QUARTERLY MACROECONOMIC UPDATES ON THE ETHIOPIAN ECONOMY

Volume 9 Number 02

August 2024

Acknowledgments

This Quarterly Macroeconomic Update is written by Dr. Tasew Tadesse, Leader of the Macroeconomy Research Theme of the Ethiopian Economics Association. The Association appreciates his contribution. The Association is also grateful to those who have reviewed and provided feedback on the draft version of the report, including EEA's management members, senior researchers, and executive committee members. The EEA is specifically thankful to Dr. Lemma Gudissa, Dr. Worku Gebeyehu, Prof. Mengistu Ketema, and Dr. Degye Goshu for their support in reviewing and improving the content of the report. Furthermore, EEA appreciates Mrs. Rahel Yilma for formatting and designing the report.

Table of Contents

List of Tables

List of Figures

1. Introduction

This quarterly macroeconomic report provides an update on the macroeconomic situation in Ethiopia, focusing on two key macroeconomic developments with significant implications for the country's economy: international trade and banking and monetary developments. Some of the key macroeconomic issues affecting the economic stability of the country are considerable growth of money supply, heavy government borrowing from the National Bank of Ethiopia (NBE), and high concentration of the banking sector's credit amidst limited credit expansion. Moreover, Ethiopia's heavy reliance on primary exports exposes the country to volatility of recurrent prices and foreign earnings along with the small size of exports contributing to the ongoing and widening trade deficit. Such persistent deficits and their financing have forced the country to depend heavily on external debt, increasing the debt vulnerability and susceptibility of the country to external shocks.

The report investigates the banking and monetary developments, including the growth of monetary aggregates, deposit mobilization, and loan disbursement performance of the banking sector, and analyses recent trends in export, import, and trade balance performance. This update covers the second quarter of the Ethiopian fiscal year (EFY 2016) that spans from 1st October to 31 December 2023. The discussion of the key developments on the selected indicators is provided in the following two sections of the updates.

2. Banking and Monetary Developments

This section analyzes the performance of the banking and monetary sector in the first six months of the Ethiopian fiscal year 2016, covering June 30th, 2023, to December 31st, 2023. It focuses on monetary aggregates, deposit mobilization, and loan disbursements by the banking sector.

Key facts and figures

- *As of 31 December 2023, the broad money supply has reached ETB 2.3 trillion, reflecting an 18.7% increase from the same period in 2022.*
- *Narrow, money supply rose by 15.9%, reaching a record high of ETB 747.9 billion on December 31, 2023.*
- *Direct advances continued to play a crucial role in deficit financing. Borrowing from the NBE increased by approximately 28.5%, amounting to ETB 37 billion, compared to the level reported on June 30, 2023.*
- *As of December 31, 2023, the total deposits collected by the banking sector amounted to ETB 2.29 trillion.*
- *At 48.7%, the Commercial Bank of Ethiopia (CBE) holds the largest share of deposits, followed by Awash Bank (8.4%) and Bank of Abyssinia (7.3%).*
- *Bank deposits are growing despite the negative real interest rates (a 7% nominal deposit rate in comparison to a staggering 28.7% inflation rate), possibly due to the lack of alternative financial instruments with higher returns and increased investment risks.*
- *Total loan disbursement for the quarter ending on 31 December 2023 was ETB 218.6 billion, which is ETB 92.4 billion lower than the 31 December 2022 disbursement of ETB 311.1 billion, representing a reduction of 29.7%.*
- *In the first half of 2023, ending on December 31st, the private sector received 76.2% of the total loan disbursements.*
- *Loan disbursement to public enterprises on 31 December 2023 has increased to ETB 50.86 billion compared to ETB 29.29 billion on 31 December 2022, unlike the private sector.*
- *Commercial Bank of Ethiopia (CBE) disbursed the largest share of loans in the country at 42%, followed by Awash Bank at 11.3% and Dashen Bank at 9.2%.*
- *The country's top three banks accounted for approximately 63% of the total loan disbursements.*
- *Credit extended by the banking sector reduced significantly between 30 June 2023, and 31 December 2023, following the NBE's credit expansion limit introduced in August 2023.*
- *Credit provision by the public banks (CBE and Development Bank of Ethiopia (DBE)) increased by ETB 39.4 billion in 2023 compared to the same period in 2022, indicating a 60% annual growth.*
- *Loan disbursements by private banks have decreased by a staggering ETB 1.8 billion on 31 December 2023 compared to 2022, indicating a 53.7% decline.*
- *The top three sectors with the highest credit in the review quarter were manufacturing, domestic trade and services, and export.*

2.1 Monetary Policy

The National Bank of Ethiopia (NBE) manages the country's monetary policy to achieve several objectives. The Bank prioritizes price stability, financial stability, and sustainable economic growth in its monetary policy framework (NBE, 2023). However, despite these goals, Ethiopia has grappled with persistently high and rising inflation over the last decade. Since 2017, the NBE has maintained a steady savings/deposit rate of 7% (NBE, 2024), while it averaged at about 5.38 before 2016/17 (NBE, 2016/17, Mengistu, 2021). This policy suggests a lesser emphasis on using interest rates as a primary tool for monetary control. Instead, according to Deloitte (2023), the NBE appears to prioritize managing inflation and exchange rates through managing monetary aggregates.

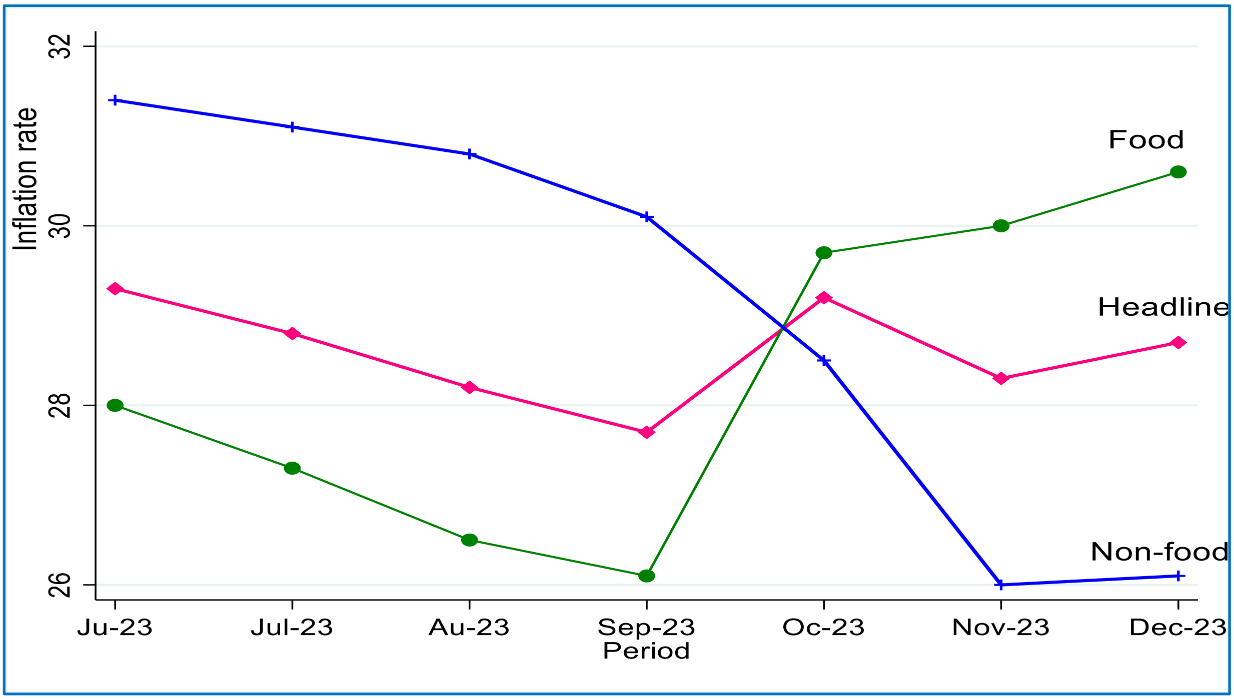
In its August 2023 monetary policy statement, the National Bank took a significant step towards curbing inflation. Concerned about rising inflation, the NBE (2023) has recently adopted a more accommodative monetary policy stance, shifting away from its previous expansionary approach. This involves raising interest rates and tightening liquidity to dampen inflationary pressures. It announced a cap on commercial banks' credit growth at 14%, aiming to restrict the money supply and dampen inflationary pressures. This approach contrasts with the NBE's previous reliance on managing monetary aggregates. Furthermore, commercial banks have raised their average lending rates from 14.3% in 2022 to 14.8% in 2023. This increase likely reflects rising operational costs and the need to account for higher risk premiums in a volatile economic environment.

The other two key changes implemented by the National Bank of Ethiopia (NBE) likely aimed at controlling inflation are reduced government borrowing and increased borrowing costs for the banking sector. The NBE plans to significantly restrict direct loans (direct advances) to the government in 2023/24. These loans are expected to be limited to just one-third of the amount provided in the previous year. To safeguard responsible use, the NBE planned to seek an agreement with the Ministry of Finance (MoF) restricting the emergency lending facility to last resort. This approach reflects the NBE's commitment to support the government's fiscal discipline, which is vital for controlling inflation, especially when government spending can be a contributing factor. Moreover, the NBE outlined to raise the interest rate on its Emergency Lending Facility from 16% to 18%. This facility provides short-term loans to banks facing liquidity issues. By increasing the interest rate, the NBE discourages banks from relying heavily on this emergency source of funds. This can help control the overall money supply and inflationary pressures.

Following the introduction of the new policy measure, headline inflation has been slightly reduced from 29.3% in June 2023 to 28.7% in December 2023, a drop of only 0.6 percentage points. Non-food inflation showed a considerable annual reduction in December 2023 from its value in June 2023. On the other hand, food inflation increased to 30.6% as of December 2023, from 28% in June 2023, suggesting that there has been a considerable increment in food prices during the review quarter. The recent decline in headline inflation, albeit modest, was largely driven by a significant slowdown in non-food prices. While food inflation remains a concern, non-food inflation dropped by 5.3% in December 2023 compared to June 2023, falling from 31.4% to a more moderate level (Figure 1). This decrease in non-food inflation may be associated with the

NBE's credit restriction and the resulting liquidity problem in the banking system, leading to a slowdown in major non-food commodities and utilities. Looking at the overall inflation rate and given the interplay of other factors, the newly introduced policy has not eased the inflationary pressure particularly for food items in the country until the reviewed quarter.

Figure 1: The trend of inflation after the recent policy measure (June 30-December 2023)



Source: Computed from data in the NBE and Ethiopian Statistical Services (2024)

According to the Ethiopian Statistical Services (ESS) data, there was a slowdown in monthly inflation in Ethiopia. Monthly, headline inflation has dropped from 3.3% in June 2023 to 0.7% in December 2023. At 3.5%, the largest decrease in inflation was observed for food items. Food inflation in December was zero while it was 1.8% for non-food items (Table 1).

Table 1: Monthly inflation rates in July, and December 2023

Month	Food	Non-Food	Headline
Jul-2023	3.5	3.1	3.3
Dec-2023	0.0	1.8	0.7

Source: Computed from data in the NBE and ESS (2024)

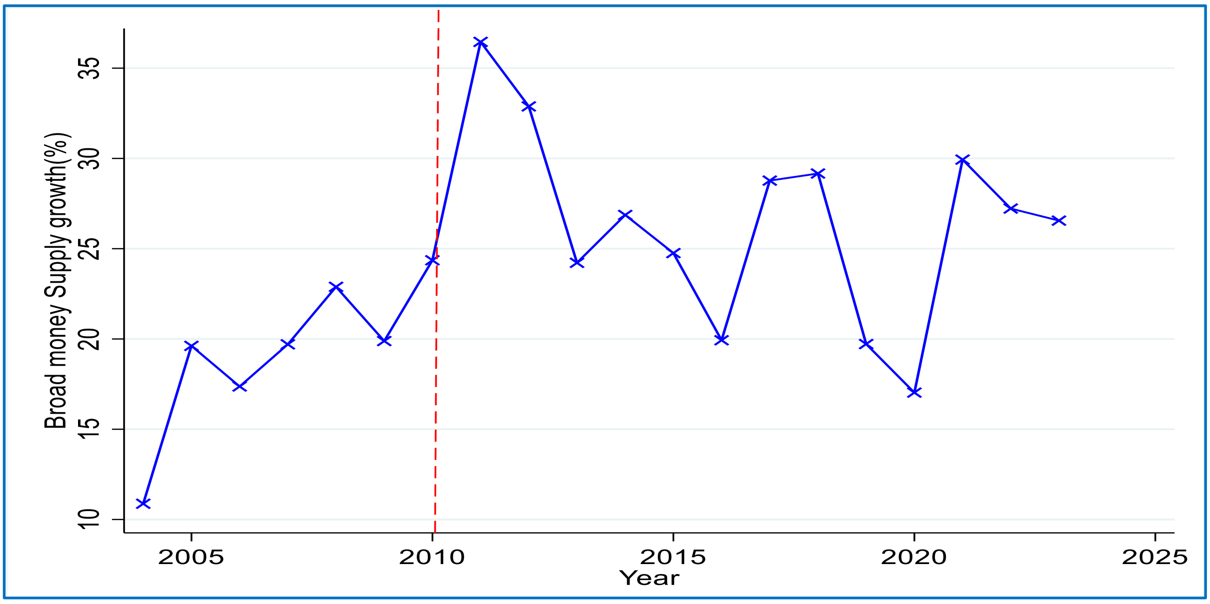
Recognizing the limitations of its prior strategy, the NBE has also signaled a potential shift towards an interest rate-based monetary policy framework. This approach could offer more precise control over inflation, allowing the NBE to adjust interest rates to influence borrowing and spending habits.

According to the Ethiopia Economics Association (EEA) report, the macroeconomic imbalances and prices are expected to fall. Compared to 2015, when inflation was more pronounced in Ethiopia, there has been a substantial fall in real GDP and per capita income of citizens, signifying the erosion of purchasing power that has led to a general decline in aggregate demand and price fall (EEA, 2024). This is the reverse of the inflationary trend partly caused by the growth of purchasing power experienced before 2015. Without addressing the structural problems on the supply side, policy measures to suppress aggregate demand led to more macroeconomic imbalances and the widening gap between aggregate supply and demand.

2.2 Money Supply and Monetary Aggregates

The trend of broad money supply has fluctuated over the last two decades. According to the African Economic Outlook (AEO) data of the African Development Bank (AfDB) in 2024, the growth of the broad money supply surged to a peak of 365% in 2011. In relative terms, the average growth rate between 2004 and 2009 was low at 18.4%. This rate climbed considerably to 26.3% on average between 2010 and 2023. The evidence suggests a clear turning point of broad money supply growth in 2010 (Figure 2).

Figure 2: Growth of narrow money and broad money supply (2004-2023)



Source: Computed from data in the African Development Bank (2024)

According to the NBE, the broad money supply has reached a substantial ETB 2.3 trillion as of 31 December 2023. This significant increase, reflecting an 18.7% expansion from the same period of 2022, is attributable to the growth of narrow money (M1) and quasi-money. Narrow money supply has increased by 15.9%, reaching an all-time high of ETB 747.9 billion on 31 December 2023 (Table 2). This signals an improvement in transaction-related demand for money in Ethiopia. A substantial rise of 20% was observed in quasi-money, which includes savings and time deposits. The growth of quasi-money is due to the expansion of time deposits (31.7%) and saving deposits (18.8%). This growth can likely be attributed to enhanced deposit mobilization efforts by financial institutions.

Table 2: Components of broad money supply (billion birr)

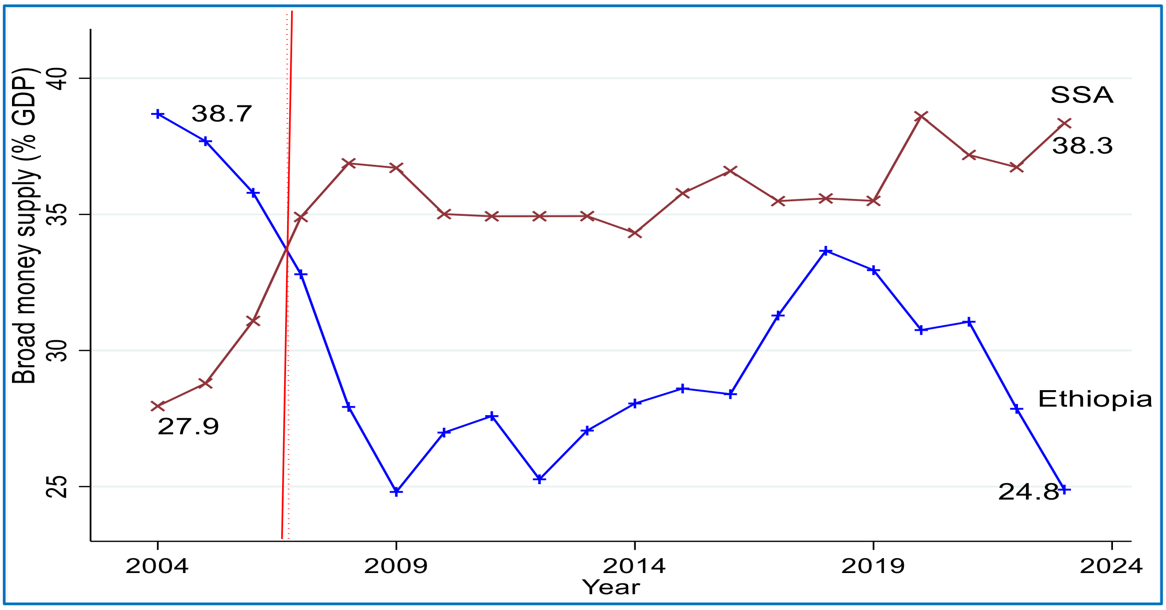
Year	Broad money (M2)	Narrow Money (M1)	Currency outside banks	Demand deposits	Quasi-money	Savings deposits	Time deposits
30-Jun-22	1,715	588.01	173.38	414.6	1,127	1,016	111.2
31-Dec-22	1,946.7	645.3	201.1	444.2	1,301	1,175	125.7
30-Jun-23	2,170	706.1	211.6	494.5	1,464	1,315	149.4
31-Dec-23	2,310	747.9	212.7	535.2	1,562.6	1,397	165.6

Source: Computed from data in the NBE (2024)

Money supply defined narrowly witnessed notable growth from ETB 747.9 billion in the review quarter to ETB 645.3 billion, showing about a 16% growth rate relative to the same quarter of 2022. The holdings of currency by the public and demand deposits have risen by 5.7% and 20.5%, respectively, contributing to the expansion of narrow money supply, a key measure of liquid money readily available for spending. Furthermore, quasi-money, which reflects less liquid instruments like time deposits and savings deposits, also saw a significant rise of 20% from ETB 1.3 trillion in 2022 to ETB 1.56 trillion in 2023. Time and savings deposits grew by an impressive 31.7% and 18.8%, respectively. This increase suggests the growing performance of deposits and preference for saving instruments in Ethiopia.

Broad money supply continued to grow during the last two decades. Notwithstanding the growth of the money supply, it has been characterized by some fluctuations over time. In particular, the broad money supply has fluctuated over the years in Ethiopia. The sub-Saharan Africa's (SSA) average broad money supply as a share of GDP (36%) was higher than Ethiopia's (28.8%) since 2007. Ethiopia's broad money supply started at 38.7% in 2004 and decreased steadily to 24.8% in 2023 (Figure 3).

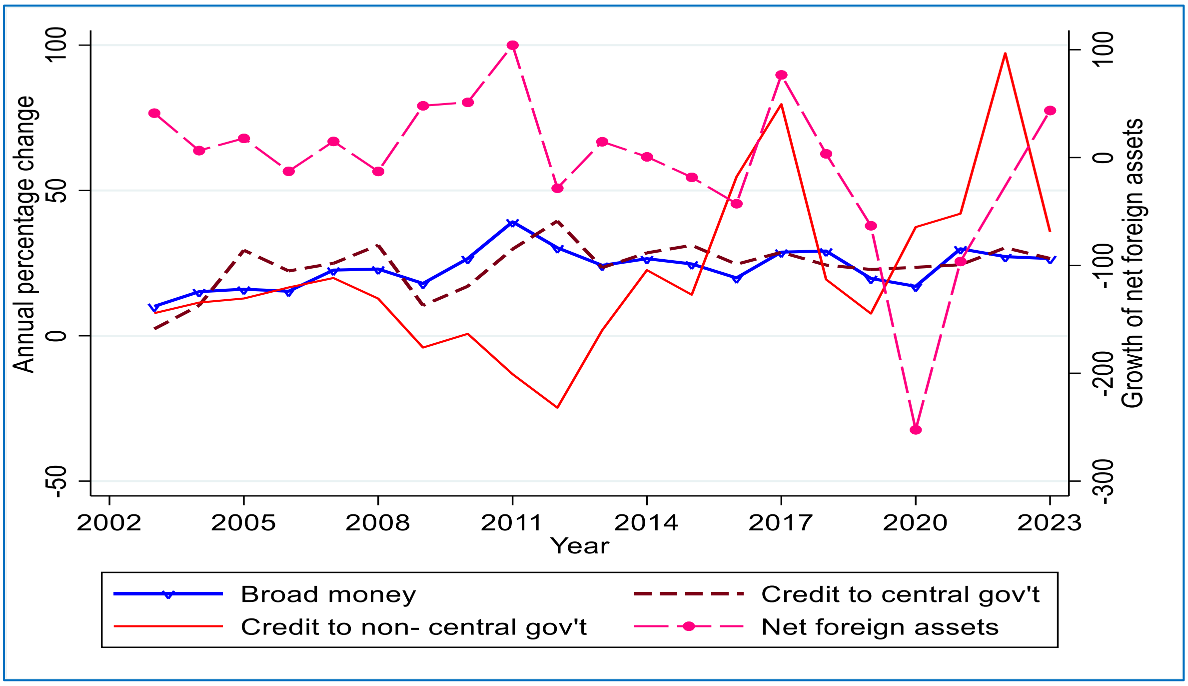
Figure 3: Broad money supply (% GDP) in Ethiopia relative to SSA (2004-2023)



Source: Computed from data in the African Development Bank (2024)

NBE's monetary policy continued to be accommodative in the review quarter. Broad money supply has reached ETB 2.3 trillion at the end of December 2023, reflecting an 18.7% annual and 6.1% growth in the first six months of 2023 (30 June to 30 December 2023). This growth was attributed to a 20.1% surge in domestic credit. The higher growth in domestic credit was in turn linked to a 32.5% increase in credit to the central government and 16% to the non-central government, respectively. Figure 3 demonstrates that the expansion in domestic credit is also accompanied by growth in net foreign assets of the NBE. Net foreign assets of the banking system grew by an impressive 70.2% annually at the end of December 2023 and by 48.9% in the first six months of 2023 (Figure 4).

Figure 4: Trends of broad money supply and its determinants (2002-2023)



Source: Computed from data in the NBE (2024)

Regarding the decomposition of domestic credit, over three-fourths of the credit (75.8%) is directed to the private sector (i.e., claims on other sectors) and about one-fourth (24.2%) to the central government (including bank advances). Government borrowing has contributed modestly to the money supply growth. Credit to the central government grew by about 9.5%, reaching ETB 628 billion on 31 December 2023, from ETB 537.6 billion on 30 June 2023. Government borrowing such as bank advances and treasury bills is used to monetize and finance the deficit of the central government, which according to the United Nations Development Program (UNDP) (2023), stood at 1.8% of GDP in 2023. However, this is against the policy measure introduced by the NBE in August 2023, which claimed to limit direct advances to one-third of the previous year. The total outstanding direct advances as of 30 June 2023 was ETB 130 billion. Nevertheless, departing from its policy, bank advances have significantly increased.

Evidence suggests that the total outstanding Direct Advance (borrowing from the NBE) increased to 167 billion as of 30 December 2023, from ETB 130 billion on 30 June 2023, and ETB 147 billion as of 30 September 2023 (Ministry of Finance, 2024). That is, from July to December 2023, the government borrowed ETB 37 billion in direct advances from the NBE. In the first six months alone, the amount borrowed is a little lower than one-third of the value on June 30, 2023 (i.e., Ethiopian birr (ETB) 43.3 billion). The six-month development shows that the government's borrowing from the NBE has increased by over 28.5% (37 billion birr) compared to the level observed on 30 June 2023 and by 13.6% relative to the previous quarter. Such monetization of deficits possibly contributes to the inflationary pressure in the country (United Nations Development Program (UNDP), 2024). Had the new policy measure been effectively implemented, direct advances made by the NBE should have shown a reduction in the review quarter. This shows that direct advances from the NBE continued to play a key role in deficit financing (UNDP, 2024), which can potentially contribute to the inflationary pressure in the country. Given the daunting problem in deficit financing following the decline in external borrowing, this may signal that the NBE has faced difficulty in effectively implementing the policy and thereby effectively lowering the inflationary pressure.

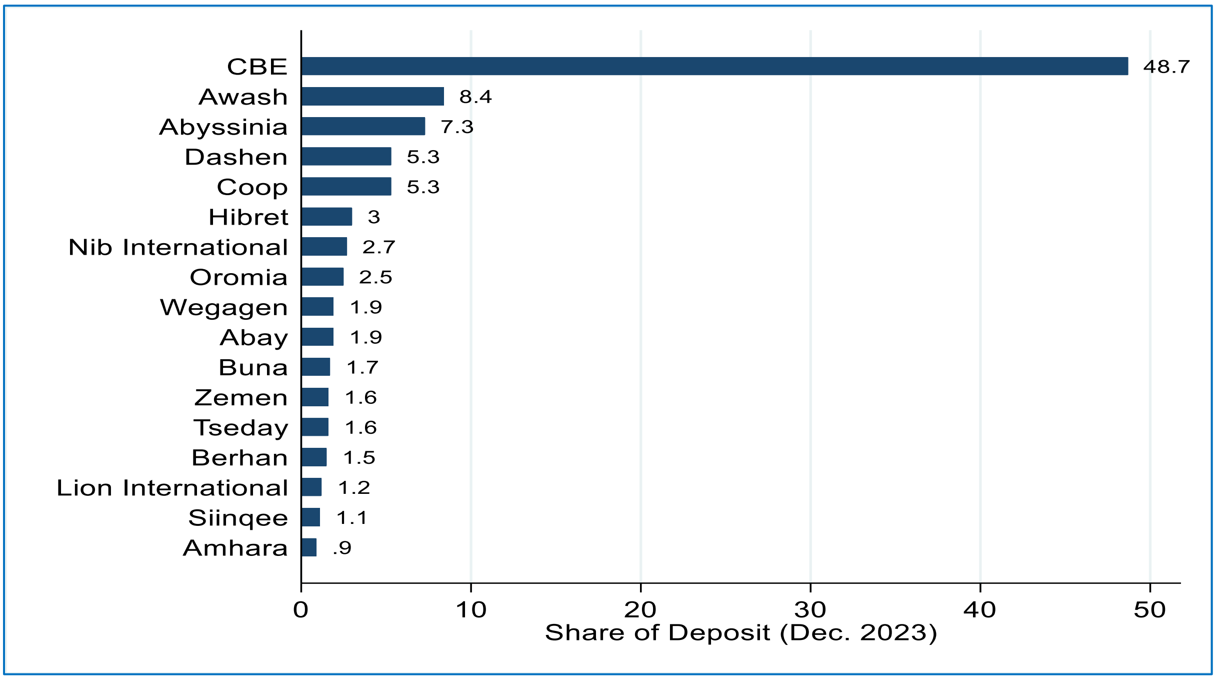
Besides direct advances, treasury bills as a short-term financing instrument have continued to play a role in deficit financing. NBE's data show that the total amount of treasury bills sold increased by 23% from ETB 277 billion in December 2022 to ETB 341.5 billion in December 2023. According to the UNDP (2023), dependence on treasury bills to finance deficits is crowing out long-term private sector development, including developing a bond market.

Overall, evidence shows that the monetary policy stance of the NBE has loosened in response to addressing recent multiple challenges/shocks such as COVID-19 and conflicts. According to the World Bank (2021), monetary policy, which had been tightening since 2018, started to loosen in February 2020, as the NBE injected funding into commercial banks, which have been experiencing liquidity challenges since November 2019, and expanded lending to the government as part of the response to the COVID-19 pandemic.

2.2 Deposit Mobilization

As of 31 December 2023, the total deposits mobilized by the banking sector reached ETB 2.29 trillion. At 48.7% (ETB 1.12 trillion), the Commercial Bank of Ethiopia (CBE) has the largest share of deposits, followed by Awash Bank (8.4%) and Bank of Abyssinia (7.3) (Figure 5). Nearly half of the banking sector's deposit is mobilized by the CBE. The high concentration of deposits in a single state-owned bank, the CBE, may limit competition in the sector.

Figure 5: Ranking of banks in deposit mobilization (percentage of total deposit mobilized)



Source: Computed from data in the NBE (2024)

Table 3 shows the performance of commercial banks in Ethiopia in mobilizing deposits over two years. During the last six months ending 31 December 2023, there was a total increase of ETB 133.8 billion in deposits mobilized by the banking sector, indicating a growth of 6.2% compared to 30 June 2023. Between 30 June and 31 December 2023, the CBE had the largest increase in the value of deposits (ETB 66.6 billion) growing by 6.3%, followed by the Bank of Abyssinia (ETB 17.7 billion) with a growth rate of 11.2% and Awash Bank (ETB 13.4 billion), showing a growth of 7.4%.

Table 3: Deposit mobilization by the banking sector (ETB in billions) (2022-2023, and (June 30-Dec. 31, 2023)

Particular	December 2022/2	June 2022/23	December 2023/24	First Six Months Change 2023/24		Annual Change 2023/24	
				Absolute	Percentage	Absolute	Percentage
	A	B	C	D=C-B	E=D/B*100	F=E-A	G=F/A*100
Commercial Bank of Ethiopia	980	1,054	1,121.8	66.6	6.3	141.1	14.4
Awash Bank	167.8	181.9	195.4	13.4	7.4	27.6	16.5
Dashen Bank	101.4	114.5	123.5	9.02	7.9	22	21.8
Bank of Abyssinia	146.17	158.2	176	17.7	11.2	29.86	20.4
Total	1,969.8	2,165.5	2,299.3	133.7	6.2	329.4	16.7

Source: Compiled from data in the NBE (2024)

On the other hand, about eight banks showed a decrease in deposits mobilized in the first six months from 30 June to 31 December 2023. The list includes banks that have operated in the industry for several years (Nib International Bank, Cooperative Bank of Oromia, Berhan Bank, Addis International Bank) and some new entrants including Tseday Bank, Hijira Bank, and Omo Bank (see annex).

Overall, total deposits in the Ethiopian banking sector increased by 16.7% between December 2022 and December 2023. This represents an increase of ETB 329.4 billion**.** Twenty-three banks out of the 31[1] saw an increase in deposits over this period. Relative to 2022, the top three banks in terms of the incremental value of deposit mobilization in 2023 were the CBE (ETB 141 billion), Bank of Abyssinia (ETB 29.8 billion), and Awash Bank (ETB 27.6 billion). While the CBE showed the highest absolute increase in terms of growth rates, the new entrants to the banking industry hold the top spot in 2023. Amhara Bank's deposits registered the highest growth (4,567.8%) from December 2022, followed by Sinqee Bank (3,976.5%), and Tsehay Bank (482.5%) (See annex). The exceptionally high growth rates reported by Amhara Bank, Sinqee Bank, and Tsehay Bank can be largely attributed to their relatively small initial deposit bases (See annex). When starting with a very small size of deposits, even a modest increase in the volume of deposits can lead to a dramatically high percentage growth rate. Apart from this, these banks have been implementing aggressive marketing campaigns and promotional offers to attract new customers and stimulate deposits. It might also be linked to the increase in the number of branches operated by these new banks. The branch networks of Sinqee Bank and Amhara Bank have both surpassed 300, with Sinqee Bank's network exceeding 466 branches[2].

Despite the higher inflation rate relative to the nominal deposit rate (negative real interest rates) in Ethiopia, bank deposits are growing, partly because of the lack of alternative financial instruments with high returns and investment risks. The minimum statutory deposit rate is 7%, while the average lending rate is 16%, which is outpaced by inflation (UNDP, 2023). On the other hand, the only exceptions to the growth in the banking sector's deposit mobilization were Ahadu Bank and Nib International Bank, which saw a decrease of 87.7% (ETB 23.7 billion) and 5.6% (ETB 3.1 billion), respectively (See annex).

2.3 Loan Disbursements

Looking at the sectoral distribution, in the last two years, Table 4 shows that the private sector has consistently been the largest recipient of loan disbursements, followed by public enterprises and cooperatives. In the first six months of 2023 ending 31 December, the private sector received over 76.2% of the total loan disbursements, a decline from 84% in the same period of 2022. The disbursements show a mixed trend across different client types over time.

[1] Six newly established banks are excluded from the total number of banks while computing the change over the past two years.
[2] Total number of Siinqee bank branches is available at: https://drive.google.com/file/d/1i5j5onC0HYjcL751CFrECcuyIz1fYj_s/view

Table 4: Loan Disbursement by Clients (in billions of birr)

Client type	June 30-December 31, 2021*	June 30-December 31, 2022*	2022/23	June 30-December 31, 2023*	Annual change in 2022/23 (%)	Annual change in 2023/24 (%)
Total disbursements	146.8	311.1	547.6	218.6	111.9	-29.7
Public enterprises	50.2	29.2	75.8	50.8	-41.7	73.6
Cooperatives	13.08	6.07	9.75	1.1	-53.5	-81.8
Private sector	83.5	275.7	462.1	166.7	230	-39.5

Source: Computed from data in the NBE (2024)

*Note that the first six months of 2023/24 refers to 30 June to 31 December 2023, while the first six months of 2022/23 refers to 30 June to 31 December 2022.

Table 4 shows that total loan disbursements declined by 29.7% on 31 December 2023, compared to 2022. Total loan disbursement for the review quarter ending 31 December 2023 (ETB 218.7 billion) is lower than the 2022 (ETB 311.1 billion) by ETB 92.4 billion, which is a decrease of 29.7%. Loan disbursement to public enterprises on 31 December 2023 (ETB 50.9 billion) is higher than the disbursement as of 31 December 2022 (ETB 29.3 billion). This shows a growth of 73.7% (or an increment of ETB 21.6 billion) compared to the same period in 2022/23.

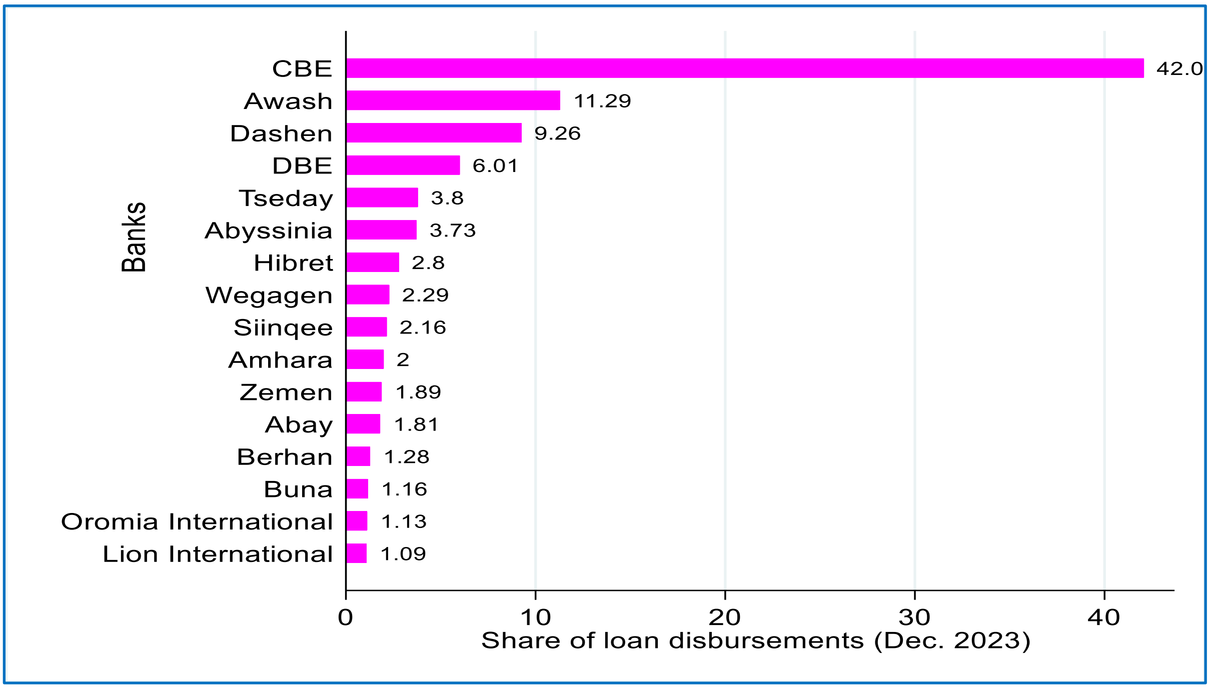
At 111.9%, total loan disbursements have seen the largest increase in 2022/23. This increment has been due to the astounding growth in loans to the private sector. Disbursements to the private sector have shown a significant increase over the years. There was a 230% increase in disbursements from the first five months of 2021/22 to the first six months of 2022/23 (i.e., 30 June to 31 December 2022). However, disbursements to the sector have declined by 39.5% in the first six months of 2023/24 (i.e., 30 June to 31 December 2023) compared to the same period of the previous year, 2022/23.

The loan disbursements to public enterprises also fluctuated over the years. There was a 41.7% drop in the first six months of 2022/23 compared to the first five months of 2021/22. However, disbursements have increased by 73.6% from the first six months of 2022/23 to the first six months of 2023/24. This growth is remarkable amidst the credit limit introduced in 2023 by the NBE. In the first six months of 2023/24, there was an 81.8% drop in disbursements to cooperatives compared to the same period of the previous year, 2022/23.

Except for public enterprises, there has been a drop in aggregate loan disbursements to various sectors in 2023/24. The decline in loans in the first six months of 2023/24 is likely associated with the credit limit introduced by the NBE in August 2023. In summary, disbursements to the private sector have shown a significant and consistent increase, while disbursements to cooperatives have fluctuated or decreased over the years.

Loan disbursements by the banking sector totaled ETB 218.7 billion for the first six months of 2023/24. Of this, loan disbursement by the CBE in the first six months of 2023/24 stood at Birr 92 billion. CBE accounted for the lion's share of loan disbursements in the country (42%), followed by Awash Bank (11.3%) and Dashen Bank (9.2%). The top three banks accounted for about 63% of the total loan disbursements in the country (Figure 6).

Figure 6: Loan Disbursement by Source (percentage of total disbursement) (30 June to December 2023)



Source: Computed from data in the NBE data (2024)

Following the NBE 's credit expansion limit introduced in August 2023, credit extended by the banking sector reduced significantly between 30 June 2023, and 31 December 2023. However, notwithstanding the policy measure taken by the NBE aiming to curb inflation, credit provision by the public banks (CBE and Development Bank of Ethiopia (DBE)) increased by ETB 39.4 billion in 2023 relative to the same period of 2022, suggesting an annual growth of 60%. During the period, CBE's loan increased by ETB 33.18 billion from the first six months of 2022 (June-December 2022) and reached ETB 92 billion on 31 December 2023. It registered a significant annual growth rate of 56.4%, the second-highest growth for the period following the DBE (90.9%) (Table 5). This may indicate that the NBE's policy measure has not significantly affected their ability to extend credit or has not been effectively implemented in public banks.

Table 5: Growth of loan disbursements by banks billion ETB

Banking sector	Value in 2022 (Dec. 31, 2022)	Growth in 2022	Value in 2023	Growth in 2023 (Dec. 31, 2023)
Public banks	(15.6)	(19.2)	39.4	60.0
CBE	(20.08)	(25.4)	33.18	56.4
DBE	4.46	184.5	6.26	90.9
Private banks	179.8	274.7	(131.8)	(53.7)

Source: Computed from data in the NBE (2024)

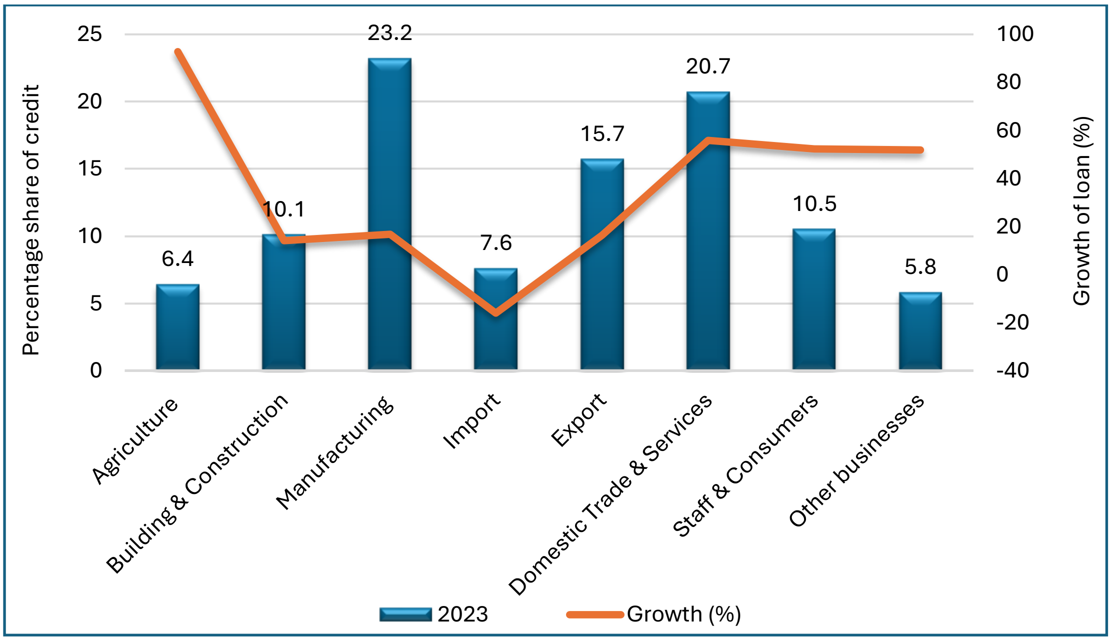
On the other hand, loan disbursements by private banks have significantly reduced by a staggering ETB 131.8 billion in 2023 relative to the same period of 2022, suggesting a decrease of 53.7% on 31 December 2023. Small-sized banks and some new entrants to the industry suffered/hurt the most probably due to the credit expansion limit introduced by the NBE. While most banks have experienced a considerable decline in credit provision, a handful of banks have registered a growth in loan disbursements. Apart from Lion International Bank (56.5%), most of the banks that exhibited expansion in loan provision were banks that joined the industry very recently: Sinqee Bank (71.8%), Shebele Bank (48.8%), and Tseday Bank (3.2%). Due to the drop in credit extended primarily by the private banks, loan disbursements have dropped nationally by 29.7% in December 2023 relative to the same period of 2022.

2.4.1 Loan Distribution and Growth by Economic Sectors

According to the NBE's 2024 Financial Stability Report, the banking sector's loans and advances are concentrated in the hands of a few large borrowers. The top ten borrowers from the banking industry held 23.5% of total loans and advances of the banking industry at the end of June 2023, a significantly higher share than a year earlier (18.7%). However, the Report skipped reporting the details of the borrowers.

In 2023, manufacturing, domestic trade and services, and exports were the top three sectors that received the highest loans. Manufacturing still accounted for the largest share of loans and advances (23.2%) from Ethiopian banks by the end of June 2023. The importance of domestic trade and services increased, growing by 3.8% to 20.7% (Figure 7). The increment in loans to domestic trade and services suggests that banks prefer domestic trade and services mainly because the private sector faces strong constraints in the external sector due to shortages and limited access to foreign exchange.

Figure 7: Loan Distribution and the Growth of Loans by Sector in 2023



Source: Computed from data in the NBE (2024)

The total credit extended to various economic sectors in the country grew by 27.3% as of June 2023 relative to 2022. Despite being relatively smaller in magnitude, at 92.8%, the growth of loans to the agricultural sector has been substantial, followed by domestic trade and services. The data shows a 16% decrease in loans for import-related activities. The decline in loan disbursements to import business is likely attributable to the shortage of foreign exchange and the limited access to importers through official banking channels, discouraging importers from applying for loans. Despite its economic importance, agriculture received the least loan disbursement, indicating marginalized access to credit.

3. External Trade Developments

This section examines Ethiopia's external trade performance in the second quarter of the Ethiopian fiscal year 2016 (October 2023 to December 2023). It analyzes trends in exports and imports compared to previous quarters, assesses the country's relative trade position, benchmarks with global regional (SSA) average, and tracks changes in the trade balance over time.

Key facts and figures

- *Exports in the review quarter totaled only $770 million, a 7.5% decline from $833.1 million in the previous quarter.*
- *Coffee held the top position with a share of about 28.3% of the total exports during the reviewed quarter, followed by cut flowers (14.7%) and pulses (11.5%).*
- *During the review quarter, the export value of three key commodities experienced a slowdown: coffee by -38.5%, textile and textile products by -9.3%, and leather and leather products by -20.6%.*
- *The highest growth was observed for oil seeds by about 148.1%, the largest increase of any commodity. This is followed by live animals (31.8%), and meat and meat products (12.4%).*
- *Total merchandise import bills amounted to $4.8 billion on 31 December 2023, which saw a 17.8% growth compared to the previous quarter.*
- *Capital goods had the largest share of imports (31.1%), followed by consumer goods (28.7%) and industrial goods imports (23%).*
- *Quarterly, capital goods saw the most significant increment at about 42%. Imports of industrial and consumer goods also increased significantly during the quarter, by 36.8% and 23.4%, respectively.*
- *Fuel imports experienced a moderate growth rate of 13.7%. Agricultural (-16.1%) and semi-finished goods imports (-11.74%) showed a declining trend in the review quarter.*
- *During the review quarter, the country had a merchandise trade deficit of about $4.3 billion, compared to $3.3 billion in the previous quarter.*

3.1 Export Performance

3.1.1 Major Exports

During the review quarter, total exports stood at only $770.7 million. Total export proceeds declined by about 7.5% from $833.1 million in the first quarter (July-September 2023) to $770.7 million in the second quarter (October-December 2023). Table 6 shows the major export values, shares, and growth in the second quarter of 2023 relative to the first quarter of 2023.

Table 6: Major export values, share, and growth

Commodity	June-September, 2023			October-December, 2023		
	Value (USD) (B)	Share (%)	Percentage change	Value (USD) (C)	Share (%)	Percentage change (%)
Coffee	355.1	42.62	(19.5)	218.4	28.3	(38.5)
Flower	112.1	13.46	(9.5)	113.5	14.7	1.2
Pulses	85.5	10.26	(8.4)	88.4	11.5	3.3
Gold	78.8	9.46	68.4	85.3	11.1	8.2
Chat	43.3	5.20	(0.7)	46.3	6	7
Oil seeds	31.6	3.79	(56.7)	78.4	10.2	148.1
Textile & Textile Products	31.5	3.78	12.6	28.6	3.7	(9.3)
Fruits & Vegetables	17.6	2.11	5.0	18.7	2.4	5.9
Meat and meat products	13.6	1.63	(12.7)	15.3	2	12.4
Live animals	8	0.96	85.2	10.5	1.4	31.8
Leather &Leather Products	6.6	0.79	31.2	5.2	0.7	(20.6)
Others	19.9	2.39	(74.1)	26.7	3.46	46.2
Total exports	833.1		(15.8)	770.7		(7.5)

Source: Computed from data from the Ethiopian Customs Commission (ECC) and the NBE (2024)

Accounting for 28.3% of the total value of the country's exports, coffee dominated the top spot during the review quarter. This is followed by cut flowers (14.7%) and pulses (11.5%). Looking at the quarterly trend, there has been a shifting trend in the share of commodities. Though coffee remains the leading export commodity, its share declined during the review quarter. On the other hand, the share of several commodities has increased slightly. The share of total exports for oil seeds, chat, gold, and cut flowers increased in the review quarter. Oil seeds witnessed the largest increment in the share of exports from 3.8% in the first quarter to 10.2% during the review quarter.

Structurally, the composition of Ethiopian exports more or less remains unchanged, dominated by coffee, cut flowers, pulses, gold, oil seeds, and chat, accounting for about 82% of total exports in the review quarter. This demonstrates its heavy reliance on agriculture and primary commodities.

In this quarter, some commodities showed growth while others exhibited a negative percentage change. Among the major exports, the highest growth between the two periods was observed for oil seeds (148.1%), the largest increase of any commodity during the review quarter. This is followed by live animals (31.8%), and meat and meat products (12.4%). For instance, looking at the drivers of the growth of oil seeds, it was mainly due to a hike in unit prices (97.6%) and an expansion in volume (55.6%) of the commodity.

The top three commodities that experienced a decrease in export value in the review quarter include coffee (by 38.5%), textile & textile products (by 9.3%), and leather and leather products (by 20.6%). Despite contributing to the lion's share of export earnings, the share of coffee in total merchandise exports declined by 33.5% in the review quarter from 42.6% a quarter earlier in the same year.

There was a decrease of 7.5% in total exports from the first quarter (USD 833.1 million) to the second quarter (USD 770.7 million). The slowdown in export earnings from key commodities can explain the faltering performance of exports. Coffee appears to be the major contributor to this decline. Among the major exports, the largest drop in export foreign earnings was observed for coffee, where exports for the commodity plummeted by a staggering 38.5% compared to the previous quarter.

3.1.2 Prices and Volume of Exports

The growth rate and the overall size of exports during the quarter show that the country's export sector is struggling. It is important to identify some of the drivers of the observed change in exports during the review quarter, at least, in terms of volume and price. Table 7 decomposes export growth into volume, price, and interaction effects. This approach enables us to decompose export growth into its constituent parts: export volume changes, export price changes, and any interaction effects between price and volume. Export growth can be decomposed into changes in volume and unit price using the following identity equation:

$$Export\ Growth\ (\%) = \ Volume\ Change\ (\%) + \ Price\ Change\ (\%) + \ Interaction\ Effect\ (\%) \quad (\mathbf{1})$$

Export growth (%) measures the overall change in the value of exports between two periods, calculated as the percentage change in total export revenue. Volume change (%) reflects the change in the quantity of goods exported, independent of price changes. It is measured in units (e.g., tons, barrels) or a volume index. Price change (%) represents the change in the average price per unit of export goods, independent of quantity changes. It is typically calculated as a percentage change in the average export unit value of the commodity. The interaction effect (%), on the other hand, captures the combined effect of changes in volume and price. It's a relatively small term and can be ignored due to its minimal impact.

Then, export growth is decomposed into volume and price effects using the following identity:

$$Export\ Growth\ (\%) = \frac{(Q_1 - Q_0)}{Q_0} * 100 + \frac{(P_1 - P_0)}{P_0} * 100 + \frac{(Q_1 - Q_0)(P_1 - P_0)}{(Q_0 P_0)} * 100 \qquad (\mathbf{2})$$

Where = [$(Q_1 - Q_0) / Q_0 * 100$] represents the percentage change in volume, [$(P_1 - P_0)$ / P0 * 100] represents the percentage change in price, [$(Q_1 - Q_0)) * (P_1 - P_0)$ is the interaction effect, and

(Q_0P_0) is the base-year quantity and price against which the changes are compared, Q_1 and P_1 are the volume and price of export in period 1 and, Q_0 and P_0 are the volume and price in the previous or reference period.

In most cases, the interaction effect is negligible, so equation (2) simplifies to

$$Export\ growth\ (\%) \approx \text{Volume change}\ (\%) + Price\ change\ (\%) \tag{3}$$

Table 7: Volume and price effects of major exports on export growth (%) (October to December 2023)

Commodity	Growth	Volume effect	Price effect	Interaction effect
Coffee	(38.5)	(25.6)	(17.4)	4.4
Oil seeds	148.1	148.6	0.2	(0.3)
Gold	8.2	3.4	4.7	0.2
Chat	7	8.5	(1.4)	0.1
Pulses	3.3	(0.4)	3.7	0.0
Cut flower	1.2	(1.6)	2.9	0.0

Source: Computed from data in the ECC and NBE (2024)

Table 7 shows the decomposition results of export growth in volume, price, and interaction effects. Oilseeds exhibit the highest volume effect at 148%, while coffee displays the highest price and interaction effects. Coffee exports saw a significant drop in earnings due to a 25.6% decrease in volume and a 17.4% price drop, leading to a total export decline of 38.5%.

The sharp decline in the growth of coffee exports can be primarily attributed to a decline in the domestic supply volume and to the effect of prices. In other words, the decline in volume seems to play a bigger role while the negative changes in both the volume and unit price of coffee indicate that both factors have contributed to the deteriorating export growth of coffee. The decline in coffee prices may be linked to the fall in demand in export destinations. More concerning is the declining volume of coffee supplied to the external market. According to the United States Department of Agriculture (USDA), Ethiopia's coffee production experienced a reduced output as dry conditions lowered yields, resulting in a lower supply of coffee bean exports (USDA, 2023).

The drop in the volume of coffee exports may also be linked to the provision of fewer loans by Ethiopian banks due to liquidity problems. Another possible explanation may be linked to the rise in domestic consumption of coffee. Ethiopia is one of the largest coffee consumers domestically. Moreover, the security situation in the country might have contributed to the falling volume of coffee supplied to the export market in terms of constraining the production, distribution, supply, and marketing of coffee. Generally, it may also reflect the stagnated productive capacity of the economy to produce the major exportable goods of the country.

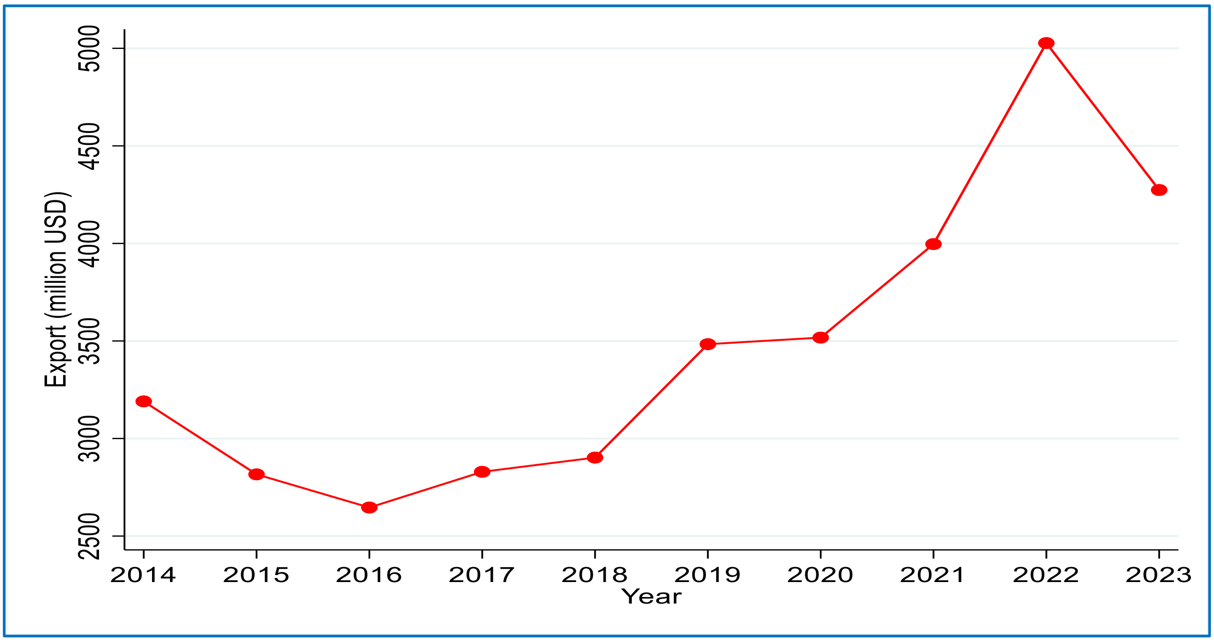
On the other hand, oilseeds exports saw a massive surge (148.1%) due almost entirely to a substantial volume increase (148.6%) with a negligible price change (0.2%). Gold exports achieved significant growth (8.2%) due to a balance between volume growth (3.4%) and price increase (4.7%). Chat exports also experienced a considerable increase (7.0%) driven primarily by a volume effect (8.5%) with a small price decline (-1.4%). Pulse exports also experienced a slight increase (3.3%) due to a price increase (3.7%) that offsets a small volume decline (-0.4%). Flower exports witnessed a small increase (1.2%) arising from price increases (2.9%) that outweighed a volume decline (-1.6%).

Overall, the contribution of volume and price effects to export growth varied across commodities. Coffee experienced a decline both in volume and price. On the other hand, exports like gold witnessed growth both in price and volume of exports. Oilseeds and chat saw significant growth primarily driven by volume increases that partially mitigated the drop or sluggish growth in price. To improve export growth, for instance, focusing on increasing the production volume of coffee alongside exploring new markets could further boost their export earnings. Production could be enhanced through encouraging the use of improved coffee cultivars and production practices. New markets could also be addressed by reaching new destinations through enhanced product quality and variety and meeting the required safety and quality standards. Moreover, it is crucial to target specialty coffee shops and roasters that value high-quality, single-origin beans.

3.1.3 Size of Exports

The size of a country's exports can be evaluated using various metrics such as the value of exports, exports as a percentage of GDP, and per capita exports. According to International Monetary Fund's (IMF) data, Ethiopia's merchandise exports totaled \$4.27 billion in 2023, with earnings declining by about 15% compared to 2022. This indicates a decline of \$753 million from the value of merchandise exports recorded in 2022. Merchandise exports of Ethiopia have changed by about \$1.08 billion in 2023 from \$3.19 billion in 2014 (Figure 8).

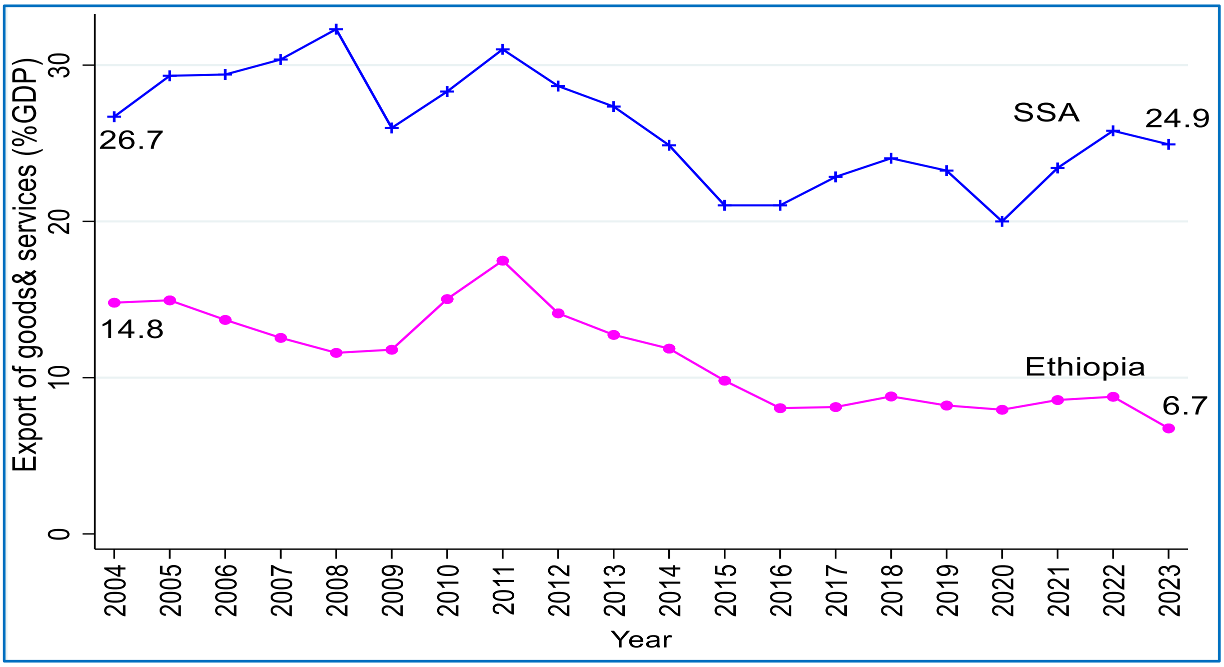
Figure 8: Merchandise exports trends for Ethiopia (2014-2023)



Source: Computed from data in the IMF Direction of Trade Statistics (DOT) (2024)

Figure 9 shows Ethiopia's exports of goods and services as a share of GDP. Ethiopia's exports of goods and services have declined steadily from 2004 to 2023. In 2004, exports of goods and services accounted for around 14.8% before declining to 6.7% of GDP in 2023. This is considerably below the SSA average of about 24.9% for 2023. This may indicate that Ethiopia's economy has been exporting less and becoming less integrated with the global economy compared to Sub-Saharan African economies over the last two decades or so.

Figure 9: Exports of goods and services in Ethiopia and SSA (% of GDP, 2004-2023)



Source: Computed from data in the African Development Bank (AfDB) (2024)

The underlying reasons for Ethiopia's exports not reflecting the potential of its GPD might be associated with the country's economy leaning heavily on agriculture with little value addition, often not generating sufficient export revenues. For instance, in the review quarter, the top six exports of the country (coffee, cut flowers, pulses, gold, oil seeds, and chat) are all primary/agricultural commodities, accounting for about 82% of merchandise exports. A related point is that the limited manufacturing base may hinder the production of high-value exportable goods. For instance, during the review quarter, among the top ten exports, the share of manufacturing/industrial goods in merchandise exports was only 7.7%. Perhaps, in 2022, evidence shows that the share of manufacturers in merchandise exports was only 9.1%, down from 17.4% in 2019. The data from the World Bank reveals that the average for the SSA was 21.4% during the same year**.**

Moreover, evidence also suggests that Ethiopia's exports are predominantly raw materials. The World Bank's World Integrated Trade Solution (WITS) also reveals that 73.2% of the country's exports are raw materials. On the other hand, for SSA, the regional average for the share of raw materials was 43%. In addition, the share of intermediate goods, textile and clothing, and capital goods accounted for barely only 9.7%, 5.7%, and 1.1% of total merchandise exports of Ethiopia, respectively.

On a per capita basis, Ethiopia has one of the lowest per capita export earnings globally. In 2023, using a population of 105.7 million (NBE, 2023), the country's per capita exports stood at $40.6. According to the OEC World, Ethiopia's per capita product export was $34.3 in 2022. It was ranked 179 out of 220 countries. This shows that the size of exports is incommensurate not only with the country's economic size but also with the population. Moreover, the per capita product exports surpassed imports in the same year. During the same year, the per capita product imports were $98.7.

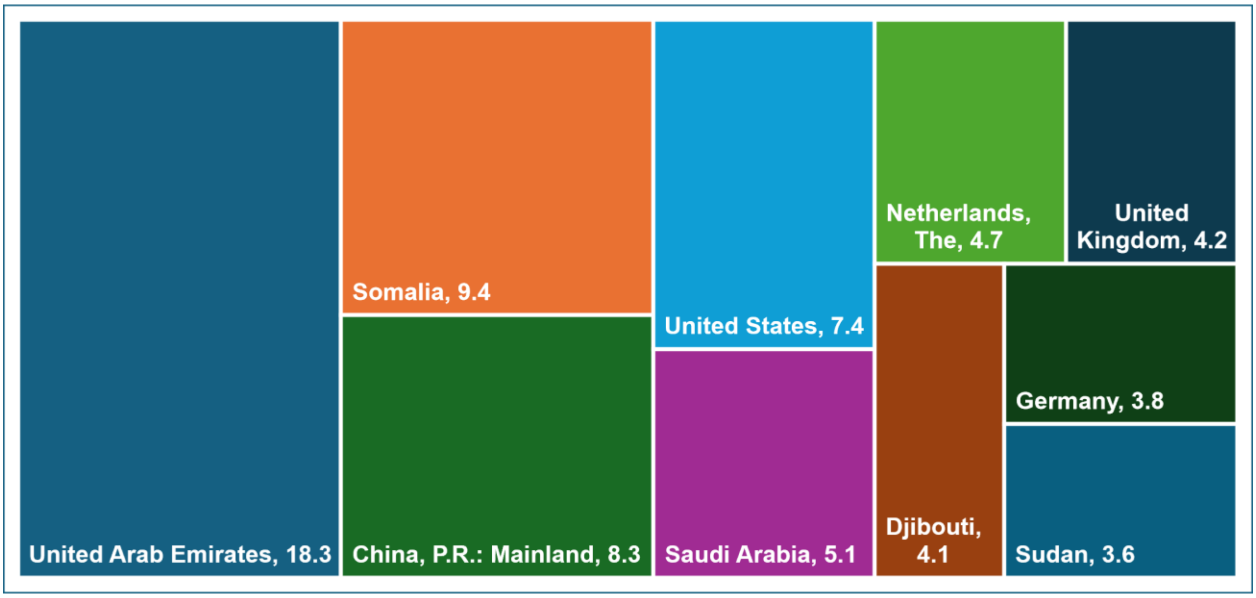
3.1.4 Major Destinations of Ethiopia's Exports

Using the latest available data, this sub-section briefly discusses the major destinations of exports. In 2023, Ethiopia exported to about 153 destinations. Figure 10 illustrates the top destination for Ethiopia's exports in 2023. The top destinations for Ethiopian exports are the United Arab Emirates, importing $781.3 million, accounting for about 18.3% of the total; followed by Somalia (9.4%), importing goods worth $400.9 million, China (8.3%), importing goods worth $356 million. United States accounted for 7.4% of the total, importing goods worth $316.9 million; Saudi Arabia (5.1%), with imports valued at $200 million. The emergence of the UAE as a leading destination of Ethiopian exports could be due to strong economic ties between Ethiopia and the UAE, including trade and investments, which might have fostered a favorable environment for Ethiopian exports. The UAE's strong re-export trade infrastructure might be the other possible reason for allowing Ethiopian goods to be re-shipped to other countries, expanding their reach and market potential[3]. In addition, the UAE's geographical location as a hub for global trade, particularly in the Middle East and North Africa, makes it an attractive destination for Ethiopian products seeking access to broader markets.

Except for the United Arab Emirates, the shares of Ethiopia's top ten export destinations are somewhat distributed evenly, indicating export market diversification. In terms of regional integration, the presence of Somalia (9.4%) as a top export destination suggests that there are strong regional trade ties between Ethiopia and its neighbors. Based on the export success to the UAE, Ethiopia could consider expanding its exports to other countries with similar characteristics. This could involve looking into regional hubs like Saudi Arabia, Egypt, and Oman in the Middle East and North Africa, as well as countries with strong re-export trade infrastructure, such as Singapore and Hong Kong, to enhance the country's exports.

[3] The UAE is among the top five countries in global re-export operations. Available at https://fastcompanyme.com/news/uae-among-top-five-countries-in-global-re-export-operations/#:~:text=%E2%80%9CThe%20UAE%20is%20the%20world's,UAE's%20GDP%2C%20said%20the%20minister.

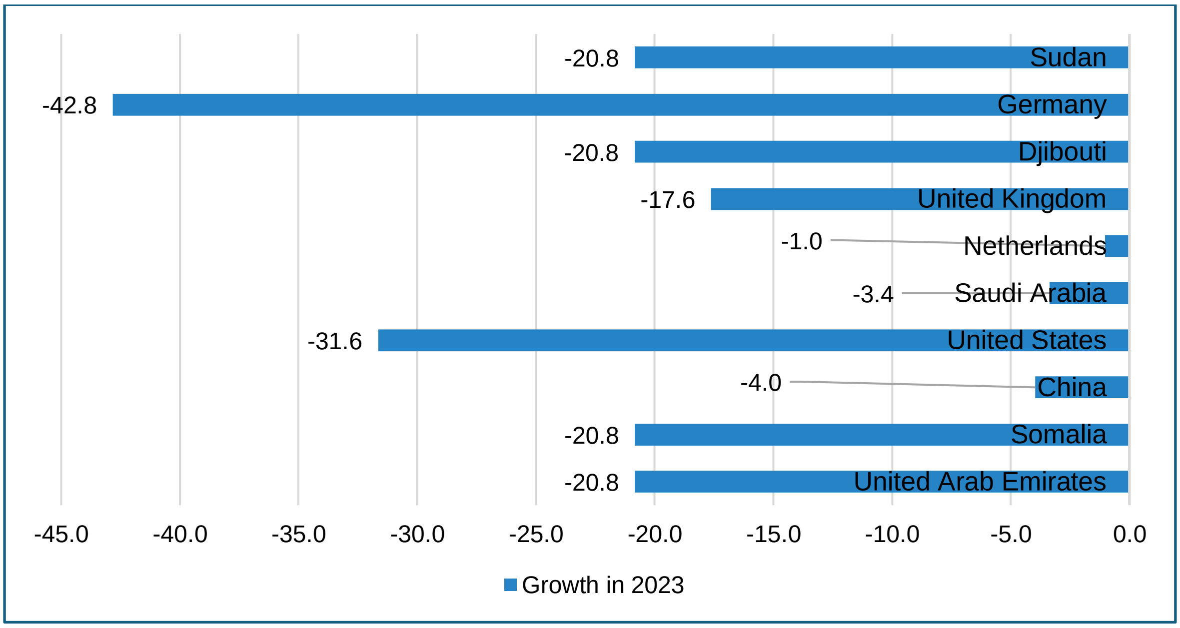
Figure 10: Top 10 Destinations of Ethiopian Exports, 2023



Source: Computed from data in the IMF's DOT (2024)

Figure 11 demonstrates the export growth for the top ten export destinations in 2023 compared to 2022. Exports to all the top destinations experienced a significant slowdown. The largest drop in export earnings was observed in Germany (42.8%), followed by the United States (31.6%) and UAE (20.8%). Somalia and Sudan were the two important regional export destinations each experiencing a drop in earnings of 20.8%. Overall, the evidence suggests a negative trend in export growth for the major destinations, with aggregate exports plummeting by about 15%.

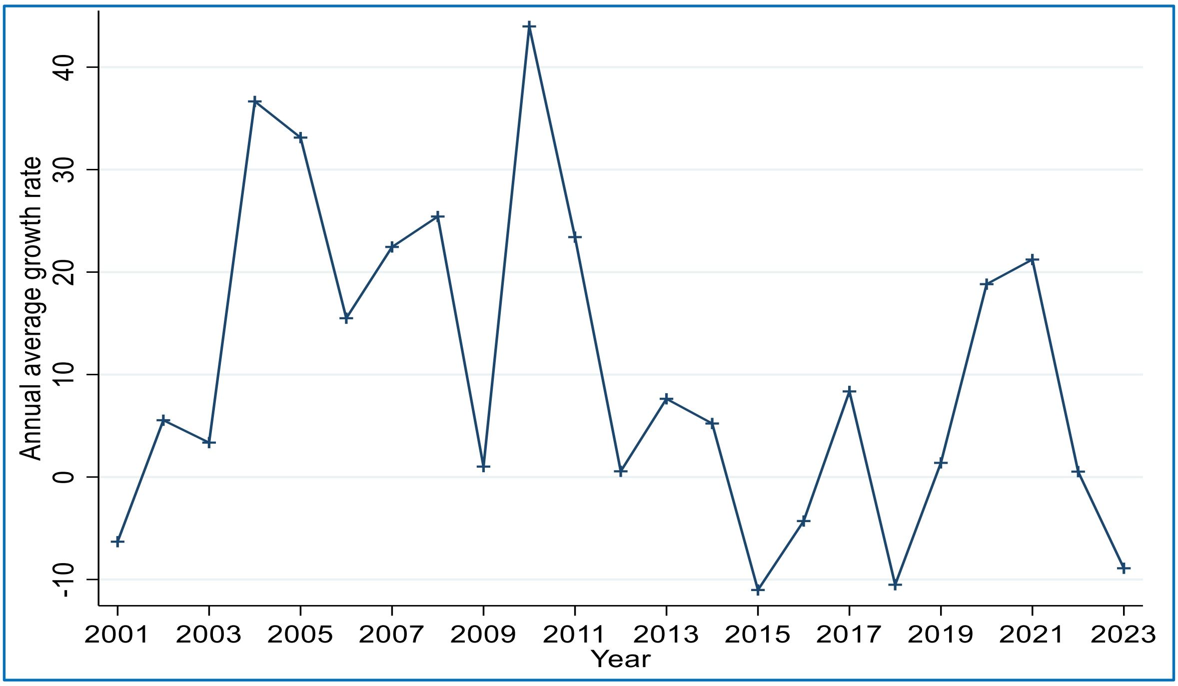
Figure 11: Total export growth by top 10 Ethiopia's export destinations (2023)



Source: Computed from data in the IMF's DOT (2024)

Figure 12 shows the average annual growth rate of exports for Ethiopia. The export growth rate fluctuates throughout the period, with some peaks and slowdowns. Overall, it appears to be slightly positive, with a possible upward trend emerging from negative growth in the post-2020 period.

Figure 12: Average annual export growth (2001-2023)



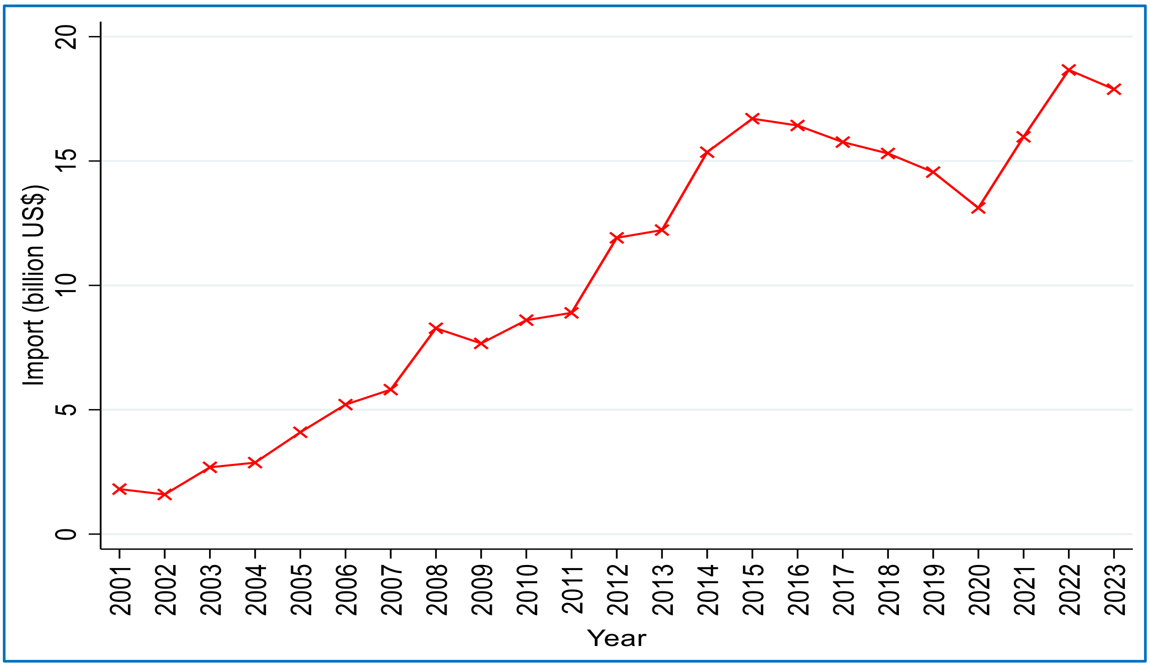
Source: Computed from data in UNCTAD (United Nations Trade and Development (2024)

The growth of exports is highly volatile, making the predictability of foreign exchange earnings and the country's trade balance more difficult. The oscillation in exports is more likely, among others, due to the fluctuation of prices and volume of exports.

3.2 Import Performance

Ethiopia's imports reached $17.8 billion in 2023. After a slowdown since 2017, imports rebounded in 2022. However, a distinct 4.1% drop in imports is observed in 2023 compared to 2022 (Figure 13).

Figure 13: Imports of goods (2001-2023)

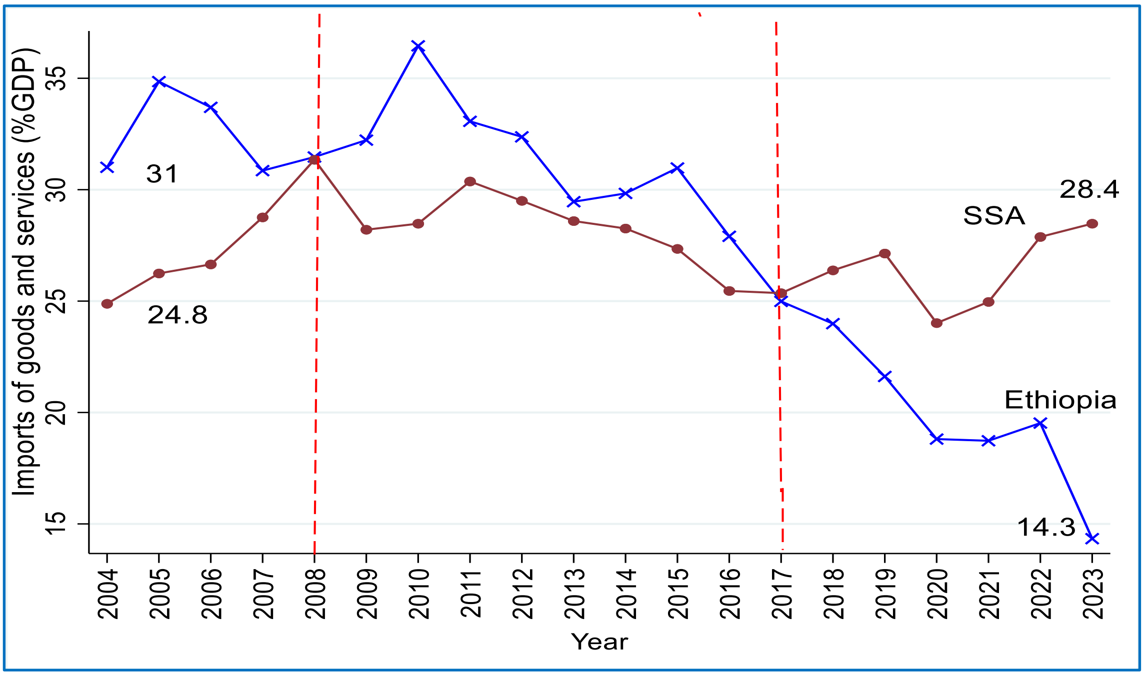


Source: Computed from data in UNCTAD (2024)

Ethiopia's imports of goods and services (% of GDP) have been higher than the SSA average until 2016, where imports averaged 31.8% while SSA's was 28%. However, the country's imports declined in the post-2016 period, declining from 27.9% in 2016 to 14.3% in 2023. Moreover, between 2004 and 2023, imports dropped by 53.7% from 31% in 2004 to 14.4% in 2023. However, the share of imports of goods and services in the SSA increased from 24.8% in 2004 to 28.4% in 2023 (Figure 14).

The decline in the value of imports and its share of GDP since 2016 might be possibly linked to rising global commodity prices, disruptions in global supply chains, such as those caused by COVID-19, limited availability and depletion of foreign exchange reserves, conflict, and a slowdown in economic activity.

Figure 14: Imports of goods and services (% GDP), 2004-2023)



Source: Computed from data in the AfDB (2024)

Major Imports

Table 8 shows Ethiopia's major import categories for the first quarter (July-September 2023) and second quarter (October-December 2023), along with the value (in million USD), share of total imports, and percentage change between the two quarters. Total merchandise import bills amounted to $4.8 billion during the review quarter, which saw a 17.8% growth compared to the previous quarter. In the review quarter, capital goods had the largest share of imports (31.1%), followed by consumer goods (28.7%) and industrial goods (23%). At 0.34%, agricultural goods have the lowest share of imports. The highest share of capital goods imports may indicate that a significant portion of Ethiopia's imports in the review quarter, as the case for the last decade, were goods used for long-term production, such as machinery and equipment. A decade ago, the share of capital goods was 32.8% in 2012/14 (NBE, 2013/14). This shows that capital goods remained the most important import of the country. On the other hand, the small share of agricultural products may suggest that reliance on foreign-produced agricultural goods has reduced.

At about 42%, capital goods, which are machinery and equipment used for production, saw the most significant increase in imports, leading to the growth in the country's imports during the review quarter. The import value of industrial and consumer goods increased significantly during the quarter, by 36.8% and 23.4%, respectively. Likewise, fuel imports, the country's fourth largest category of imports, experienced moderate growth (13.7%). On the other hand, agricultural goods imports (-16.1%) and semi-finished goods imports (-11.74%) decreased in the review quarter. The decline in the share of agricultural and semi-finished goods might be associated with the import restrictions/bans introduced by the government.

Table 8: Major imports by broad product category

Particulars/major import items	July-Sep. 2023		Oct-Dec. 2023		Percentage change in the review quarter
	Value (million, USD)	Share of imports (%)	Value (million, USD)	Share of imports (%)	
Semi-finished goods	950.2	23	838.6	17.2	-11.74
Fuel	914.5	22.2	1,039.6	21.4	13.7
Capital goods	1,066.6	25.8	1,513.9	31.1	41.9
Agricultural	19.9	0.5	16.7	0.34	-16.1
Industrial	817.9	19.8	1,119	23	36.8
Consumer goods	1,134.40	27.5	1,399.5	28.7	23.4
Total imports	4,126.9		4,863.6		17.8

Source: Computation based on Ethiopian Customs Commission (2024)

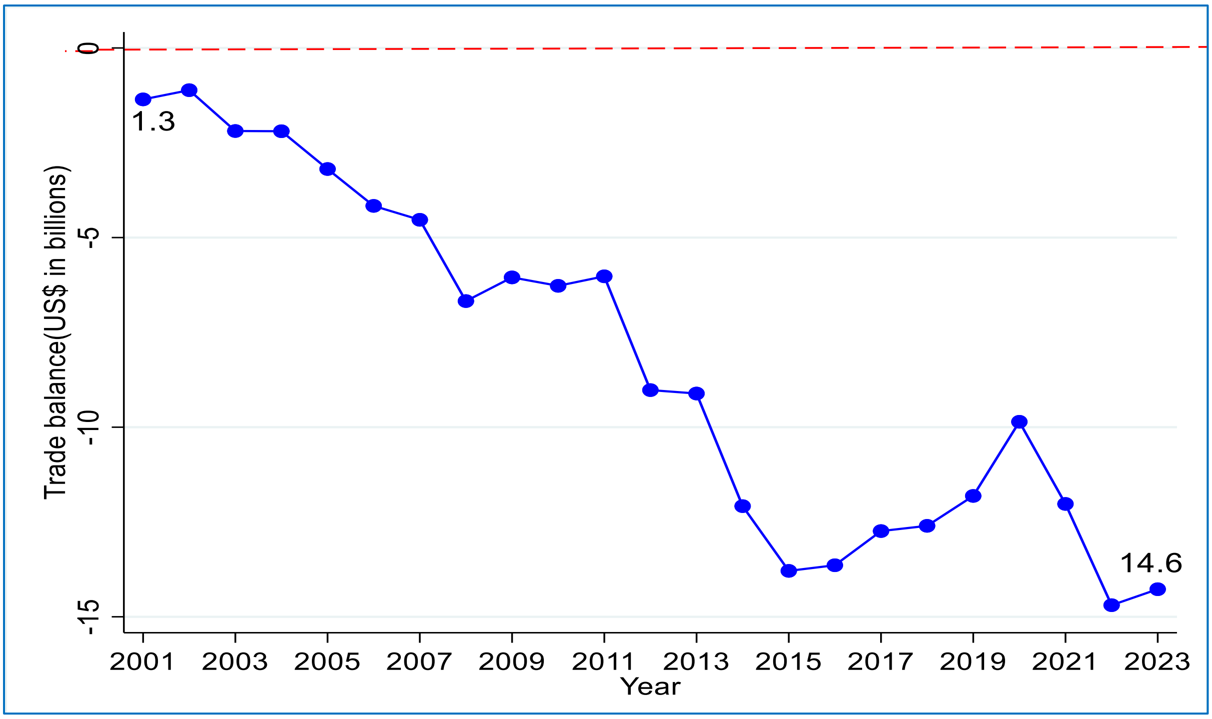
The Ethiopian government has imposed import bans on non-essential goods to address the shortage of foreign exchange and conserve foreign currency. As the forex shortage in the country is becoming critical, the government has banned 38 different products that are considered luxury items which include packaged food, household items, furniture, beauty products and automobiles, and various types of liquor imports in a circular order written by the Ministry of Finance to the National Bank of Ethiopia (NBE) on October 14, 2022. The government has decided to utilize the limited hard currency to import important items like medicines, agricultural inputs, capital goods, and raw materials for local industries (USDA, 2022). The allocation of limited foreign currency often prioritizes sectors deemed critical for economic stability and growth, such as capital goods, and essential consumer goods. In general, these fluctuations might be due to a combination of limited demand, and limited availability of foreign exchange for such goods, which may suggest that priority might be given to other goods or import substitution of such goods.

Overall, imports grew by 17.8% in the review quarter (October-December 2023) relative to the previous quarter. Despite the acute shortage of foreign exchange facing traders in the official market and the depletion of the foreign currency reserves in the country, the value of imports increased during the review quarter relative to a quarter earlier in the same year. It may be linked to the recent rise in the import price of commodities in the world market. According to UNCTAD, the unit value index of imports has been exhibiting a rising trend. The unit value index has increased to 160.1 in 2022 from 94.2 in 2016. This may also be linked to the fact that aside from foreign currency supplied through the official/formal channel, importers were accessing foreign exchange through the black market.

3.3 Trade Balance

Ethiopia's trade balance has been negative over the past two decades, suggesting that imports have consistently exceeded its export earnings. In 2001, the trade deficit was $1.35 billion. The deficit demonstrated strong growth over the years, reaching an all-time high of $14.6 billion in 2022. There was a modest improvement in 2023, with the deficit declining to $14.2 billion. A closer look at the figure illustrates that the trade balance growth rate has also been positive for most of the years, indicating that the deficit is worsening.

Figure 15: Trade balance, in billion US$ (2001-2023)

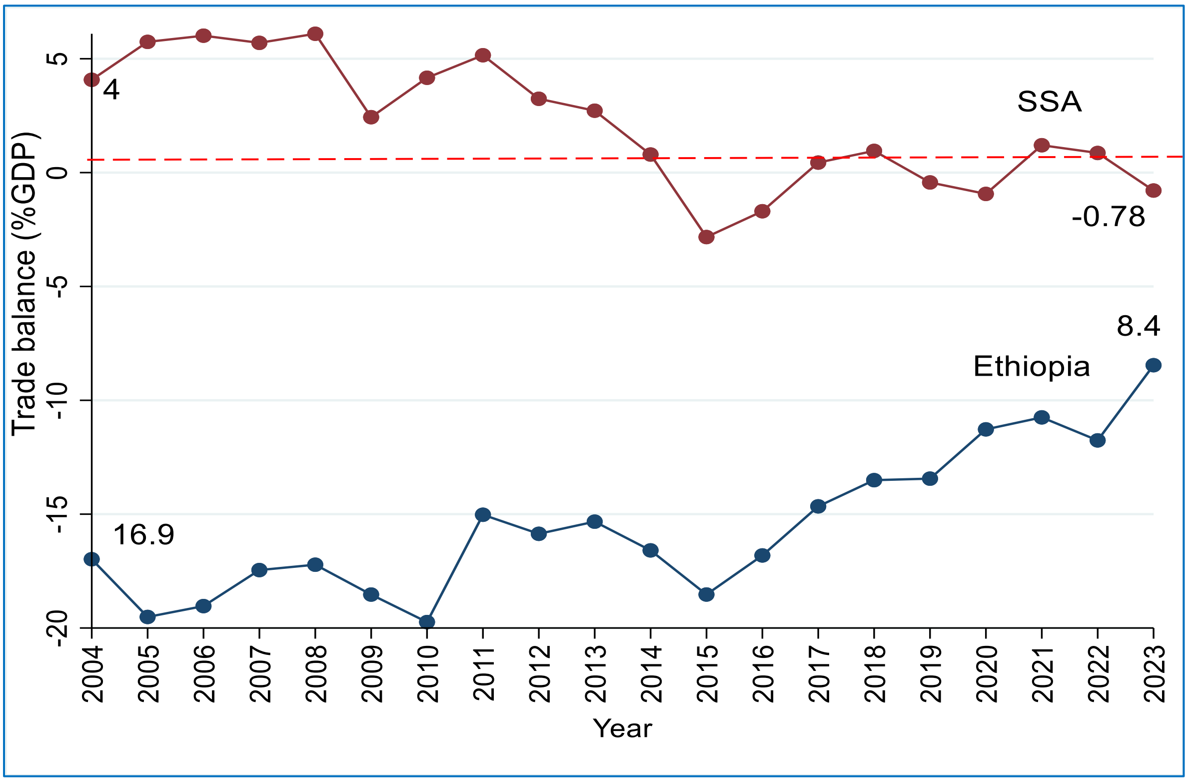


Source: Computed from data in UNCTAD (2024)

The AfDB's African Economic Outlook (AEO) data reveals a significant trade deficit relative to the country's economic size. While the deficit has declined from a peak of 19.7% of GDP in 2010 to 8.45% in 2023, it remains considerably higher than the SSA average of 0.78% in 2023. Notably, the SSA average has also declined from a surplus of 4% in 2004 (Figure 16).

Looking at the most recent dynamics, the country's trade deficit narrowed to 8.45% of GDP in 2023, a modest improvement from 11.7% in 2022. The modest improvement in the trade deficit might be associated with the slowdown in import growth from about 16.8% in 2022 to -4.1% in 2023, rather than an acceleration in the size of exports (Figure 17).

Figure 16: Trade balance (% GDP), 2004-2023)

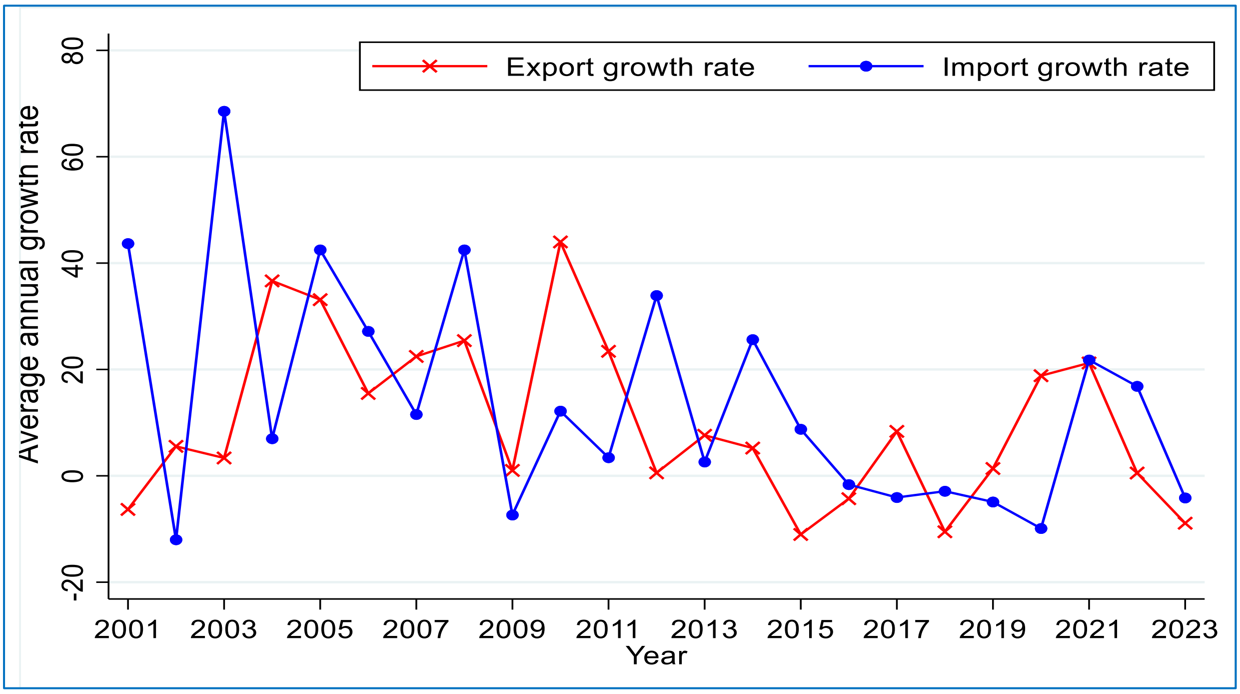


Source: Computed from data in AfDB (2024)

The trade balance deficit continues primarily due to the small size of exports compared to the demand for imports and the significant increase in imports, exceeding that of exports**.** The growth of imports is expected in an import-dependent and growing small economy. What is concerning is the small size and faltering export performance that contributes further to the widening of the current account deficit. Ethiopia's export sector remains particularly small. Perhaps, UNCTAD's data shows that merchandise exports increased by only $750.8 million between 2012 and 2022. More concerning, Ethiopia's export contribution to the GDP has been on a downward trajectory over the last decade. The size of exports of goods and services as a percentage of GDP declined significantly from 12.7% in 2013 to 6.7% in 2023. This is significantly below the 24% expected from a country the size of Ethiopia at its level of development (World Bank, 2017).

Ethiopia's chronic trade deficit reveals a structural imbalance in its international trade. Apart from the tiny size of exports, this imbalance may appear to suggest two key issues. First, demand for imports outpaces export capacity. That is, Ethiopia imports more goods than its exports. This might be explained by the lack of industrial capacity to manufacture diversified industrial goods Second, it is also linked to the type of goods that Ethiopia exports—low-value goods characterized by high price volatility in the global markets. Ethiopia's exports are less complex products produced by most countries and less competitive in international markets. There is no diversity and uniqueness of agricultural commodities to compete in international markets. They rather lead to high instability of export earnings and widening trade deficits.

Figure 17: Average export and import growth (annual %)



Source: Computed from data in UNCTAD (2024)

What is disappointing is that the size and growth of merchandise exports have not witnessed a significant increment following measures of exchange rate devaluation and export promotion policies**.** To support exports and encourage the private sector, for instance, on October 10, 2017, the NBE devalued the local currency by 15% (World Bank, 2017). Following the devaluation, however, exports as a percentage of GDP declined from 8.2% in 2017 to 6.7% in 2023. During the same period, imports increased by $2.12 billion while merchandise exports increased by only $594 million. The small size and underperformance of exports are mainly due to structural and competitiveness issues, such as rigid product markets and overvalued exchange rates. Challenges range from supply issues and quality of products to marketing channels, branding, and so forth (World Bank, 2017). Given the small size and sluggish growth of exports and significant trade deficit, Ethiopia faces critical economic challenges driven by an imbalance in import-export dynamics.

4. Concluding Remarks

The Ethiopian economy faces significant macroeconomic imbalances and challenges, arising partly from rapid monetary expansion, an overdependence on primary commodity exports, and a burgeoning trade deficit. Excessive money supply growth, fueled by multiple shocks, government borrowing, and deficit financing is exacerbating inflationary pressures. Despite recent policy interventions by the NBE, the effectiveness of monetary policy in curbing inflation is possibly hindered by continued government borrowing and other supply-side problems.

Moreover, the concentration of the banking sector, with a dominant state-owned bank, limits competition and may distort credit allocation. While the private sector remains the primary recipient of loans in the country, the overall deposit mobilization and loan disbursements are skewed towards a few (state-owned) large banks and the credit landscape towards specific sectors such as manufacturing, domestic trade, and export. This concentration, coupled with the recent decline in credit extended by private banks, raises concerns about the effectiveness of monetary policy transmission in public banks and potential credit constraints for key businesses.

Ethiopia's external sector is characterized by a small size of exports, heavy dependence on primary exports, growing import demand, and persistent trade deficit. The country's vulnerability to global price volatility and limited export diversification hinders export earnings growth, exacerbating the trade deficit. The trade deficit is primarily due to the dominance of low-value primary commodities in exports and imports outpacing export growth. The persistent trade deficit is leading to a growing external debt problem for the country, weakening the economy's ability to withstand external shocks.

Ethiopia requires a comprehensive and coordinated policy response to address these macroeconomic challenges. This shall include stringent fiscal discipline to reduce government borrowing, particularly from the NBE and inflationary pressures. In this regard, although the NBE's 2023 policy statement aimed to limit lending to the government to one-third of the previous fiscal year, the implementation is not as claimed and needs to be properly implemented. The measures shall also include fostering a competitive banking sector to enhance credit allocation efficiency and implementing structural reforms to diversify the export base. By promoting value-added production and manufacturing, Ethiopia can increase its export earnings, reduce its heavy reliance on primary commodities, and build a more resilient economy. Ultimately, the success of these efforts hinges on the government's commitment to macroeconomic stability, financial sector development, and export-led growth. To promote export-led growth, it is crucial to address infrastructure constraints by investing in improvements, streamlining export procedures to overcome bureaucratic hurdles, expanding export credit facilities to increase access to finance, and implementing certification programs and quality control measures to address issues related to product quality and standards. Without decisive action, the country may risk further macroeconomic balances and reduced prospects for macroeconomic stability.

References

Deloitte (2023). *East Africa Macroeconomic Outlook Volume IV.* Nairobi: Deloitte.

EEA (Ethiopian Economics Association) (2024). Economic Performance and Governance in Ethiopia (unpublished), Report on the Ethiopian Economy 2024, Addis Ababa, Ethiopia

Mengistu, A. (2021). Ethiopia's Macroeconomic and Finance Policy Framework for Structural Transformation. *UNCTAD/BRI PROJECT/RP 19. UNCTAD.*

Ministry of Finance (2023). *Public Sector Debt Statistical Bulletin, Bulletin No. 47.* Quarterly, Addis Ababa: MoF.

Ministry of Finance (2024). Public sector debt statistical bulletin, *Bulletin No. 47.* Quarterly, Addis Ababa: MoF.

National Bank of Ethiopia (2014). *Annual Report 2013/14.* Addis Ababa: NBE.

National Bank of Ethiopia (2017). *Annual Report 2016/17.* Addis Ababa: NBE.

National Bank of Ethiopia (2023). *Annual Report 2021/22.* Addis Ababa: NBE.

National Bank of Ethiopia (2023). Delivering on our Stability Goals: NBE's Strategic Plan for 2023-26. Addis Ababa: NBE.

National Bank of Ethiopia (2023). *Monetary Policy Statement.* Press Release, Addis Ababa: NBE.

National Bank of Ethiopia (2024). A New Monetary Policy Framework. Press Release, Addis Ababa: NBE.

United Nations Development Program (UNDP). (2023). *Ethiopia: Quarterly Economic Profile.* UNDP.

United Nations Development Program (UNDP) (2024). *Ethiopia: Quarterly Economic Profile.* UNDP.

United States Department of Agriculture (USDA) (2023). Coffee: World Markets and Trade. USDA.

United States Department of Agriculture (USDA) (2022). Ethiopia bans the import of 38 items including packed food. USDA.

World Bank (2017). Ethiopia Economic Update. The Inescapable Manufacturing-Services Nexus: Exploring the Potential of Distribution Services. Washington, D.C.

World Bank (2021). Ethiopia Economic Update. Ensuring Resilient Recovery from COVID-19. World Bank, Washington, D.C.

https://oec.world/en/profile/country/eth

https://ourworldindata.org/grapher/share-manufacture-exports

Annex

Deposit mobilization by the banking sector (2022-2023, and (June 30-Dec. 31, 2023)

Particular	End of December 2021/22	End of December 2022/23	June 2022/23	End of December 2023/24	First Six Months Change		Annual Change			
					2023/24		22/23		23/24	
					Absolute	Percentage	Absolute	Percentage	Absolute	Percentage
	A	*B*	*C*	*D*	*E=D-C*	*F=E/C*100*	*G=B-A*	*H=G/A*100*	*I=D- B*	*J=I/B*100*
Commercial Bank of Ethiopia	824,700.60	980,084.8	1,054,546.5	1,121,187.7	66,641.1	6.3	155,384.2	18.8	141,102.8	14.4
Development Bank of Ethiopia	980.80	927.0	1,584.4	1,776.3	191.9	12.1	(53.8)	(5.5)	849.3	91.6
Awash Bank	109,469.34	167,839.2	181,996.7	195,469.1	13,472.5	7.4	58,369.9	53.3	27,629.9	16.5
Dashen Bank	69,274.02	101,468.9	114,522.2	123,548.3	9,026.1	7.9	32,194.8	46.5	22,079.4	21.8
Bank of Abyssinia	100,430.44	146,176.3	158,276.8	176,038.3	17,761.5	11.2	45,745.8	45.5	29,862.1	20.4
Wegagen Bank	30,208.84	38,968.4	42,365.3	46,495.6	4,130.3	9.7	8,759.5	29.0	7,527.3	19.3
Hibret Bank	43,672.75	59,025.8	64,837.5	67,034.9	2,197.4	3.4	15,353.1	35.2	8,009.1	13.6
Nib International Bank	43,065.04	55,584.5	58,461.0	52,480.9	(5,980.1)	(10.2)	12,519.5	29.1	(3,103.6)	(5.6)
Cooperative Bank of Oromia	76,098.98	111,106.3	115,826.9	113,725.7	(2,101.2)	(1.8)	35,007.3	46.0	2,619.5	2.4
Lion International Bank	24,898.33	26,647.0	27,307.5	31,047.6	3,740.0	13.7	1,748.7	7.0	4,400.6	16.5
Zemen Bank	19,738.52	30,366.8	36,241.5	38,309.4	2,067.9	5.7	10,628.2	53.8	7,942.7	26.2
Oromia Bank	34,741.35	48,845.5	53,874.5	53,946.1	71.6	0.1	14,104.1	40.6	5,100.6	10.4
Berhan Bank	22,083.48	29,674.4	33,675.8	32,283.9	(1,391.9)	(4.1)	7,590.9	34.4	2,609.5	8.8
Buna Bank	23,497.63	32,272.3	36,598.0	40,167.7	3,569.7	9.8	8,774.6	37.3	7,895.5	24.5

Abay Bank	26,526.02	37,149.3	41,642.8	47,321.9	5,679.2	13.6	10,623.3	40.0	10,172.6	27.4
Addis International Bank	6,039.27	6,991.1	7,474.6	7,435.6	(39.0)	(0.5)	951.8	15.8	444.5	6.4
Debub Global Bank	9,525.24	12,558.6	13,986.6	15,647.6	1,660.9	11.9	3,033.3	31.8	3,089.0	24.6
Enat Bank	11,492.28	14,936.0	17,806.5	18,055.7	249.2	1.4	3,443.8	30.0	3,119.7	20.9
ZamZam Bank	335.33	3,039.4	4,980.5	5,417.5	437.0	8.8	2,704.1	-	2,378.1	78.2
Hijra Bank	187.27	2,371.4	4,839.3	4,800.0	(39.3)	(0.8)	2,184.1	-	2,428.6	102.4
Goh Betoch Bank	8.73	610.5	911.8	975.8	64.0	7.0	601.8	-	365.3	59.8
Tseday Bank	-	18,631.7	34,160.1	32,094.0	(2,066.1)	(6.0)	18,631.7	-	13,462.2	-
Shebelle Bank	-	9,764.1	801.6	1,170.0	368.4	46.0	9,764.1	-	(8,594.1)	-
Siinqee Bank	-	811.6	24,047.7	33,086.0	9,038.3	37.6	811.6	-	32,274.4	3,976.5
Amhara Bank	-	484.7	19,714.2	22,623.8	2,909.6	14.8	484.7	-	22,139.1	4,567.8
Sidama Bank	-	5,714.9	29.2	331.5	102.3	44.6	-	-	(5,383.4)	-
Omo Bank	-	147.8	8,878.3	6,623.5	(2,254.8)	(25.4)	-	-	6,475.7	-
Tsehay Bank		525.9	2,302.1	3,063.6	761.5	33.1	-	-	2,537.7	482.5
Ahadu Bank	-	27,094.0	2,023.5	3,321.9	1,298.3	64.2	-	-	(23,772.1)	(87.7)
Gadaa Bank			1,605.6	3,046.1	1,440.5	89.7	-	-	3,046.1	-
Rammis Bank			-	771.4	771.4	-	-	-	771.4	-
Total	**1,476,974.2**	**1,969,818.1**	**2,165,519.2**	**2,299,297.4**	**133,778.2**	**6.2**	**492,843.8**	**33.4**	**329,479.4**	**16.7**

Source: Compiled from data in the NBE (2024)