to mark the period of active implementation of most financial sector reforms. The opening of the sector to foreign banks remains unlikely even in 2021, in our view. Instead, the second half of 2020 or 2021 should see the start of some limited private debt and equity markets as well as the emergence of new financial institutions (including non-banks) specialized in fin-tech offerings, Islamic banking, leasing, SME financing, mortgage loans, and agricultural credit—all of which promises to gradually broaden the volume, mix, instruments, pricing, and terms of funding provided by Ethiopia's fast-growing financial sector.

Quarterly Macroeconomic Review
Fourth Quarter 2019

Macro Research Ethiopia

CEPHEUS
RESEARCH & ANALYTICS

February 28, 2020

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SUMMARY: Recent Developments and Year-Ahead Outlook

- **Growth**: Compared to last year's 9 percent outturn, GDP growth should slow slightly this year due to some of the tightening measures being implemented to reduce credit growth to the government and state enterprises. However, as recent agriculture data show a solid harvest (up almost 5 percent) and various proxies for construction and service activity point to near double-digit expansion in these large sub-sectors, we don't expect a major slowdown and see a decent chance that growth will reach 8 percent for the year. The IMF forecasts 6.2 percent growth this year, which exaggerates the scale of the expected slowdown, in our view.

- **Inflation**: Ethiopia's inflation rate remains in the range of 18-19 percent at the start of 2020 and this high rate has now spread to services such as housing and transport (whose inflation rate was—until recently—only around 10 percent for an extended period). An inflation rate in the low- to mid-teens will likely persist for most of 2020, though a reduction towards 10 percent should be possible—given tight limits now placed on base money growth—towards the end of the year. While central bank policies will work to reduce inflation, supply-side shocks (such as potential domestic disruptions linked to elections) could affect food prices and keep inflation high; this is not our baseline expectation but is a noteworthy risk.

- **Investment:** While some components of investment (e.g. FDI) are stalling, total investment should still remain at around 33-35 percent of GDP this fiscal year given high government capital spending and the substantial credit expansion taking place at private banks (with its associated private domestic investment).

- **Fiscal:** Even with a Birr 28bn Supplementary Budget being added this month, fiscal deficit outturns for the year should—due to extra available resources—come in close to the initial budgeted figures (below 3% of GDP), while the debt ratio will decline markedly to 52 percent of GDP by June 2020. Judging by commitments in the macro

program, the fiscal year starting in July 2020 will show a 2.5% of GDP budget deficit, while debt ratios should remain broadly unchanged.

- **Banking and credit**: Credit conditions for private business improved last year and should continue to do so in 2020, as the end of NBE Bill purchase requirements allows private banks to boost lending to the private sector. Recent liquidity problems (due to weak asset-liability management by banks) should be short-lived and lending growth at private banks is on track to reach 40 percent for the fiscal year judging from end-December outturns; reflecting this, plus improved fx inflows at most banks, profits at private banks will pass Birr 14bn this year, by our estimates, vs Birr 11bn last year.

- **Foreign exchange**: Despite a somewhat faster pace of monthly exchange rate adjustment, fx conditions will remain challenging this year given the backlog of unmet fx demand and the gradual pace of some large expected fx inflows (i.e., privatization). The gap between the official and parallel market rates is now roughly 25 percent—notably lower than last year's gap of 37 percent but substantial nonetheless. The Government's IMF-supported macro program takes a gradual approach to addressing Ethiopia's exchange rate misalignment (though we would have expected—and liked to have seen—a quicker correction). Reflecting this state of affairs, businesses seeking foreign exchange will continue to face extended waiting times at banks till at least the end of 2020, though planned reforms to the fx market (including a promised review of policies in this area being prepared by April 2020) could—if substantive—help reduce and remove fx waiting times at banks next year.

- **Risks**: Given planned elections this year, public confidence and business sentiment may turn cautious or negative during the year (leading to cutbacks in investment and thus lower growth), but risks in this area are offset somewhat by on-going improvements in macro policies and by the continuation of structural reforms (privatization, PPPs, job creation initiatives, and ease of doing business reforms). A relatively stable socio-political environment for the remainder of the year will remain critical to avoid an interruption of Ethiopia's recent investment and growth record—and indeed forms the basis for our baseline macro projections.

A summary of our full set of macroeconomic projections for the new fiscal year—covering the real, banking, fiscal, and external sectors—is provided in the attached Annex (pages 49 and 50).

ECONOMIC ACTIVITY: Recent Developments and Outlook

- Recently released agricultural data show this year's crop harvest was 32.9mn tons, up 4.3 percent, and in line with our forecasts last year.

- Total acreage cultivated during the crop season was 12.8 mn hectares (unchanged from a year-ago) which gives an average yield—across all crops—of 2.58 tons per hectare. Yields were up by 4 percent from year-ago, and so virtually all of the observed crop increase was driven by improved yields rather than increasing hectares farmed.

- The growth of 4.3 percent seen for crops is somewhat below the long-term average, given the 6.2 percent average annual growth seen for Ethiopia's crop sector over the past decade.

- Among cereals, growth was particularly strong for teff and maize (both up 7.5 percent) as well as wheat (up 4.1 percent); these three crops—together with sorghum and barley—make up Ethiopia's top 5 cereal crops.

- Among pulses and oilseeds, the strongest growth was seen in soya beans, mung beans, and oilseeds—all of which grew strongly from depressed levels in the prior year.

Figure 1A: Agricultural Production and Growth

Agricultural Production (Mns of tons)

	2015-16	2016-17	2017-18	2018-19	Estimates 2019-20
Major Crops	**26.7**	**29.0**	**30.6**	**31.6**	**32.9**
Cereals	**23.1**	**25.4**	**26.8**	**27.8**	**29.1**
of which:					
Maize	7.2	7.9	8.4	9.5	10.2
Teff	4.5	5.0	5.3	5.4	5.8
Sorghum	4.3	4.8	5.2	5.0	5.1
Wheat	4.2	4.5	4.6	4.8	5.0
Pulses	**2.8**	**2.8**	**3.0**	**3.0**	**3.0**
Oilseeds	**0.8**	**0.8**	**0.9**	**0.8**	**0.8**

Growth Rates--PRODUCTION

	2015-16	2016-17	2017-18	2018-19	Projection 2019-20
Major Crops	-1.3%	8.8%	5.4%	3.1%	4.3%
Cereals	-2.0%	9.8%	5.5%	3.7%	4.8%
Pulses	3.6%	1.6%	5.8%	1.1%	-0.3%
Oilseeds	3.2%	6.9%	1.9%	-8.2%	4.0%

Source: CSA's Agricultural Sample Survey Reports, Ministry of Agriculture

Table 1B: Ethiopia's Major Crops, Harvest Output, and Growth rates

Ranked by Growth Rate within each category

	Production, Mns of Quintals, FY 2017-18	Production, Mns of Quintals, FY 2018-19	Percent change
Total Crops	**315.6**	**329.3**	**4.3%**
Cereals	**277.6**	**291.1**	**4.8%**
Teff	54.0	58.1	7.5%
Maize	94.9	102.0	7.5%
Wheat	48.4	50.4	4.1%
Sorghum	50.2	51.1	1.7%
Barley	17.7	17.5	-0.9%
Rice	1.7	1.7	-1.3%
Finger Millet	10.4	10.1	-2.5%
Oats/'Aja'	0.3	0.2	-25.1%
Pulses	**30.1**	**30.0**	**-0.3%**
Soya Beans	1.5	2.1	39.6%
Gibto	0.2	0.3	35.1%
Mung bean "Masho"	0.6	0.8	33.0%
White Haricot beans	1.5	1.7	13.7%
Lentils	1.4	1.5	5.1%
Field Peas	3.6	3.7	2.1%
Grass Peas	2.6	2.6	0.9%
Faba Beans	10.4	10.2	-2.6%
Red - Haricot beans	3.4	3.2	-6.6%
Red Chick-Peas	3.3	3.0	-10.3%
White Chick-Peas	1.3	0.9	-31.6%
Fenugreek	0.3	0.2	-32.2%
Oilseeds	**7.9**	**8.2**	**4.0%**
Sesame	2.0	2.6	30.3%
Groundnut	1.4	1.6	12.2%
Neug	3.0	2.8	-4.7%
Sufflower	0.1	0.1	-5.3%
Linseed	1.0	0.8	-14.9%
Rapeseed	0.4	0.2	-49.1%
Potatoes	10.4	9.5	-8.9%
Taro / 'Godere'	14.6	15.9	8.8%
Sweet potatoes	14.9	15.3	2.9%

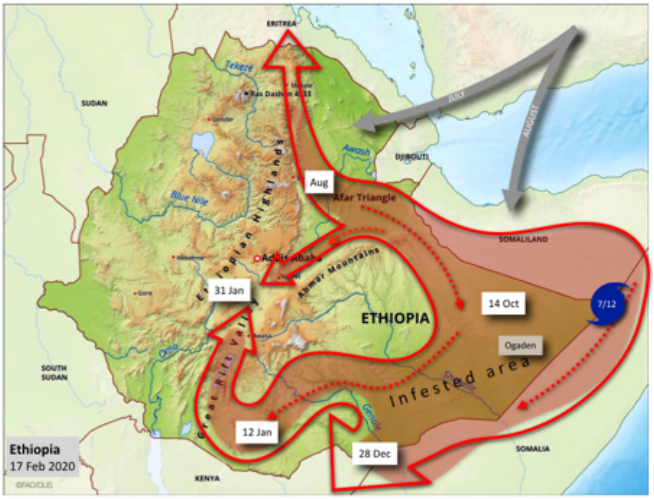
Source: CSA

Growth outlook:

- Though there have been concerns about agriculture growth being affected this year due to the locust infestation in many parts of East Africa, our assessment of FAO and the Ministry of Agriculture information releases suggests there will not be a material impact.

- FAO reviews as of February 2020 show that most of the locust infestations occurred either in areas with limited crop production or well after Ethiopia's harvest season.

Figure 2A: Locust infestation--affected areas and approximate dates



Source: UN FAO, February 17, 2020

- Moreover, estimates of locust-infested areas by the Ministry of Agriculture are that a total of 70,000 hectares have been affected across different parts of the country.

- This figure is only 0.55 percent of Ethiopia's total crop land (12.7 million hectares). Even if all the crops in those affected areas were assumed lost (an extreme case), the impact on the overall economy would be just 0.2 percent of GDP (as crop output is just 33 percent total GDP).

Table 2B: Estimated Impact of Locust Infestation

	Hectares, mns
Total Land Covered by Crop Production in 2018-19:	12,773,912
Locust-affected land, in hectares*	70,000
Locust-affected land, percent of all crop land	0.55%
	Quintals, mns
Total Output from all Crops in 2018-19	329.2
Potentially locust-affected crop volumes	1.8
Locust-affected land, percent of all crop land	0.55%
Potential Agricultural GDP impact:	-0.55%
Share of Agriculture in total GDP:	33.30%
Potential Total GDP impact:	-0.18%

**Per Ministry of Agriculture February 2020 estimate of locust-affected land*

Growth outlook—continued:

- Beyond agriculture, activity indicators in the wider economy point to generally positive trends up to end-December (or end-September depending on data availability), though there are notable weaknesses in some areas.

- The weak spots include a slowdown in FDI inflows (down 25 percent for the first six months of the fiscal year), a slower rate of SOE bond borrowing (negative in real terms and suggesting lower investment), lower capital goods imports, and a moderation of deposit growth at banks.

Figure 2C: Activity Indicators for First Quarter and First Half of Fiscal Year

Data available to end-Sept 2019	FY 2018-19 Q1	FY 2019-20 Q1	Nominal growth	Real growth
Fuel consumption (Tons)	907	1,010	...	11.4%
Electricity power generation (Kwh mns)	1,787.4	3,697	...	106.9%

Data available to end-Dec 2019	FY 2018-19 HI	FY 2019-20 HI	Nominal growth	Real growth
Tax collections	**98.60**	**127.50**	**29.3%**	**13.5%**
o/w Direct tax collections	*61.61*	73.95	*20.0%*	*4.2%*
o/w Trade tax collections	*36.95*	53.6	*44.9%*	*29.1%*
Deposit levels	793	960.37	21.1%	5.3%
Loan levels	403	525.24	30.5%	14.6%
Ethio Telecom (Total Subscribers in mns)	41.1	45.6	...	10.9%
Ethio Telecom Revenue	16.7	22.0	...	32.0%
FDI ($bns)	1,828	1,362	...	-25.5%
Industrial parks exports ($mns)	69.56	93.79	...	34.8%
Industrial parks employment	63,968	86,246	...	34.8%
Tourist arrivals	380,376	422,198	...	11.0%
Employment created (JCC)	821,000	1,184,868	...	44.3%
Private		*920,155*	...	
Govt		*254,101*	...	
Others		*10,612*	...	

Source: NBE, Ministry of Transport, Ministry of Revenue, Banks survey data, Jobs Creation Commission .
For calculating real growth ,year-average inflation used for flow variables (taxes) and year-end inflation used for stock variables (deposits, loans)

- Areas suggesting still-positive and expanding economic activity include tax collections (up 29 percent in nominal terms, or 13 percent in real terms), lending growth (up 31 percent in nominal terms), industrial park exports, tourist arrivals, and fuel consumption (in volume terms).

Figure 2D: Recent Investment Indicators

	FY 2018-19 Q1	FY 2019-20 Q1	Percent change
First Quarter Performance*			
SOE bond borrowing (Birr bns)	293.2	341.6	**16%**
Govt Capital Expenditure (Birr bns)	21.1	27.2	**29%**

Half Year Performance*	FY 2018-19 H1	FY 2019-20 H1	Percent change
Capital Goods Imports (USD bns)	3.0	2.3	**-23%**
Foreign Direct Investment (USD bns)	1.83	1.36	**-26%**

** Depending on lags in data availability, figures reported are either for Sept 2019 or Dec 2019.*
Source: NBE quarterly bulletin, MOTI,ERCA. EIC

Growth outlook—continued:

- Taken all together, i.e., considering 4 percent crop growth as well as proxies for construction and services activity, we expect that overall GDP growth can reach 8 percent for the fiscal year.

Figure 2E: Growth Projection by Sector

	2016-17	2017-18	2018-19	Projection 2019-20
Overall GDP	**10.1**	**7.7**	**9.0**	**8.0**
Agriculture	**6.7**	**3.5**	**3.8**	**4.5**
Of which: Major crops	*8.2*	*4.7*	*3.1*	**4.3**
Industry	**20.3**	**12.2**	**12.6**	**12.0**
Of which: Construction	*20.7*	*15.7*	*15.0*	*14.0*
Of which: Large Manufacturing	*19.2*	*6.0*	*7.7*	*8.0*
Services	**7.2**	**8.8**	**11.0**	**8.3**

Source: MOFEC and NBE for historical data, Cepheus projection for FY 2019-20

- Our growth projection is somewhat above the average growth forecasts of various institutions, per our compilation.

- Our slightly higher projection (versus the average of all others) likely reflects our incorporation of recent data on this year's crop harvest and of end-December banking, tax, and services indicators.

Table 2F: Growth Projections for Ethiopia, FY 2019-20

Institution	Growth Proj
Ethiopia's Ministry of Finance	9.0%
International Monetary Fund	6.2%
World Bank	6.3%
African Development Bank	7.1%
Economic Commission for Africa	7.5%
Economist Intelligence Unit	7.1%
Renaissance Capital	7.2%
Focus Economics	7.6%
Standard & Poor's	8.0%
Fitch	7.3%
Moody's	7.5%
Standard Bank	7.8%
AVERAGE of above projections:	7.4%
Cepheus Capital	8.0%

Source: MOFEC and websites/reports of the respective institutions

PRICES AND INFLATION: Recent Developments and Outlook

Inflation outturns:

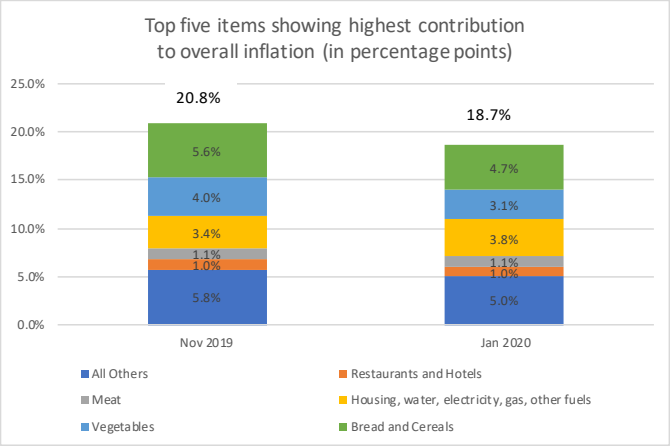
- Year-on-year inflation was 18.7 percent in January 2020, and has now shown double-digit rates for over two years and remained above 15 percent for 17 months.
- After an extended period of moderate inflation, services inflation is now nearing 20 percent, driven by items such as housing, electricity, and transport costs.
- We find the persistence of inflation inconsistent with some recent developments (i.e., positive food harvests, restored transport links, and moderating money supply growth), and its underlying sources may thus be better explained and driven by (self-fulfilling) public expectations.
- If expectations have become the dominant influence for inflation, only a convincing break from past policies and a disciplining macro framework can help alter expectations—in which case the recent Govt-IMF macro program may begin to make a difference.

Figure 4A: Inflation Outturns by key analytical categories -- January 2020

	Weight in CPI index	Weights within	Inflation (M-o-M)	Inflation (Y-o-Y)
A. Domestically Produced and Domestically Consumed				**20.1%**
1 Bread and Cereals	*17.1%*	47%	-0.6%	27.3%
2 Alcoholic beverages and tobacco	*4.9%*	13%	-3.5%	3%
3 Other food products	*5.6%*	15%	4.4%	18%
4 Meat	*4.2%*	12%	1.5%	26%
5 Milk, Cheese, Eggs	*3.1%*	9%	2.3%	13%
6 Sugar, jam, honey and others	*1.4%*	4%	-7.5%	-1%
Sub-Total	*36.5%*	100%		
B. Domestically produced but also heavily exported				**22.2%**
7 Vegetables	*12.3%*	70%	0.6%	25%
8 Non- alcoholic beverage and coffee	*5.1%*	29%	1.5%	15%
9 Fruits	*0.2%*	1%	2.2%	30%
Sub-Total	*17.6%*	*100.0%*		
C. Import-Heavy Commodities				**10.0%**
10 Clothing and footwear	*5.7%*	33%	1.4%	9%
11 Furnishings, Household Equipment, and others	*4.7%*	27%	0.9%	10%
12 Oils and Fats	*4.3%*	25%	-1.9%	7%
13 Miscellaneous goods	*2.5%*	15%	1.7%	17%
Sub-Total	*17.2%*	*100.0%*		
D. Services				**18.7%**
14 Housing, water, electricity, gas, other fuels	*17%*	59%	2.4%	22%
15 Restaurants and Hotels	*5.3%*	18%	0.0%	19%
16 Transport	*2%*	9%	2.2%	13%
17 Health	*1%*	5%	-3.7%	12%
18 Communication	*2%*	7%	-0.8%	-2%
19 Recreation and culture	*0%*	1%	3.3%	16%
20 Education	*0%*	1%	2.8%	10.2%
Sub-Total	*28.7%*	*100.0%*		
Overall inflation	**100%**		**0.7%**	**18.7%**

Source: CSA and Cepheus Research for categorizations; shaded figures are those items with highest weight in CPI index

Figure 4B: Top five items showing highest contribution to overall inflation

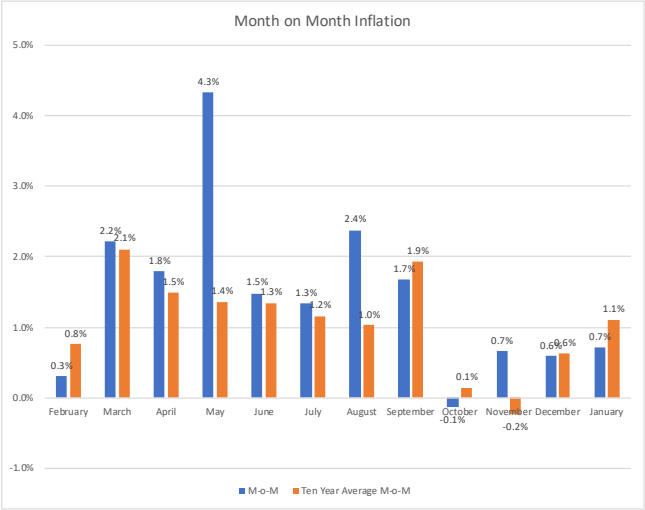


Source: CSA and Cepheus Research

Month on month inflation:

- One positive element within the most recent inflation data is that month-on-month inflation has been below its long-term norms the past two months, suggesting that it is mainly the accumulated price increases to date that are carrying over into high year-on-year inflation figures.

Figure 5: Month on Month Inflation



Source: CSA

Inflation projections:

- If the current pattern of month-on-month figures continues to mid-year, then inflation should begin to fall sharply by June 2020, as the index showed large jumps in mid-2019 and comparisons to mid-2020 will show more moderate year-on-year price increases.

- Though inflation has become difficult to forecast, and could continue to show one or two months of upside surprises in the period ahead, we still see it falling to around 13 percent by mid-June and to near 10 percent by December.

Figure 6: Inflation Projections to December 2020

	Price index	M-o-M inflation	Y-o-Y inflation
Actuals			
July 2019	146.3	1.3%	15.5%
August 2019	149.8	2.4%	17.9%
September 2019	152.3	1.7%	18.6%
October 2019	152.1	-0.1%	18.7%
November 2019	153.1	0.7%	20.8%
December 2019	154.0	0.6%	19.8%
January 2020	155.1	0.7%	18.7%
Projections			
February 2020	156.1	0.6%	19.1%
March 2020	157.7	1.0%	17.7%
April 2020	160.0	1.5%	17.3%
May 2020	161.4	0.9%	13.4%
June 2020	163.6	1.4%	13.3%
July 2020	165.7	1.2%	13.2%
August 2020	166.9	0.8%	11.4%
September 2020	170.2	2.0%	11.8%
October 2020	169.9	-0.2%	11.7%
November 2020	169.3	-0.3%	10.6%
December 2020	169.4	0.1%	10.0%

Source: CSA and Cepheus Research; M-o-M inflation projections guided by recent trends and historical medians

MONETARY POLICY: Recent developments and outlook

Monetary growth:

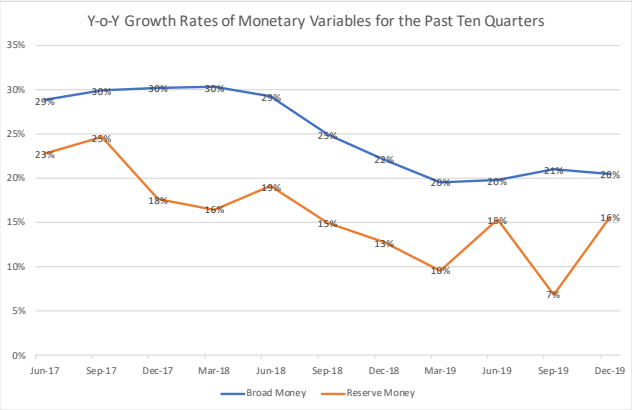
- Broad money growth has remained within the narrow 20-25 percent annual increases seen over the past year.
- With nominal GDP growth expected to be above 26 percent this year, the ratio of broad money to GDP will be falling this year (pointing to a decline in monetization, or the ratio of money-to-GDP, within the economy).
- Reserve money growth had fallen substantially at end-September but has now reverted back to growth of 15 percent. This is likely to moderate for the period ahead, given a 12.5 percent growth target set under the Government-IMF macro program.

Figure 7A: Broad Money and Reserve Money (Birr bns)

	June 2017	June 2018	Jun 2017	Dec 2018	June 2019	Dec 2019	% Change
Broad Money	**573.4**	**740.6**	**752.1**	**789**	**886.8**	**950.6**	**20.5%**
o/w Domestic credit	631.1	784.6	797.0	844.9	963.7	1,041.0	23.2%
o/w Net foreign assets	38.0	39.4	37.9	23.5	14.5	(14.6)	-162.2%
Reserve Money	**146.3**	**174.2**	**174.8**	**170**	**200.7**	**197.0**	**15.6%**
o/w Currency in circulation	94.2	112.9	110.9	120.3	121.8	128.1	6.4%
o/w Bank deposits at NBE	52.0	61.3	63.9	50.1	78.9	69.0	37.6%
Government Borrowing from NBE (net)	**116.6**	**140.2**	**147.1**	**155**	**172.2**	**173.3**	**11.9%**
o/w NBE credit to govt (gross)	135.6	160.1	166.7	178.7	194.7	204.2	14.3%
o/w Government deposits at NBE	19.0	19.9	19.6	23.8	22.5	30.9	30.1%

Source: NBE

Figure 7B: Y-o-Y growth Rates of Key Monetary Variables



Source: NBE Quarterly Reports

Domestic financing:

- Total financing supplied within the economy grew to 1.3 trillion as of end-September 2019, up around 26 percent from year-ago.
- The public sector's use of total domestic financing is now 64 percent, a slight decline from 68 percent at end-2018.
- By instrument, the share of bond-financing has risen to 36 percent, reflecting large SOE borrowings via bond issues to the CBE.

Figure 8A: Domestic Borrowing by Sector and Instrument

	June 2017	June 2018	June 2019	Sep 2019	% Total
Total Domestic Borrowing (Birr bns)	**831**	**1,026**	**1,256**	**1,296**	**100.0%**
By broad sector categories	**831**	**1,026**	**1,256**	**1,296**	**100.0%**
Public sector borrowers	568	696	819	840	64.9%
Private sector borrowers	264	329	436	455	35.1%
By borrower and instrument:	***831***	***1,026***	***1,256***	***1,296***	**100.0%**
Government	**278**	**341**	**388**	**400**	**30.9%**
o/w Bank loans	*43*	*54*	*54*	*54*	4.2%
o/w NBE loans (gross basis)	*128*	*152*	*187*	*192*	14.8%
o/w Bonds held by banks	*40*	*45*	*32*	*32*	2.4%
o/w Bonds held by NBE	*8*	*8*	*7*	*7*	0.6%
o/w Bonds held by non-banks	60	81	107	115	8.8%
State Enterprises	**290**	**356**	**432**	**440**	**34.0%**
o/w Bank loans	*92*	*110*	*125*	*126*	9.7%
o/w NBE loans	-	-	-	-	0.0%
o/w Bonds held by banks	*198*	*246*	*307*	*314*	24.2%
o/w Bonds held by NBE		-			0.0%
Private sector	**264**	**329**	**436**	**455**	**35.1%**
o/w Bank loans	*231*	*284*	*378*	*394*	30.4%
o/w MFI loans	*32*	*45*	*59*	*62*	4.8%
By instrument type:	***831***	***1,026***	***1,256***	***1,296***	**100.0%**
Loans	***526***	***646***	***803***	***828***	**63.9%**
o/w Bank loans	366	449	557	574	44.3%
o/w NBE loans	128	152	187	192	14.8%
o/w MFI loans	32	45	59	62	4.8%
Bonds	***306***	***380***	***453***	***468***	**36.1%**
o/w Bonds held by banks	238	291	339	346	26.7%
o/w Bonds held by NBE	8	8	7	7	0.6%
o/w Bonds held by non-banks	60	81	107	115	8.8%

Source: Cepheus categorization based on NBE Quarterly Bulletin
The "Government" line-item includes regional government borrowing.

Bank loans by sectors:

- Based on Sept 2019 data, the areas of fastest credit growth were housing and construction, domestic trade, exports and imports, and personal loans
- Industry remains the largest recipient of loans, largely reflecting SOE allocations at CBE

Figure 8B: Distribution of Bank Loans by Sector*

Outstanding Bank loans by Sector (Birr bn:	June 2017	June 2018	Sept 2018	June 2019	Sept 2019	% Change	% Total
Central Government	42.6	54.4	54.18	54.2	54.4	0.5%	9%
Agriculture	20.0	19.5	24.52	20.4	18.7	-23.7%	3%
Industry	130.0	154.9	169.47	188.7	194.6	14.8%	34%
Domestic Trade	41.8	44.9	55.99	65.4	68.8	22.9%	12%
International Trade	52.2	78.0	89.31	102.2	106.2	18.9%	19%
of which: Exports	30.0	47.8	58.08	66.1	68.8	18.4%	12%
of which: Imports	22.2	30.2	31.24	36.1	37.9	21.3%	7%
Hotels and Tourism	5.8	9.9	11.91	13.7	13.9	17.1%	2%
Transport & Communication	14.4	13.8	13.32	12.4	12.3	-7.7%	2%
Housing & Construction	38.0	43.6	41.49	51.3	53.4	28.6%	9%
Mines, Power & Water Resources	0.2	0.2	1.53	1.6	1.6	4.7%	0%
Others	16.4	23.0	8.41	5.9	9.6	13.7%	2%
Personal	4.3	6.7	32.46	40.8	40.1	23.5%	7%
TOTAL LOANS BY BANKS*	**365.6**	**449.0**	**502.6**	**556.6**	**574.0**	**14.2%**	100%

Source: NBE, Quarterly Bulletin
** Note this only covers loans provided by commercial banks, and thus excludes credit extended by banks in the form of bonds and also excludes credits given by NBE, MFIs, and non-banks.*
See Figure 8A for broader domestic financing sources, instruments and users.

Outstanding bond issuances:

- Growth in bond issuance is in line with the 15-20 percent seen recently.
- As before, EEPCO remains the largest bond issuer

Figure 9: Outstanding Bonds Issued as of Sept 2019

	June 2017	June 2018	Sep 2018	June 2019	Sep 2019	% Change
Total Bonds Outstanding (Birr bns)	**237.8**	**291.4**	**293.2**	**338.6**	**341.6**	**16%**
Public Enterprises	**198.2**	**245.5**	**248.1**	**306.8**	**314.2**	**27%**
EEPCO	179.3	216.4	216.35	263.9	271.3	25%
Railways Corporation	18.9	29.2	31.79	42.9	42.9	35%
Regional Government	**39.6**	**45.9**	**45.1**	**31.8**	**27.4**	**-39%**
Addis Ababa City Govt	39	45.3	44.53	31.2	26.9	-40%
Other Regions	0.6	0.6	0.6	0.6	0.5	-5%

Source: NBE, Quarterly Bulletin

BANKING: Recent developments

Deposit and lending trends:

- Overall deposit growth has moderated, to 21 percent, but is notably higher at 29 percent at private banks.
- The rapid pace of loan growth at private banks continued till end-2019, with their loan books up 44 percent from year ago levels.

Figure 10: Banking Trends (Birr bns)

	Jun 2017	Jun 2018	Dec 2018	Jun 2019	Dec 2019	Y-o-Y % Change
Bank deposits	**567.7**	**729.1**	**793**	**899**	**960**	**21%**
CBE	366.0	453.0	482	541	560	**16%**
Private Banks	201.7	276.0	311	358	401	**29%**
Bank loans outstanding	**289.8**	**355.4**	**403**	**456**	**525**	**30%**
CBE	157	177	185	197	212	**14%**
Private Banks	133	179	217	259	313	**44%**
Other indicators--all banks						
Assets	**745.2**	**914.1**	**1,003**	**1,165**	**1,261**	**26%**
Paid-up capital	**60.9**	**66.2**	**70**	**74**	**77**	**10%**
Branches	**3,888**	**4,442**	**5,211**	**5,164**	**5,607**	**8%**

Source: Bank Annual Reports and Bank Survey Data

FISCAL POLICY: Recent developments

Revenue performance:

- Tax collections continue to post positive results (Birr 127bn in six months), with the latest reading at end-December up 29 percent from last year.
- Trade taxes, which are boosted by the faster depreciation, did particularly well with growth of 44 percent from year-ago levels.

Figure 11: Revenue Performance, Birr bns

	FY 2018-19 H1	FY 2019-20 H1	% change
Taxes on domestic activity	**61.61**	**73.95**	**20.0%**
Direct tax	*35.30*	...	...
Indirect tax	*26.31*	...	...
Trade taxes	**36.95**	**53.6**	**44.9%**
Customs tarrif and tax	*35.75*	...	...
Non tax revenue	*1.20*	...	...
Lottery Sales	**0.11**	...	...
	-	...	...
TAX REVENUE TOTAL:	**98.67**	**127.50**	**29.2%**

Source: Ministry of Revenue

Budget performance:

- Full budget data (including expenditure outturns) are only available up to Sept 2019 and show spending growing in line with revenue growth, and the deficit appears to be in line with year-total levels (91bn for the fiscal year).

Figure 12:Budget Performance, Birr bns

	FY 2018-19 Q1	FY 2019-20 Q1	Percent change
Total revenue and grants	**52.5**	**66.0**	**26%**
Total Revenue	52.5	65.7	25%
Grants	-	0.3	...
Total Expenditure	**69.0**	**86.7**	**26%**
Current Expenditure	17.4	25.7	48%
Capital Expenditure	21.1	27.2	29%
Regional Transfers	30.5	33.8	11%
Deficit, Birr bns	**-16.5**	**-20.8**	**26%**
Deficit, percent of GDP	**-0.6%**	**-0.6%**	...
GDP (Birr bns)	**2,696.2**	**3,422.1**	**27%**

Source: NBE--Full budget data available only until September 2019

Public debt, in USD terms:

- Public debt is beginning to decline in levels and not just as a share of GDP; for end-Sept 2019, public debt was $53.6 bn, or down from its peak of $53.7bn.
- Public debt is now almost exactly split evenly between domestic and external debt

Figure 13: Public Debt, USD bns

	June 2017	June 2018	Sept 2018	June 2019	Sept 2019	% of Total
Total Public Debt	**$ 45.8**	**$ 49.5**	**$ 50.2**	**$ 53.7**	**$ 53.6**	**100.0%**
External debt	**$ 23.3**	**$ 25.9**	**$ 26.1**	**$ 27.0**	**$ 26.8**	**50.0%**
Central Government	$ 13.0	$ 14.7	$ 14.8	$ 16.0	$ 15.9	29.8%
State Owned Enterprises	$ 10.4	$ 11.2	$ 11.3	$ 11.1	$ 10.8	20.2%
Domestic Debt	**$ 22.4**	**$ 23.6**	**$ 24.1**	**$ 26.7**	**$ 26.8**	**50.0%**
Central Government	$ 10.3	$ 11.0	$ 11.4	$ 12.5	$ 12.7	23.8%
State Owned Enterprises	$ 12.1	$ 12.6	$ 12.7	$ 14.2	$ 14.0	26.2%

Source: MoFEC

Public debt, relative to GDP:

- Relative to this year's anticipated USD GDP, public debt as of Sept 2019 fell to just 48.9% of GDP. As new loans are contracted up to June 2020, this figure will rise modestly and should end the fiscal year in the low 50s as a share of GDP.

Figure 14: Public Debt, % GDP

	June 2017	June 2018	Sept 2018	June 2019	Sept 2019
Total Public Debt	**56.0%**	**58.7%**	**52.3%**	**55.9%**	**48.9%**
External debt	**28.5%**	**30.7%**	**27.2%**	**28.1%**	**24.4%**
Central Government	15.9%	17.4%	**15.4%**	16.6%	14.6%
State Owned Enterprises	12.7%	13.3%	**11.7%**	11.5%	9.9%
Domestic Debt	**27.5%**	**28.0%**	**25.1%**	**27.8%**	**24.5%**
Central Government	12.6%	13.1%	**11.9%**	13.0%	11.6%
State Owned Enterprises	14.8%	14.9%	**13.2%**	14.7%	12.8%
Memo items:					
GDP, Birr bns	1,717	1,834	1,987	1,987	3,422
Exchange rate, year avg	23.11	27.26	28.91	28.91	33.13
GDP, USD bns	$ 81.8	$ 84.4	$ 96.1	$ 96.1	$ 109.5

Source: MoFEC

External debt stocks:

- Total external debt is now just below 25 percent of USD GDP, one of the lowest levels in years.

Figure 15: External Debt (Public Sector), In USD bns

	June 2017	June 2018	Sept 2018	June 2019	Sept 2019	% of Total
Total External Debt of Public Sector, USD bns	**$ 23.3**	**$ 25.9**	**$ 26.1**	**$ 27.0**	**$ 26.8**	**100%**
Government	$ 13.0	$ 14.7	$ 14.8	$ 16.0	$ 15.9	60%
EAL & Ethio-telecom	$ 6.9	$ 7.6	$ 7.6	$ 7.3	$ 7.2	27%
Other State Enterprises	$ 3.4	$ 3.6	$ 3.7	$ 3.8	$ 3.7	14%
Total External Debt of Public Sector, % GDP	**28.6%**	**30.9%**	**27.4%**	**28.4%**	**24.4%**	**100.0%**
Government	15.9%	17.5%	15.6%	16.7%	14.6%	59.5%
EAL & Ethio-telecom	8.5%	9.0%	7.9%	7.6%	6.5%	26.8%
Other State Enterprises	4.2%	4.3%	3.9%	4.0%	3.4%	13.7%
GDP, USD bns	$ 81.6	$ 84.0	$ 95.3	$ 95.3	$ 109.5	...

Source: MoFEC

BALANCE OF PAYMENTS (BOP): Recent developments

Balance of payments:

- Full balance of payments data are only available to Sept 2019, though some components (exports, imports, FDI, reserves) are available and reported here for end-December 2019.
- The outturns for the first quarter of the fiscal year point to a marked drop in reserves that quarter, reflecting a drop in several current account items (services exports, remittances and grants) as well as large public sector debt repayments.
- Some of these items appear to have reversed, however, as reserves rose in the second quarter of the fiscal year (see below).

Figure 16: Balance of Payment, FY 2018-19

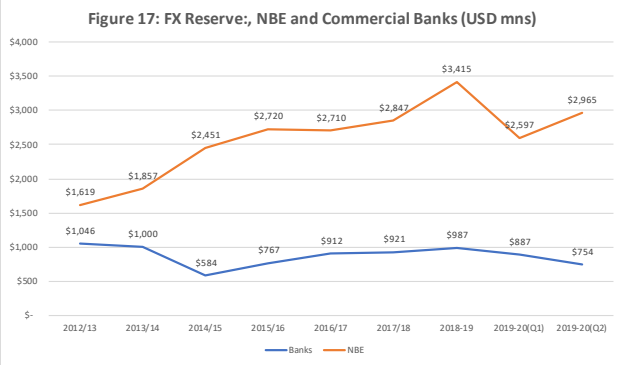
Balance of Payments in USD mns	FY 2018-19 Q1	FY 2019-20 Q1	Percent change
Exports	**628**	**723**	**15%**
Imports	**3,682**	**3,746**	**2%**
Trade Balance	**(3,054)**	**(3,024)**	**-1%**
	-	-	
Services, net	**264**	**75**	**-72%**
Non-factor services, net	**348**	**250**	-28%
Exports of non-factor services	**1,482**	**1,308**	-12%
Imports of non-factor services	**(1,134)**	**(1,058)**	-7%
Income, net	**(84)**	**(175)**	108%
O/w Gross official int. payment	**104**	**195**	87%
Dividend	-	-	0%
Private transfers, net	**1,598**	**1,344**	**-16%**
O/w: NGO's,(Net)	-	-	
Remittances	**1,422**	**1,138**	-20%
	-	-	
Current account balance excluding grants	**(1,192)**	**(1,605)**	**35%**
Official transfers, net	**352**	**187**	-47%
Current account balance including grants	**(840)**	**(1,418)**	**69%**
	-	-	
Capital account	**965**	**550**	**-43%**
Official Long-term Capital, net	**172**	**161**	-7%
Disbursements	**217**	**276**	27%
Amortization	**45**	**115**	158%
Other public long-term capital	**74**	**(287)**	-489%
Private sector, long term	**76**	**36**	-53%
Foreign Direct Investment, net	**689**	**700**	2%
Short term Capital	**(46)**	**(60)**	28%
	-	-	
Errors and omissions	**(194)**	**(3)**	**-99%**
	-	-	
Overall balance	**(69)**	**(871)**	**1160%**
	-	-	
Financing	**69**	**871**	**1160%**
	-	-	
Reserves [Increase(-), Decrease (+)]	**69**	**871**	1160%
Central Bank (NFA)	**284**	**758**	167%
Asset	**(897)**	**818**	-191%
Liabilities	**1,181**	**(60)**	-105%
Commercial banks (NFA)	**(215)**	**113**	-152%

Source: NBE Quarterly Bulletin

FX reserves:

- Fx reserves were around $3bn at end-December 2019, despite having dropped to as low as $2.6bn in Sept 2019.
- Official inflows, particularly funding received as part of the IMF program approved in Dec 2019, are likely to explain the year-end increase to near $3bn.

Figure 17: FX Reserves: NBE and Commercial Banks (USD mns)



Source: NBE, Quarterly Bulletin

TRADE PERFORMANCE: Recent developments

Export performance:

- Exports are performing moderately well, though the growth rate slowed from 15 percent at end-September to 11 percent at end-December 2019.

- Given $1.3bn in six-month exports, the full year export figure is unlikely to exceed $3bn. We forecast 8 percent growth in exports this year, for a full year figure of $2.9bn.

- Among large-value exports, the best performing exports this past quarter were flowers, fruits and vegetables, live animals, and textile products.

- Some export sub-components are showing record high levels, including flowers and textile products. On current trends, flowers are likely to become Ethiopia's second largest export after coffee, and textiles will not be that far behind (potentially fourth largest overall within the coming year).

Figure 18A: Export Performance

	FY 2018-19 H1	FY 2019-20 H1	Percent Change
Total Exports	**1,206.1**	**1,333.5**	**10.6%**
Coffee	333.94	365.4	9.4%
Oilseeds	149.37	107.3	-28.2%
Leather & Leather products	67.08	49.1	-26.8%
Pulses	110.35	98.1	-11.1%
Meat & Meat Products	48.10	35.4	-26.4%
Fruits & Vegetables	27.85	53.5	92.0%
Textile & Textile Products	68.65	99.9	45.5%
Flower	105.64	225.3	113.2%
Gold	19.37	13.5	-30.2%
Live Animals	19.06	32.7	71.3%
Chat	159.52	173.7	8.9%
Spices	4.92	10.3	109.0%
Cereals & Flour	1.0	1.6	60.8%
Natural Gum	1.70	3.5	105.2%
Electronics	19.89	8.7	-56.1%
Chemicals & Construction Inputs	8.8	4.5	-49.2%
Electricity	33.03	25.4	-23.0%
Bees Wax	1.03	0.94	-8.0%
Others	26.71	24.8	-7.3%

Source: MOTI, ERCA

Figure 18B: Export Performance--Ranked by Growth Rate

	FY 2018-19 H1	FY 2019-20 H1	Percent change
Total Exports, USD mns	**1,206**	**1,334**	**10.6%**
Ranked by growth rate:			
Flowers	105.64	225.3	113.2%
Spices	4.92	10.3	109.0%
Natural Gum	1.70	3.5	105.2%
Fruits & Vegetables	27.85	53.5	92.0%
Live Animals	19.06	32.7	71.3%
Cereals & Flour	1.0	1.6	60.8%
Textile & Textile Products	68.65	99.9	45.5%
Coffee	333.94	365.4	9.4%
Chat	159.52	173.7	8.9%
Others	26.71	24.8	-7.3%
Bees Wax	1.03	0.94	-8.0%
Pulses	110.35	98.1	-11.1%
Electricity	33.03	25.4	-23.0%
Meat & Meat Products	48.10	35.4	-26.4%
Leather & Leather products	67.08	49.1	-26.8%
Oilseeds	149.37	107.3	-28.2%
Gold	19.37	13.5	-30.2%
Chemicals & Construction Inputs	8.8	4.5	-49.2%
Electronics	19.89	8.7	-56.1%

Source: MOTI, ERCA

Export performance--continued

- Industrial park exports stalled in the latest quarter (down 2 percent between Sept and Dec), but are 28 percent above year-ago levels and are likely to exceed $200mn in annual exports this fiscal year

- The top three Industrial Parks with the best export performance are Hawassa IP, Bole Lemi IP, and Eastern IP

Import performance

- Overall imports are down 6 percent in the first half of the fiscal year, which would normally suggest weak domestic economic activity.

- However, a closer look at the data shows that this partly reflects declines in one-off aircraft imports (-94%) and in reduced fuel imports due to lower global oil prices (-6%). Excluding these two items, non-fuel and non-aircraft imports grew by 5 percent.

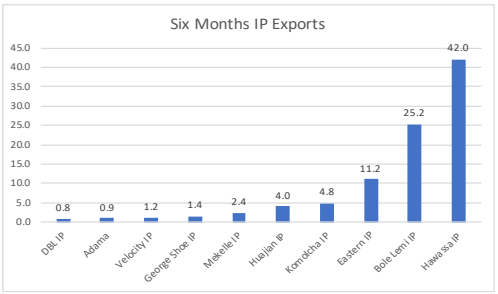
- Consumer goods were down 6 percent, likely reflecting the faster recent depreciation and an adjustment away from higher-cost consumer items.

- Capital goods imports were down overall—but mainly due to declines in aircraft imports. Capital goods related to agriculture were up 57% and those related to industry up 6%.

Figure 18C: Industrial Parks Exports: Quarterly Trends since 2018

Source:EIC

Figure 18D: Industrial Parks Exports: Six Months Performance



Source: EIC

Figure 19A: Import Performance

	FY 2018-19 H1	FY 2019-20 H1	% Change
Total Imports	**8,118**	**7,566**	**-6.8%**
Raw materials	**91.87**	**86.58**	**-6%**
Semi-finished goods	**1,186.46**	**1,411.80**	**19%**
Chemicals	214.18	320.08	49%
Fertilizers	14.58	31.51	116%
Textile materials	42.25	53.06	26%
Others	915.45	1,007.14	10%
Fuel	**1,336.92**	**1,232.65**	**-8%**
Crude petroleum	0.03	-	-100%
Petroleum products	1,264.55	1,188.24	-6%
Others	72.34	44.41	-39%
Capital goods	**3,020.78**	**2,330.66**	**-23%**
Transport	1,071.01	246.52	-77%
Aircraft	803.92	44.71	-94%
Agricultural	30.47	47.97	57%
Industrial	1,919.26	2,036.17	6%
Consumer Goods	**2,337.88**	**2,200.99**	**-6%**
Durables	611.57	527.80	-14%
Non-durables	1,726.31	1,673.19	-3%
Cereals	346.87	490.35	41%
Other Food	343.51	310.91	-9%
Medical & Pharmaceuticals	374.68	315.21	-16%
Textile Fabrics	207.10	221.32	7%
Others	454.15	335.39	-26%
Miscellaneous	**144.46**	**303.64**	**110%**
Non-fuel, non-aircraft imports	**5,977.53**	**6,288.95**	**5%**

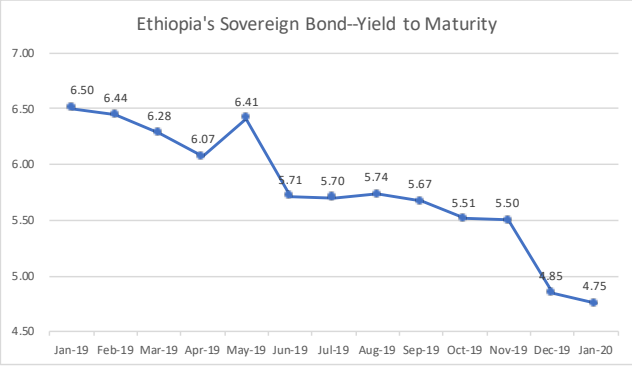
Source: MOTI, ERCA

ETHIOPIA'S SOVEREIGN BOND: Recent developments and outlook

Sovereign Bond Yields:

- Ethiopia's sovereign bonds have fallen to their lowest yields since they were issued five years ago in December 2014.
- This mainly reflects global factors (EM yields have fallen across the board), but Ethiopia also saw a distinct decline in yields following the IMF program announcement in early Dec 2019

Figure 20: Ethiopia's Soveregn Bond--Yield to Maturity

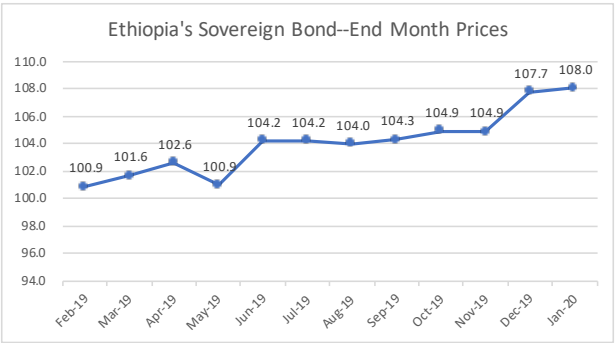


Source: FactSet

Sovereign Bond Prices:

- Bond prices are at historic highs, and holders of Ethiopia's Eurobonds have received a more than 15 percent total return in dollar terms for 2019 (given the 6.625% coupon on the bond plus a near 8% price appreciation).

Figure 21: Ethiopia's Sovereign Bond--End Month Prices

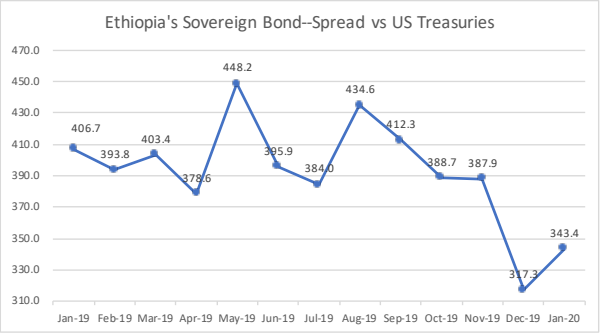


Source: FactSet

Spread vs US Treasuries:

- The gap between US 10-Year bonds and Ethiopia's 10-Year bond is also now at one of its lowest ever levels of just 3.43 percentage points.

Figure 22: Ethiopia's Sovereign Bond--Spread vs US Treasuries



Source: FactSet

EXCHANGE RATE: Recent developments and outlook

Exchange rate trends:

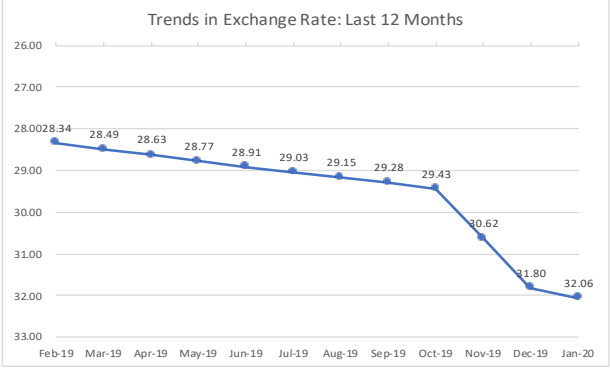
- After two months of sharp depreciations in November and December (1.2 Birr per month), exchange rate adjustments have moderated more recently—as we expected—and are now averaging 22 cents per month.

- The exchange rate has now depreciated by 14 percent from year-ago levels (32.28 at end-February 2020 vs 28.34 at end February 2019).

- Continuing the current pace of Birr depreciation, i.e. 22 cents per month, would move the exchange rate by 8 percent in a year's time. We think the central bank would aim for a somewhat higher annual rate of depreciation, given inflation differentials between Ethiopia and its trading partners and the need to maintain external competitiveness.

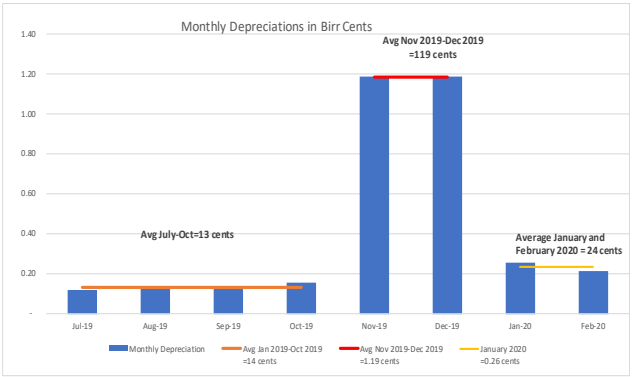
- An annual depreciation of between 10-15 percent is thus more likely to be targeted, in our view, implying somewhat higher monthly depreciations in the latter half of 2020. On this basis, we see the rate reaching 33.16 Birr/USD by end-June and just under 36 Birr/USD by end-December.

Figure 23: Trends in Exchange Rate: Last 12 Months



Source: CBE FX Rates

Figure 24: Monthly Depreciations in Birr Cents



Source: CBE website FX Rates.

Figure 25: Exchange Rate: Forecasts to End-2020

Actuals: End Month	Buying Rate	Selling Rate	Depreciation from year ago
July 2019	29.03	29.61	6.1%
August 2019	29.15	29.74	6.1%
September 2019	29.28	29.86	6.1%
October 2019	29.43	30.02	6.1%
November 2019	30.62	31.23	9.8%
December 2019	31.80	32.44	13.4%
January 2020	32.06	32.70	13.7%
Projections: End Month			
February 2020	32.28	32.93	13.9%
March 2020	32.50	33.15	14.1%
April 2020	32.72	33.38	14.3%
May 2020	32.94	33.60	14.5%
June 2020	33.16	33.82	14.7%
July 2020	33.41	34.08	15.1%
August 2020	33.66	34.33	15.5%
September 2020	33.91	34.59	15.8%
October 2020	34.36	35.05	16.8%
November 2020	35.11	35.81	14.7%
December 2020	35.96	36.68	13.1%

Source: CBE website for historical data and Cepheus Research for projections

ETHIOPIA--Key Macroeconomic Indicators: 2011 to 2021

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	FY 2020/21
	Actual	*Actual*	*Actual*	*Actual*	*Actual*	*Actual*	*Actual*	*Actual*	*Actual*	*Projection*	*Projection*
Real Sector: GDP, Prices, and Investment											
Real GDP growth	11.4%	8.7%	9.9%	10.3%	10.4%	8.0%	10.2%	7.7%	9.0%	8.0%	7.5%
Agriculture growth	*9.0%*	*4.9%*	*7.1%*	*5.4%*	*6.4%*	*2.3%*	*6.7%*	*3.5%*	*3.8%*	*4.5%*	*4.0%*
Industry growth	*18.6%*	*19.7%*	*24.0%*	*17.1%*	*19.9%*	*20.5%*	*20.3%*	*12.2%*	*12.6%*	*12.0%*	*12.0%*
Services growth	*17.0%*	*9.6%*	*9.0%*	*13.0%*	*11.1%*	*8.6%*	*7.2%*	*8.8%*	*11.0%*	*8.3%*	*7.5%*
Inflation: CPI (end-of-period)	38.1%	20.7%	7.4%	8.5%	10.4%	7.5%	8.8%	14.7%	15.3%	13.3%	10.0%
Inflation: CPI (period average)	18.1%	34.1%	13.5%	8.1%	7.7%	9.7%	7.2%	13.1%	12.6%	17.5%	10.0%
Nominal GDP growth	31.6%	45.1%	16.0%	22.4%	22.4%	20.8%	16.9%	20.0%	22.5%	26.9%	18.3%
Nominal GDP level (Birr billions)	515.1	747.3	866.9	1,060.8	1,298.0	1,568.1	1,832.8	2,200.1	2,696.2	3,422.1	4,047.0
Nominal GDP level (USD billions)	$ 32.0	$ 43.2	$ 47.6	$ 55.5	$ 64.5	$ 74.1	$ 81.6	$ 83.9	$ 95.9	$ 109.5	$ 114.5
GDP per capita (USD)	$ 392	$ 516.4	$ 554.0	$ 631.1	$ 715.8	$ 803.9	$ 864.6	$ 869.3	$ 971.8	$1,086.2	$ 1,112.1
Exchange rate (Birr/USD, end-of-period)	16.82	17.73	18.64	19.58	20.57	21.80	23.11	27.26	28.91	33.16	37.50
Exchange rate (Birr/USD, year-average)	16.10	17.28	18.23	19.11	20.13	21.16	22.47	26.23	28.12	31.25	35.33
Exchange rate annual depreciation (year-average)	24.8%	7.3%	5.5%	4.8%	5.3%	5.1%	6.2%	16.7%	7.2%	11.1%	13.1%
Investment-to-GDP ratio	27.2%	34.6%	32.6%	38.0%	39.3%	37.3%	38.4%	34.7%	35.2%	34.0%	36.5%
By investor category:											
Public sector investment-to-GDP ratio	19.6%	26.1%	24.3%	17.0%	17.6%	16.8%	14.4%	12.8%	11.0%	11.0%	10.5%
Private sector investment-to-GDP ratio	7.6%	8.5%	8.3%	21.0%	21.7%	20.5%	24.0%	21.9%	24.2%	23.0%	26.0%
By source of financing:											
Domestic Savings-to-GDP ratio	12.8%	16.5%	15.9%	20.5%	21.8%	22.4%	22.4%	24.1%	24.0%	23.5%	24.5%
External Savings-to-GDP ratio	14.4%	18.1%	16.7%	17.5%	17.5%	14.9%	16.0%	10.6%	11.2%	10.5%	12.0%
Banking Sector	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	FY 2020/21
Deposits at all commercial banks (Br bn)	143.3	189.3	237.8	292.9	366.5	436.7	567.7	729.1	899.1	1,087.9	1,305.5
Loans by all commercial banks (Br bn)	61.9	85.4	116.5	145.6	189.3	232.1	289.8	355.4	456.1	592.9	758.9
NBE Bills held by all comm banks (Br bn)	3.0	11.0	19.1	25.1	37.4	49.9	54.6	70.1	88.8	85.1	68.0
Bonds held by all commercial banks (Br bn)	43.1	64.5	82.8	111.8	152.7	188.7	237.8	291.4	338.6	399.5	459.5
Total bank financing: Loans/Bills/Bonds (Br bn)	108.0	160.9	218.4	282.5	379.4	470.7	582.2	716.9	883.5	1,077.5	1,286.4
Deposit-to-GDP ratio (%)	27.8%	25.3%	27.4%	27.6%	28.2%	27.8%	31.0%	33.1%	33.3%	31.8%	32.3%
Total bank financing-to-Deposit ratio (%)	75.3%	85.0%	91.8%	96.5%	103.5%	107.8%	102.5%	98.3%	98.3%	99.0%	98.5%
Total commercial bank financing-to-GDP ratio (%)	21.0%	21.5%	25.2%	26.6%	29.2%	30.0%	31.8%	32.6%	32.8%	31.5%	31.8%
Annual growth in bank deposits (%)	40.0%	32.1%	25.6%	23.2%	25.1%	19.2%	30.0%	28.4%	23.3%	21.0%	20.0%
Annual growth in total bank financing (%)	50.7%	49.0%	35.7%	29.4%	34.3%	24.1%	23.7%	23.1%	23.2%	22.0%	19.4%

Data Sources: NBE, MOFEC, CSA, and IMF for historical data series; Cepheus Capital Research for some estimates and for projection years.

ETHIOPIA--Key Macroeconomic Indicators: 2011 to 2021

Fiscal Sector	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	FY 2020/21
Revenue and grants (Birr bns)	85.6	115.7	137.2	158.1	199.6	243.7	269.1	287.6	344.9	425.3	566.2
Expenditure (Birr bns)	93.8	124.4	153.9	185.5	230.5	272.9	329.3	354.2	413.1	509.8	655.8
Fiscal balance after grants (Birr bns)	-8.2	-8.7	-16.7	-27.4	-30.9	-29.3	-60.2	-66.6	-68.2	-84.5	-89.6
Revenue and grants (% GDP)	16.6%	15.5%	15.8%	14.9%	15.4%	15.5%	14.7%	13.1%	12.8%	12.4%	14.0%
Expenditure (% GDP)	18.2%	16.6%	17.8%	17.5%	17.8%	17.4%	18.0%	16.1%	15.3%	14.9%	16.2%
Fiscal balance after grants (% GDP)	-1.6%	-1.2%	-1.9%	-2.6%	-2.4%	-1.9%	-3.3%	-3.0%	-2.5%	-2.5%	-2.2%
Public Sector Debt (% GDP)	36.2%	30.6%	41.9%	45.7%	52.9%	52.4%	55.2%	59.0%	56.0%	51.7%	52.1%
External Debt (% GDP)	24.4%	20.6%	23.6%	25.2%	29.6%	29.0%	28.7%	30.9%	28.2%	26.1%	26.5%
Domestic Debt (% GDP)	11.9%	10.1%	18.3%	20.5%	23.3%	23.4%	26.5%	28.1%	27.8%	25.6%	25.6%

External Sector: Balance of Payments	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	FY 2020/21
Exports of goods (USD mn)	2,747	3,153	3,116	3,300	3,019	2,868	2,908	2,840	2,667	2,880	3,168
Exports of services (USD mns)	2,586	2,811	2,853	3,174	3,028	3,196	3,331	4,220	4,949	5,196	5,612
Imports of goods (USD mn)	(8,253)	(11,018)	(11,461)	(13,712)	(16,458)	(16,725)	(15,803)	(15,253)	(15,112)	(15,036)	(16,239)
Imports of services (USD mns)	(1,828)	(2,639)	(2,281)	(2,461)	(3,107)	(3,442)	(3,393)	(3,983)	(4,910)	(5,401)	(5,941)
Remittances (USD mn)	2,032	2,401	2,489	2,968	3,797	4,420	4,428	5,121	5,693	5,978	6,456
Private transfers (USD mn)	715	845	1,086	1,071	1,085	2,008	1,058	953	683	717	753
Foreign official grants (USD mn)		1,788	1,530	1,461	1,508	1,391	1,428	1,226	2,087	1,800	1,600
Current account balance (USD mn)	(210)	(2,755)	(2,781)	(4,352)	(7,401)	(6,657)	(6,528)	(5,253)	(4,534)	(4,556)	(5,407)
Current account balance (% GDP)	-0.7%	-6.4%	-5.8%	-7.8%	-11.5%	-9.0%	-8.0%	-6.3%	-4.7%	-4.2%	-4.7%
Foreign direct investment (USD mn)	1,243	1,072	1,232	1,467	2,202	3,269	4,171	3,723	3,015	3,500	5,050
Net foreign borrowing: Govt (USDmn)	2,073	938	1,270	2,309	3,352	1,628	1,402	1,632	1,158	1,500	1,647
Net foreign borrowing: Public Sector (USDmn)		231	882	332	2,347	1,052	626	937	1,326	300	400
Overall External Balance (USD mn)	1,446	(1,067)	(7)	(97)	(521)	(831)	659	(201)	58	644	1,743
Stock of Foreign Reserves, (USD mn)	3,044	2,262	2,368	2,496	3,249	3,402	3,197	2,843	3,415	4,059	5,802
Stock of Foreign Reserves, months imports	4.4	2.5	2.5	2.2	2.4	2.4	2.4	2.2	2.7	3.2	4.3
External Debt Stock (Public Sector, USD bn)	7.8	8.9	11.2	14.0	19.1	21.5	23.4	25.9	27.0	28.5	30.3
External Debt Stock (Public Sector, % GDP)	24.4%	20.6%	23.6%	25.2%	29.6%	29.0%	28.7%	30.9%	28.2%	26.1%	26.5%
Growth of Goods Exports	37.1%	14.8%	-1.2%	5.9%	-8.5%	-5.0%	1.4%	-2.3%	-6.1%	8.0%	10.0%
Growth of Goods Imports	-0.2%	33.5%	4.0%	19.6%	20.0%	1.6%	-5.5%	-3.5%	-0.9%	-0.5%	8.0%

Market Ratings and Sovereign Bond Performance											
Country Ratings	...	...	...	...							
Standard and Poor's	...	...	...	...	B	B	B	B	B	B	...
Fitch	...	...	...	...	B	B	B	B	B	B	...
Moody's					B1	B1	B1	B1	B1	B1	...
Ethiopia Sovereign Bond: $1bn issued Dec 2014											
Yield in percent (fiscal year average)	...	...	...	...	6.83%	7.96%	7.40%	6.34%	6.64%	...	...
Yield in percent (end fiscal year)	...	...	...	...	6.70%	8.07%	6.79%	7.06%	5.71%	...	...

Data Sources: NBE, MOFEC, CSA, and IMF for historical data series; Cepheus Capital Research for some estimates and for projection years.

Economic and Business News
Fourth Quarter 2019: October 1 – December 31, 2019

The compilation of economic and business news reports normally presented in our Quarterly Macroeconomic Reviews is available to readers at our website at https://cepheuscapital.com/insights/

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