ETHIOPIA

Quarterly Economic Brief

United Nations Development Programme

1. Overview

The Ethiopian economy continues to show good prospects and has maintained a Strong growth momentum under a manageable inflationary environment. The public investment in major infrastructure projects is still driving the growth coupled with expansion in the services sector. According to national income data, the service sector contributed over 50% of the growth followed by agriculture contributing one-third of the growth and the balance by the industrial sector (MoFED, 2014).

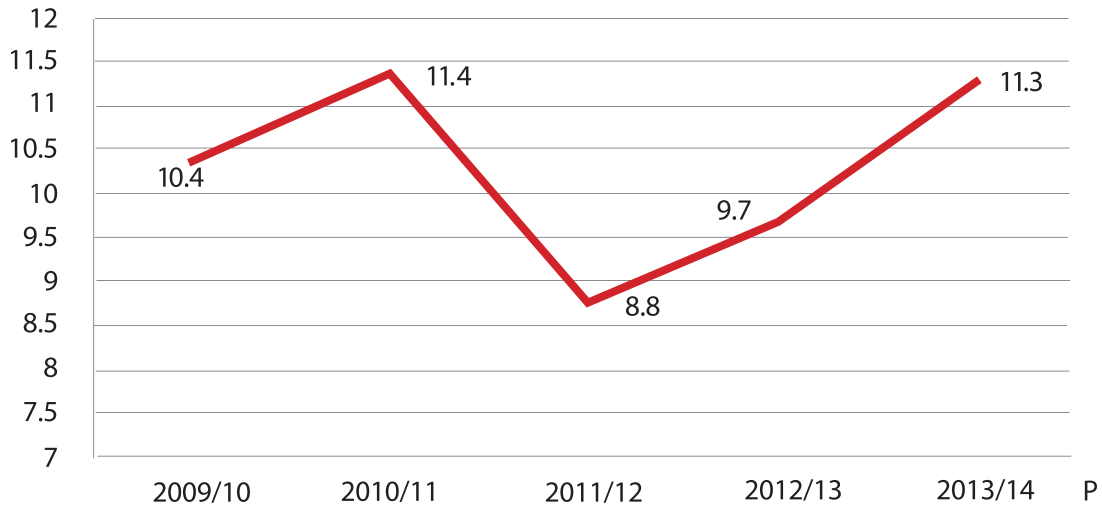
To sustain the growth trajectory, there is need to adapt policies to provide greater scope for a robust private sector-led development. Consequently, the Government is taking steps to improve the business environment and export competeviness. With support of UNDP, the Maritime Affairs Authority has undertaken a diagnostic study under the National Logistics Strategy for Ethiopia with the aim of bringing efficiency gains in the external sector. These efforts must be accompanied by deliberate steps to enhance the performance of the manufacturing sector and catalyze industrial transformation by putting in place incentive packages for value-addition.

To further augment support and partnership in private sector development, UNDP is currently working with the inistry of Finance and Economic Development an Innovative Investment Facility that will mobilize resources to provide entrepreneurs with financial access. In addition, work is in progress to develop a framework on private equity and venture capital. These efforts will provide a strong platform for nurturing entrepreneurial capacity and accelerate inclusive growth.

2. Macroeconomic Trends

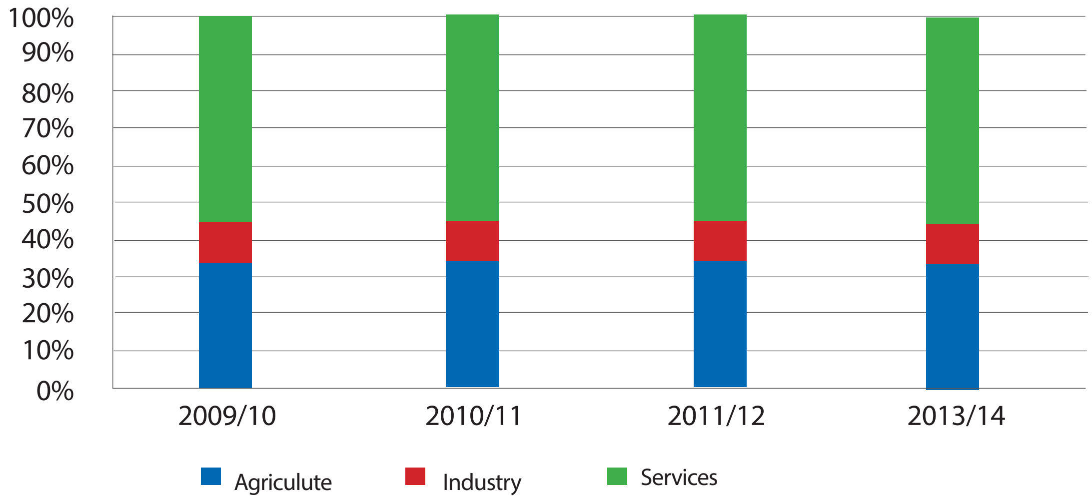
According to official forecasts, Ethiopia is expected to sustain the robust economic growth into the medium term. The economy is expected to register 11.3 percent real GDP growth in 2013/14 while the IMF projection is 8.5 percent growth. However, the economy will likely face challenges of remaining on the steady path of price stability, improving export competitiveness and increasing pressure in the financial system.

Figure 1 : Real GDP Growth (in %)



Source: MoFED, National Accounts, 2014

Figure2 : Contribution of Sectors to real GDP growth in %



Source: Calculated based on MoFED, National Accounts, 2014

The contribution of agriculture, service and industry sectors to the Gross Domestic Product, in the past five years (2008/09-2012/13), averaged 45, 44 and 11 percent, respectively. In terms of sector contribution to the growth trends, however, the services sector has stood out by contributing about 53 percent, while the contribution of agriculture was 31 percent and that of industry was 16 percent on average.

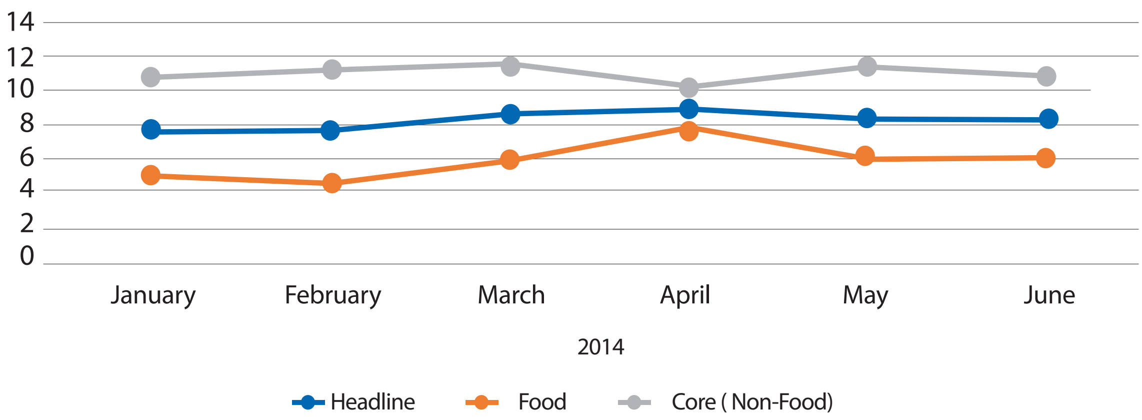
2.1 Price Developments

Inflation

Annual inflation remained in single digit throughout the fiscal year 2013/14. However, it had slightly increased and reached 9.1 percent in April 2014 but declined to 8.5 percent by end of 2013/14 in contrast to 7.4 percent in the same period last year. Generally the food category kept the inflation at single digit as the non-food inflation stubbornly remained above 10 percent for most of the period, even though both remained stable throughout the year.

Inflation in Ethiopia is mainly determined by the agricultural supply, as food and beverage category takes 53 percent of the household expenditure. In addition, the high import dependency has made the country prone to imported inflation. Accordingly, good harvest and favorable price conditions around the world and mainly by trading partners have cushioned the inflation to stay at single digit level.

Figure 3: Trends in Annual Inflation



Source: Central Statistical Agency

Interest Rates

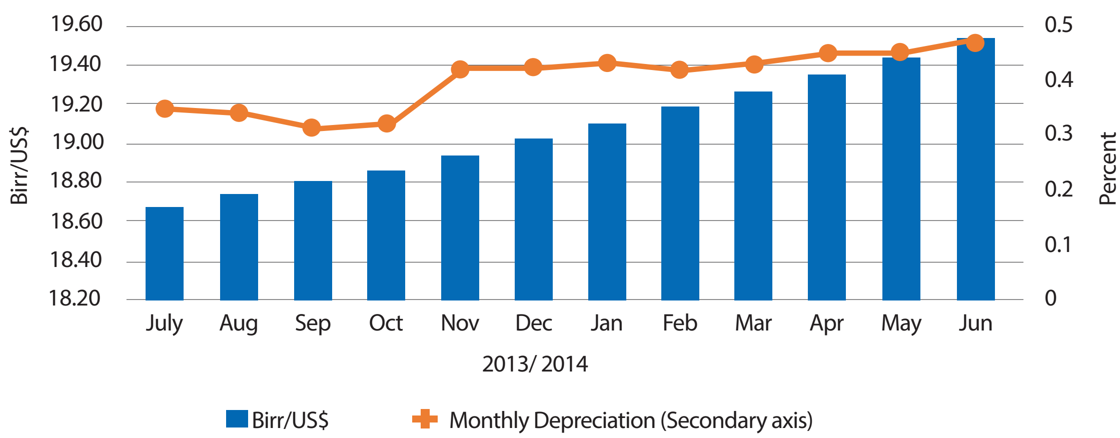
The nominal interest rate in Ethiopia do not change much (tend to be rigid) even though the central bank's policy is to setting the a minimum (floor) rate for deposits. The current floor is rate 5 percent under which commercial banks could freely decide how much to pay above the minimum and to set their own lending rates.

The average saving rate stood at 5.4 percent and average lending rate at 11.88 percent, during 2013/14. The real interest rates have remained negative due to rigid nominal interest rates and high inflationary regime. The IMF has recommended to the Government to develop and implement indirect monetary policy tools that could gradually raise the nominal interest rate.

Exchange Rate

By June, 2014 the exchange rate (Birr to USD) reached 19.53/Birr, showing a 4.9 percent annual depreciation Birr since June 2013. The National Bank of Ethiopia, intervenes in the foreign exchange market by supplying and buying foreign exchange to prevent high volatility in nominal exchange rate. The monthly depreciation rate has been relatively faster since November 2013 compared to the beginning of the fiscal year. (See fig 2)

Figure 4: Monthly Movements in exchange rate of Birr/US$ in 2013/14

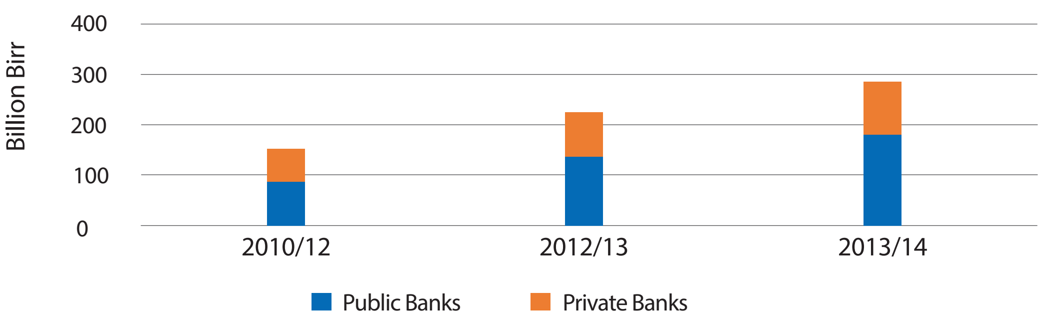


Source: National Bank of Ethiopia

2.2 Development in the financial sector

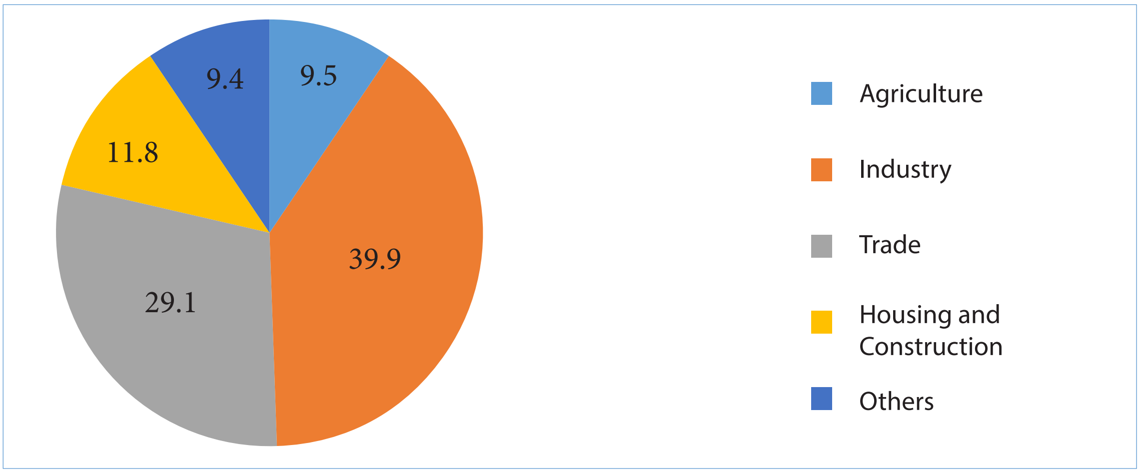
Ethiopia's financial sector constitutes 19 banks, 17 insurance companies, 31 micro finance institutions, social security agency and numerous credit cooperatives. The banking system has been growing especially in terms of branch networks. As of December 2013, the number of bank branches reached 2,015 in contrast 1,515 a year earlier. Majority of the bank branches are located in the capital city (33 percent) and the regional capitals. Deposit mobilization by the banks has increased by 23 percent between June 2013 and June 2014 to reach 292.8 billion birr, which is around 29 percent of GDP. The share of private banks in the deposit mobilization is 31.5 percent and remained the same on average in the past three years indicating the dominance of one bank, Commercial Bank of Ethiopia. The outstanding credit in the banking system has reached 168.3 billion birr (17 percent of GDP) by end of 2013/14, registering 24 percent annual growth. The credit disbursement of the banking systems seems to be in line with the priority given to the industry sector as 39.9 percent of the outstanding credit is held by this sector. 29.1 percent of the credit supported the trade sector, 11.8 percent housing and construction and 9.4 percent agriculture. Compared to the preceding year the share of outstanding credit to industry increased by 4 percentage points while that of agriculture declined by 3 percentage points. In terms of the clients, 68 percent of the outstanding bank credit is held by the private sector including cooperatives. Looking at the trend in quarterly fresh loan disbursements, as well, the private sector including cooperatives took 78 percent on average in 2013/14. (See figure 7)

Figure 5: Savings mobilized by the banking system (oustanding)



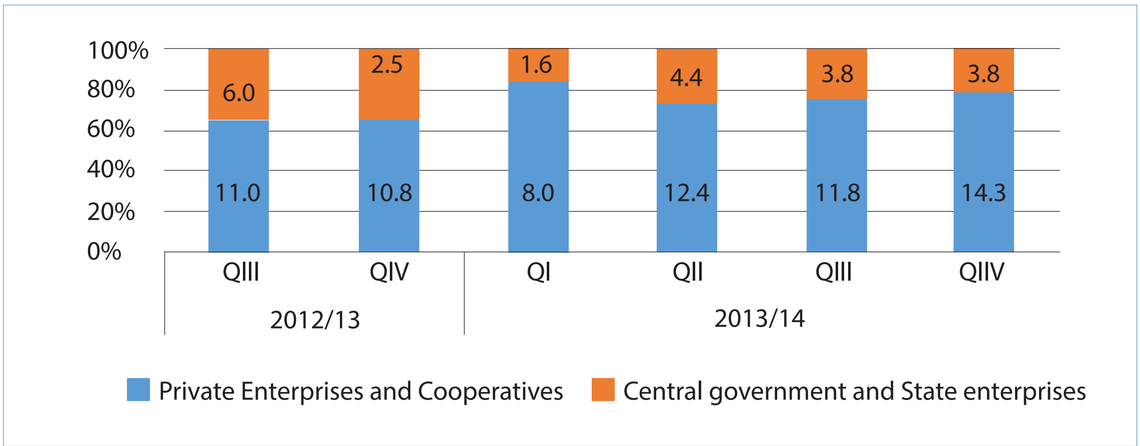
Source: National Bank of Ethiopia

Figure 6: Outstanding Credit by Sector in % (2013/14



Source: National Bank of Ethiopia

Figure 7: Quarterly trend in loan Disbursement by clients in billion Birr

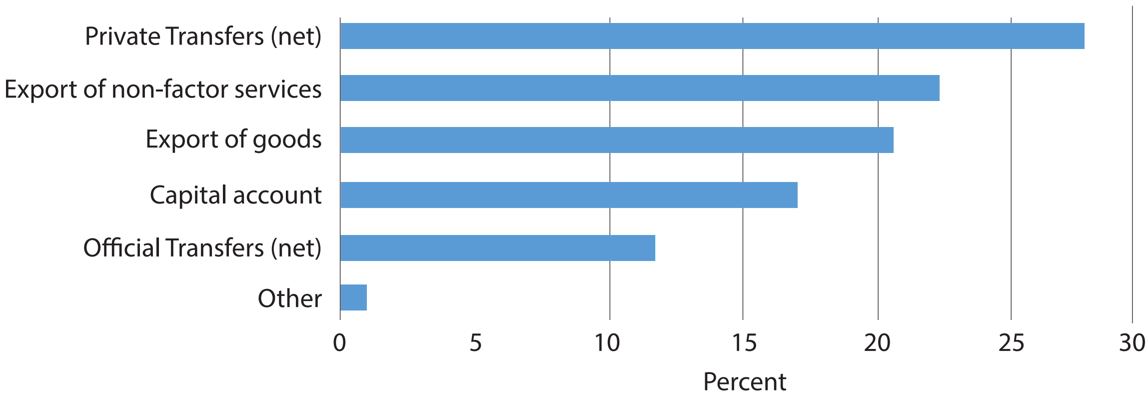


Source: National Bank of Ethiopia, 2014

2.3 Developments in External Sector

The performance of the external sector remain dampened with export sector being less than competitive. Foreign exchange earnings amounted to 10.8 billion US$ in the first 9 months of 2013/14 (July 2013 to March 2014). The main source of foreign exchange was private transfers (27 percent) followed by earnings from export of non-factor services (22.3 percent), export of goods (20.5 percent), capital account that includes long-term loans and FDI (16.9 percent) and official transfers (11.7 percent). In the same period, the payments for imports of goods and imports of non-factor services were 11.8 billion US$, 85 percent for import of goods and the rest for import of non-factor services. Meanwhile, the gross foreign reserve of the country, measured by months of imports remained at 1.9 months of imports far below the target of 3 months of imports by the central bank.

Figure 8: Foreign exchange earnings in the first nine months of 2013/14 by component in %

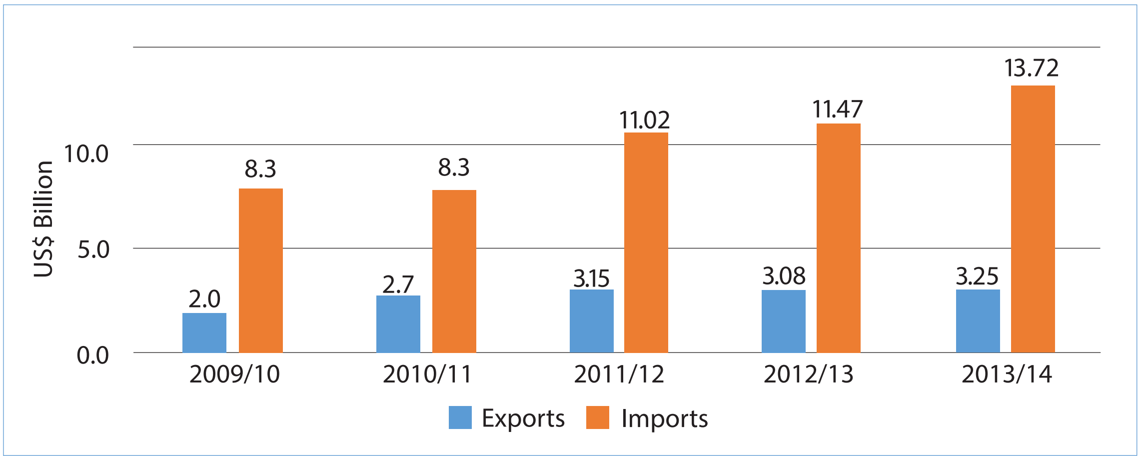


Source: National Bank of Ethiopia

By end of 2013/14 EFY, exports seem to have slightly recovered from the last year's dip to reach USD 3.25 billion. This is a 5.6 percent increase compared to 2011/12 which recorded US$ 3.15 and 3.2 percent increase compared to 2012/13 which recorded US$ 3.08 billion (see figure: 9). The increase in this year's export is mainly a result of increased export of oilseeds by 208 million US$ due to rising export volume.

On the other hand, the other major exports like coffee and gold suffered a decline of 4.3 and 21.2 percent, respectively. This trend is worrying because the decline in the case of coffee is attributed to a fall in coffee export volume , while the decline in export earning of gold is a result of 16.6 percent reduction in price and 5.4 percent contraction in the volume of gold export.

Figure 9: The Trend in export and import in US$ billion

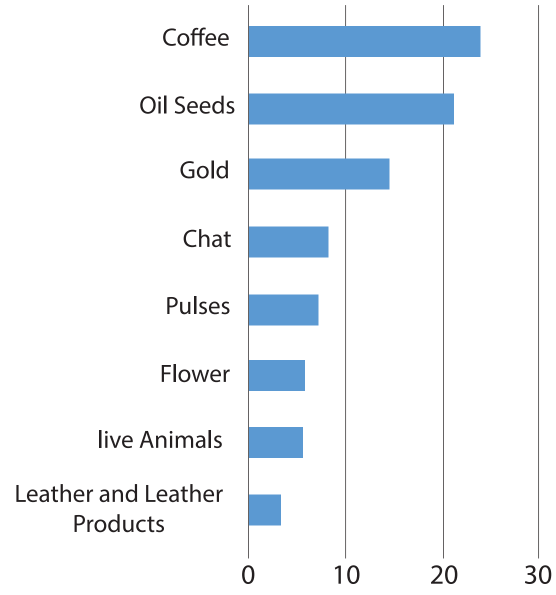


Source: National Bank of Ethiopia, 2014

The six major export items are coffee, oilseeds, gold, chat, pulses, and flower jointly accounting for 79 percent of the revenue. Ethiopia's export continued to be primary agricultural commodities dominated indicating diversification is still low and the earnings from the sector has not been growing as planned and even showed slight declines. The share of the only major manufactured item, leather and leather products remained 4 percent between 2012/13 and 2013/14. However, looking at a longer time span its export contribution has increased from 57.5 million US$ in 2009/10 to 129.8 million US$ in 2013/14.

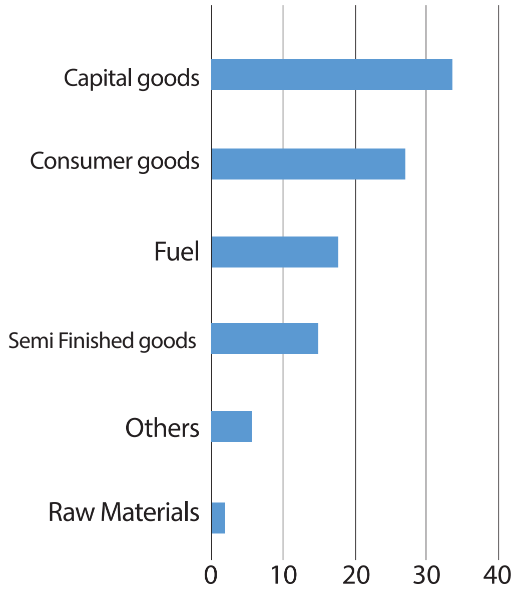
Imports of goods increased by 19.7 percent in 2013/14 to reach 13.7 billion US$ compared to the preceding year. The major imports are capital goods (32 percent) mainly industrial goods (23.7 percent); consumer goods 27.9 percent (of which 17 percent is non-durables); fuel (18.5 percent) and semi-finished goods 15.3 percent. There have not been much change in the structure of international trade; Ethiopia's exports are primary agricultural commodities dominated while in the case of imports both capital and nondurable goods dominated. The value of imports increased by 19.7 percent while exports increased by only 5.6 percent. This explains the widening deficit in merchandise trade by 24 percent to reach 10.4 billion US$ in 2013/14 against 8.4 billion US$ in 2012/13.

Figure 10: Share of Major Exports in 2013 / 14 (in %)



Source: National Bank of Ethiopia

Figure 11: Share of Major imports in 2013 / 14 (in %)

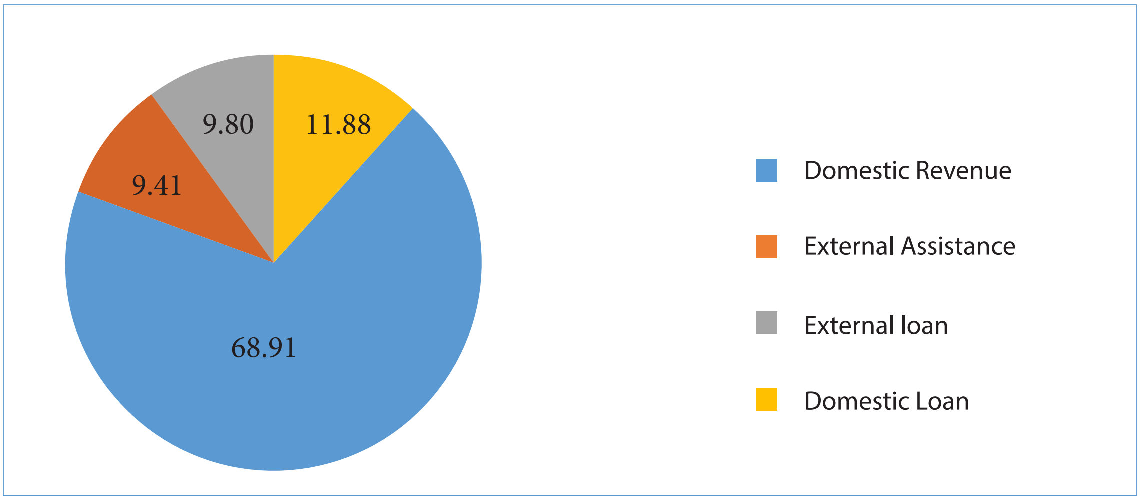


Source: National Bank of Ethiopia

2.4 Federal Government Finance

In July, Parliament approved a budget of 178.6 billion birr for federal government for the 2014/15 fiscal year, translating to a 14 percent increase compared to the 154.9 billion birr budget in 2013/14. The budget constitutes 46 percent in capital expenditure, (of which 35 percent is earmarked for road sector development, and 17 percent towards the education sector) with the rest going to recurrent budget (including subsidies to the regional states). Approximately 68.9 percent of budget will be financed from tax and non-tax domestic revenue, 11.89 percent from domestic loans, 9.8 percent from external loan and 9.4 percent from external assistance.

Figure 12: Ethiopia Federal Government budget for 2014/15 by components in %



Source: MoFED,2014

3. Human Development

The last decade of robust economic growth has led to a drop in poverty levels (currently at 29 percent) and attained significant human development gains since 2000. Ethiopia is one of the 14 countries that have recorded Human Development Index (HDI) gains of more than 2 percent annually. The country was ranked 173 out of 187 countries putting the country at the lower tier in the human development category. However, it is important to note that between 2000 and 2013, Ethiopia's HDI value had increased from 0.284 to 0.435, which is an increase of 53.2 percent. In the period between 1980 and 2013, Ethiopia's life expectancy at birth increased by 19.8 years, mean years of schooling increased by 0.9 years and expected years of schooling increased by 5.3 years. Ethiopia has also managed to reduce gender inequality, which is reflected in 27.8 percent of parliamentary seats being held by women. Ethiopia has managed to reduce its Gender Inequality Index (GII) to 0.547, ranking 120 out of 149 countries in the report. Overally, the country is also on track to meet most of the MDGs except for MDG 3 on promoting gender equality & empower women and MDG 5 on improving maternal health that are still lagging behind. The table below summarizes some of current MDG values in Ethiopia based on 2014 mini-DHS:

	Millennium Development Goal Indicators, Ethiopia 2014	Female	Value	Male	Total
Goal	Indicator				
1.	Eradicate extreme poverty and hunger				
	1.8 Prevalence of underweight children under five years of age	25.4%		25.3%	25.3%
2.	Achieve universal primary education				
	2.1 Net attendance ratio in primary education	63.0%		66.5%	64.8%
	2.3 Literacy rate of 15-24 year olds	63.5%		na	na
3.	Promote gender equality and empower women				
	3.1a Ratio of girls to boys in primary education[4]				1.1
	3.1b Ratio of girls to boys in secondary education				2.3
	3.1c Ratio of girls to boys in tertiary education[4]				1.6
5.	Improve maternal health				
	5.2 Proportion of births attended by skilled health personnel	14.5%		na	na
	5.3 Contraceptive prevalence rate 5.4 Adolescent birth rate[7]	41.8% 65 per 1,000		na	na na
	5.5 a) Antenatal care coverage: at least one ANC visit	57.2%		na	na
	b) Antenatal care coverage: at least four ANC visits	31.6%		na	na
		Urban		Rural	Total

7.	Ensure environmental sustainability				
	7.8 Proportion of population using an improved drinking water source	93.2%		43.8%	50.3%
	7.9 Proportion of population using an improved sanitation facility[9]	17.5%		2.5%	4.5%

Source: 2014 Mini-DHS, CSO and World Bank

"Government of Ethiopia has shown its commitment to achieve the MDGs by allocating about 8 percent of the national budget since 2011/12, specifically to MDGs." The budget for 2014/15 EFY has allocated Birr 15 billion to cater for the achievement of the MDGs. The budget proclamation has specifically stated that that capital expenditure support will be provided for regional states to finance only capital projects that help achieve the MDGs. However it is not clearly indicated in the budget which specific MDGs will be covered.