I. Overview

1.1 International Economic Developments

The global activity has witnessed some strengthening since the middle of the year. The main drives for growth in the world economy stems from advanced economies, which are increasingly benefitting from declining private sector de leveraging, less fiscal drag and monetary accommodation. By contrast, in numerous emerging market economies, structural challenges, such as infrastructure deficits, product and labor market rigidities, and domestic and external imbalances, as well as tightened financial conditions are restraining the growth potential. Geopolitical risks, relating typically to the conflict between Ukraine and Russia and tension in major oil-producing countries remain present, but their impact on oil prices and global activity has been rather limited so far. Additionally, a potential reversal of global risk sentiment following a period of compressed risk spreads and very low volatility in financial markets could have negative consequences for the global economy.

In the United States, the upturn in economic activity has become more sustained over the past six months. Following an increase in GDP in the second quarter at an annualized rate of 4.6 percent real GDP rose by 3.5 percent at an annualized rate in the third quarter according to the first estimate by the Bureau of Economic Analysis. The expansion in the third quarter was supported by a turnaround in the contribution from net trade as exports grew strongly and imports declined, and by the continued strength of domestic demand.

In Japan, the recovery in economic activity following the sharp drop in output in the second quarter of 2014 has been subdued so far. Monthly indicators available up to September 2014 were generally soft, signaling that real GDP growth in the third quarter is expected to have returned to positive territory, albeit at a slower pace than originally anticipated. Despite picking up in September, industrial production has slowdown in the third quarter following weak demand. At the same time the rebound in private consumption has been limited in part by declines in real incomes and consumer sentiment. Meanwhile net exports of goods together with public and private (non-residential) investment are likely to have supported growth in the third quarter.

In China, GDP growth slowed slightly to 7.3 percent annually in the third quarter, from 7.5 percent in the previous quarter, as the effect of the modest monetary and fiscal stimulus started to relax. On a quarterly basis, growth decreased to 1.9 percent from 2.0 percent. Consumption and trade contributed most to growth, while the contribution from investment weakened, reflecting a slowdown in housing investment and more moderate credit growth.

1.2 Macroeconomic Developments in Ethiopia

Fuel prices

During the first quarter of 2014/15, the average price of Brent crude oil, used as a point of reference for international oil price has declined by 7.3 percent and stood at USD 102.1 per barrel compared with USD 110.1 per barrel recorded last year same quarter.

Following the movements in the level of international oil prices and other domestic factors, domestic retail prices have been adjusted accordingly. In the first quarter of 2014/15, the average retail price of fuel products in Addis Ababa scaled up by 12.7 percent to 18.97 Birr/liter from 16.83 Birr/liter last year same quarter.

Inflation

During the first quarter of fiscal year 2014/15, headline inflation slowed down to 1.9 percent from 4.1 percent registered last year same quarter. The quarter-on-quarter slowdown of general inflation by 2.3 percentage points, was attributed to the respective decline in both food & non-alcoholic beverages and non-food inflation by 2.0 and 2.6 percentage points. Similarly, quarterly headline inflation dropped by about 1.0 percentage point due to 1.1 and 0.8 percentage point decrease in food & non-alcoholic beverage and non-food inflation, respectively. In the review quarter, food & non-alcoholic beverage inflation contributed 1.5 percent to the headline inflation while non-food inflation contributed the remaining 0.4 percent.

Monetary Developments

Broad money supply (M_2) reached Birr 304.5 billion at the end of the first quarter of 2014/15, revealing quarterly growth rate of 2.3 percent and quarter-on-quarter expansion of 28.4 percent. The quarterly expansion in broad money supply was driven by 2.8 percent rise in domestic credit offsetting the 15.2 percent slowdown in net foreign assets.

Meanwhile, reserve money at Birr 86.4 billion during the same period depicted 21.0 percent quarter-on-quarter growth while it showed a 2.9 percent quarterly contraction. Excess reserves of commercial banks scaled up by 5.9 and 10.3 percent quarter-on-quarter and quarterly bases, respectively. The money multiplier, measured by the ratio of broad money to reserve money, grew by 3.3 percent vis-à-vis last year same quarter revealing continued improvement in monetization of the economy. On the other hand, the ratio of narrow money to reserve money showed 6.3 percent quarter-on-quarter decline owing to expansion of banking services that resulted in increased mobilization of quasi-money deposits.

Interest rate

Average savings deposit and lending rates remained unchanged at last year same quarter level 5.4 and 11.88 percent, respectively. Weighted average time deposit rate, however, slightly increased by 0.4 percentage points. On the other hand, weighted average yield on T-bills went down to 1.68 percent from 1.95 percent a year ago. During the review quarter, average time deposit rate and average lending rates were positive in real terms given 5.6 percent annual headline inflation in September 2014 while demand deposit rate and T-bills yield remained negative.

Financial Sector Developments

Banks, insurance companies and microfinance institutions are the main formal financial institutions operating in the Ethiopian economy. The number of banks existing in the country was 19 as at the end of September 2014, unchanged from the previous quarter and last year same quarter. Of the total banks, 16 were privately owned. During the review quarter, 115 new bank branches were opened, raising the total number of bank branches to 2,323, thereby improving population to total bank branch ratio from 42,985 in the previous quarter to 41,088.

About 34.5 percent of the total bank branches were located in Addis Ababa. Of the total bank branches, the share of private banks increased marginally to 55.8 percent from 54.6 percent in the preceding quarter due to their opening of 92 new branches as opposed to only 23 new branches for by public banks during the review quarter.

Likewise, the total capital of the banking system registered a 8.3 percent quarterly build up and reached Birr 28.7 billion, of which the share of private banks was 52.3 percent. Commercial Bank of Ethiopia, the state owned bank, accounted for 37.3 percent of the total capital of the banking system while the other for public banks namely Development Bank of Ethiopia and Construction & Business Bank together accounted for 10.4 percent.

The number of insurance companies was 17 by the end of the review quarter, of which 16 were private. Their branch network increased to 337 from 284 last year same quarter. Of the total branches, about 54.0 percent were located in Addis Ababa.

During the review quarter, the total capital of the insurance industry recorded an 8 percent quarterly growth and reached Birr 2.2 billion of which private insurance companies accounted for 79 percent, slightly higher than 78.7 percent share in the preceding quarter.

Similarly, the 32 micro-finance institutions (MFIs) operating in the country mobilized a total saving deposit of Birr 11.8 billion, which was 52.3 percent higher than last year same quarter. Their outstanding credit also surged by 28.9 percent quarter-on-quarter to reach Birr 17.5 billion. As a result, their total asset expanded by 34.7 percent on annual bases and totaled Birr 25.1 billion at the end of September 2014. MFIs are significantly contributing to poverty reduction by mobilizing savings from and providing loans to the low-income segments of the population.

Total resources mobilized by the banking system (as measured by the sum of net change in deposit, loans collected and net change in borrowings) plummeted by 44.9 percent on quarterly bases, but it has been surged by 89.9 percent compared to last year same quarter.

In the review quarter, the banking sector disbursed Birr 16.1 billion in fresh loans, showing 67.8 percent growth as compared to last year same quarter. Public banks disbursed Birr 7.5 billion with (46.8 percent) share while the remaining balance was disbursed by private banks.

The banking system collected Birr 15.2 billion, about 8.9 percent lower than the preceding quarter but 23.6 percent higher than last year same period. Of the total loan collection, private banks collected Birr 7.8 billion (51.1 percent) while public banks collected Birr 7.4 billion (48.9 percent). Of the total loan collection, 91.9 percent was from private enterprises (including cooperatives).

Total outstanding credit of the banking system (excluding credit to government and interbank lending) increased to Birr 172.3 billion at the end of September 2014, up by 2.4 percent on quarterly basis.

External Sector and Foreign Exchange Developments

In the quarter under review, total earnings from merchandise export increased by 14.1 percent but decreased by 25.5 percent compared to last year same period and the preceding quarter, respectively and amounted to USD 720.4 million. The quarter-on-quarter growth was ascribed to the 32.9 percent surge in the export earnings from coffee, oilseeds (23.7 percent), pulses (31.6 percent), flower (10.9 percent), meat & meat products (19.2 percent), leather & leather products (3.2 percent), fruits & vegetables (4.1 percent) and gold (0.4 percent). The increase in these export earnings was due to higher export volume, international prices or both. The 25.5 percent quarterly decline in total export revenue was due to slow down in export earnings from major export items, mainly coffee (44.2 percent), oilseeds (36.1 percent), flower (21.2 percent), fruits & vegetables (15.0 percent), gold (41.8 percent) and chat (7.7 percent).

Export earnings from coffee in the review period increased by 32.9 percent quarter-on-quarters but decreased by 44.2 percent on quarterly basis. The quarter-on-quarter increment in export earnings from coffee was attributed to a significant recovery in coffee prices and an increase in volume of coffee export. In the review period, coffee unit price increased by 28.1 and 5.0 percent vis-à-vis last year same quarter and the previous quarter, respectively. On the other hand, the volume of coffee export rose by 3.8 percent compared to last year same quarter, but plummeted by 46.8 percent over the previous quarter. Consequently, export earnings from coffee in the first quarter of 2014/15 decreased to USD 182.6 million from USD 326.9 million in the preceding quarter but increased from USD 137.3 million in the first quarter of 2013/14. The share of coffee export revenue in total export earnings increased to 25.3 percent from 21.8 percent last year same quarter but it was lower than 33.8 percent recorded in the preceding quarter.

Total value of merchandise import during the first quarter of 2014/15 stood at USD 3.7 billion. Which was 26.6 percent lower than last year same quarter owing to a rise in import values of capital goods (63.8 percent), consumer goods (30.1 percent), semi-finished goods (8.6 percent) and raw materials (3.1 percent). Import value of fuel, however, went down by 11.2 percent vis-à-vis last year same period.

On the other hand, despite a fall in import bill of capital goods (1.2 percent), fuel (16.5 percent), semi-finished goods (7.1 percent) and raw materials (28.8 percent), total import bill in the first quarter of 2014/15 went up by 2.1 percent compared to the preceding quarter owing to a 31 percent hike in consumer goods bill as imports of both durable consumer goods and non-durable consumer goods increased by 12.1 and 42.3 percent, respectively.

During the review period total net transfer receipts went up by 2.84 percent quarter-on-quarter to reach USD 1.2 billion as net official transfers increased by 11.8 percent and private transfers up by 0.72 percent. Relative to last year same period, net private transfers increased by 0.72 percent and amounted to USD 931 million on account of the 11.96 percent growth in cash remittances from private individuals despite lower transfers to NGO (26.5 percent).

In the review period, current account balance (including official transfers) registered USD 1.8 billion in deficit, which was higher than USD 1.4 billion recorded a year earlier. The widening deficit was attributed to a 83.4 percent drop in net services receipts and a 30.1 percent surge in trade deficit. On the other hand, capital account recorded USD 1.4 billion in surplus about 214.2 percent higher than last year same quarter, as a result of 158.3 percent growth in net official long-term capital inflows, 105.3 percent increase in other public long-term capital inflow and 105.2 percent expansion in foreign direct investment.

The average official exchange rate of the Birr depreciated by 5.3 and 1.5 percent compared to last year same quarter and the preceding quarter, respectively, to reach Birr 19.7288/USD in the first quarter of 2014/15. Similarly, the parallel market average exchange rate at Birr 21.0731/USD depreciated by 6.6 and 3.6 percent during the same period. Hence, the premium in the parallel foreign exchange market widened to 6.8 percent from 5.5 and 4.7 percent on last year same quarter and the preceding quarter bases, respectively.

The review quarter witnessed the depreciation of REER of the Birr by 2.4 percent vis-à-vis last year same quarter owing to the weakening of nominal exchange rate of the Birr coupled with the slowdown in domestic inflation in the face of rising trading countries average inflation. However, the REER of the Birr marginally appreciated by 0.8 percent on quarterly basis. At the same time, NEER depreciated by 0.3 percent against the preceding quarter and by 3.7 percent compared to last year same quarter.

Federal Government Fiscal Operations

During the first quarter of 2014/15, Federal government total revenue and grants increased by 8.2 percent to Birr 33.5 billion from Birr 31 billion in the preceding quarter. Quarter-on-quarter basis, total revenue and grants increased by 17.1 percent.

On the other hand, quarterly Federal government expenditure decreased by 23 percent to Birr 32.7 billion but rose by 9.7 percent on annual terms.

Hence, the overall fiscal balance (including grants) depicted an overall surplus of Birr 827.8 million compared to Birr 1.17 billion and Birr 11.5 billion deficit a year ago and the preceding quarter, respectively.

Investment

A total of 1,359 investment projects with an aggregate capital of Birr 39.8 billion were licensed by the Ethiopian Investment Agency and Regional Investment Offices during the fourth quarter of 2013/14. The number of approved investment projects has increased by 21.9 percent on quarterly basis, despite 20.8 percent decline in investment capital. However, on annual basis the number of registered projects and capital investment rose by 110 and 52.6 percent, respectively. Of the licensed investment projects, about 99.7 percent were private of which 1,277 projects (94.2 percent) were domestic while the remaining 78 projects (5.8 percent) were foreign.