I. OVERVIEW

1.1 International Economic Developments

According to the European Central Bank economic bulletin, issued on 5 May, 2015, the global economy is expected to continue its modest upturn path following a slowdown in the pace of expansion in early 2015. The global composite output Purchasing Managers' Index (PMI), excluding the euro area, dished slightly in June, to below its long-term average. In quarterly terms, the index recorded a modest decline in the second quarter of 2015 compared with the previous quarter.

Quarterly output growth remained solid in developed economies, predominantly in the United States and the United Kingdom. PMIs in the emerging market economies (EMEs) continued to weigh on the global index, reflecting the ongoing decelerate in EME growth caused by both cyclical and structural factors. Meanwhile, other short-term indicators point to some resilience in global activity.

In United States, activity shows signs of a rebound, after freezing at the start of 2015. The decline in real GDP (at -0.04 percent quarter on quarter) in the first quarter of 2015 turned out smaller than previously estimated. The soft patch was mainly the result of cold weather, port disruptions caused by labor disputes, the impact of an earlier US dollar appreciation and a sharp decline in investment in the energy sector. Recent indicators are consistent with a bounce back in GDP growth in the second quarter.

In Japan, available indicators suggest a renewed softening in the growth outlook following the strong pick-up at the start of the year, while inflation remains low. GDP growth gained traction in the first quarter of 2015, with real GDP increasing by 1.0 percent quarter on quarter, mostly supported by a pick-up in private capital investment and a large contribution from the change in inventories. The short-term indicators for May were rather soft, with both industrial production and real exports falling, and growth in real consumption remaining weaker than in the first quarter. Meanwhile, the Bank of Japan's Tankan survey for June 2015 signaled an improvement in business confidence among both manufacturing and non-manufacturing firms compared with March.

In United Kingdom, economic growth slowed down at the beginning of 2015 and is expected to recover in the second quarter of the year. Real GDP growth decelerated to 0.4 percent in the first quarter, from 0.8 percent in the last quarter of 2014, largely as a result of a sharp fall in the contribution of net exports. However, domestic demand continued to support growth. The composite PMI and industrial production data suggest that growth should accelerate in the second quarter of the year.

In China, after a slowdown in the pace of expansion at the start of the year, real GDP growth rebounded, but the recent equity market correction has increased uncertainty. Following passive growth in real GDP of 1.4 percent, quarter on quarter, in the first quarter of this year, GDP growth rebounded to 1.7 percent in the second quarter. This was supported by the recent monetary fiscal stimulus measures. At the same time, pockets of weakness persist, as housing investment remained lackluster and imports weak. Uncertainty regarding China's growth outlook and financial stability has increased somewhat following the sharp improvement in equity markets observed over the past month, which followed very rapid increases in previous months.

1.2 Macroeconomic Developments in Ethiopia

Fuel prices

During the fourth quarter of FY 2014/15, the average price of Brent Crude Oil, used as a point of reference for international oil price, turned down by 43.4 percent and reached USD 62.1 per barrel compared with USD 109.8 recorded in the previous year same quarter.

Following the movements in the level of international oil prices and other factors, domestic retail prices have been adjusted accordingly. In the review quarter, the average retail price of fuel products in Addis Ababa declined by 18.1 percent to 15.43 Birr/liter from 18.83 Birr/liter a year ago. Similarly, the retail prices fell by 2.1 percent compared with 15.76 Birr/liter registered in the preceding quarter.

Inflation

During the fourth quarter of the fiscal year 2014/15, headline inflation surged to 4.3 percent from 2.8 and 2.3 percent in the same quarter last year and the previous quarter, respectively. The rise in quarterly headline inflation by 2.0 percentage points was attributed to an increase in food & non-alcoholic beverages inflation by 4.2 percentage points offsetting a 0.3 percent marginal decline in non-food inflation. Quarter-on-quarter, headline inflation registered 1.5 percentage point rise owing to 2.1 percentage point growth in food & non-alcoholic beverages inflation and 0.8 percentage point in non food inflation. In the review quarter, food & non alcoholic beverage inflation contributed 3.1 percent to the headline inflation while non-food inflation contributed 1.2 percent.

Monetary Developments

Broad money supply (M_2) reached Birr 371.2 billion by end June 2015 indicating a quarterly growth rate of 6.3 percent and 24.7 percent annual expansion. The annual expansion in broad money was mainly driven by 31.1 percent surge in domestic credit, offsetting an 18.4 percent slow down in NFA. At the same time, the annual growth in domestic credit was due to a 32.8 percent growth in credit to non-central government and 14.1 percent rise in net credit to the central government.

Reserve money reached Birr 102.5 billion at the end of the fourth quarter of 2014/15, depicting 14.7 percent annual and 7.5 percent quarterly expansion. Excess reserves of commercial banks also showed 98.2 percent quarterly increase and 7.4 percent annual decline.

The money multiplier measured by the ratio of broad money to reserve money, grew by 8.7 percent on annual basis implying increased monetization of the economy. Similarly, the ratio of narrow money to reserve money showed 0.5 percent annual increase.

Interest rate

Average savings deposit and lending rates remained unchanged at 5.4 and 11.88 percent, respectively, while weighted average time deposit rate slightly rose by 0.5 percentage points to

5.77 percent. Weighted average yield on T-bills, however, dropped from 1.31 to 0.98 percent.

Considering the June 2015 headline inflation of 10.5 percent, all deposit rates and the t-bills yield remained negative while average lending rate was positive in real terms.

Financial Sector Developments

Banks, insurance companies and microfinance institutions constitute the main financial institutions in Ethiopia. The number of banks operating in the country reached 19 as at end of June 2015 of which 16 are owned privately. Compared to last year same quarter, 485 new bank branches were opened, raising the total number of bank branches to 2693. As a result, the ratio of total bank branch to population went down to 33,448.2 from 39,833.8 last year, reflecting an improvement in financial service outreach. About 35.5 percent of the total bank branches were located in Addis Ababa. Of the total bank branches, the share of private banks increased to 58.1 percent from 54.6 percent last year same quarter as they opened 359 new branches versus 126 new branches by public banks during the year.

The total capital of the banking system increased by 19.0 percent compared to last year same quarter and reached Birr 31.5 billion, of which private banks jointly accounted for 56.5 percent while the three state owned banks constituted the remaining balance. Commercial Bank of Ethiopia, the state owned bank, alone accounted for 34 percent of the total capital of the banking system with Development Bank of Ethiopia and Construction & Business Bank taking up 9.5 percent share.

The total number of insurance companies operating in the country remained at 17 of which 16 were private. The number of insurance branches increased to 377. Of the total branches, about 52.8 percent are located in Addis Ababa.

During the review quarter, the total capital of the insurance industry increased by 40.8 percent on annual basis and reached Birr 2.8 billion. The capital share of private insurance companies declined marginally by 1.1 percentage point as compared to the same period last year and stood at 77.6 percent.

On the other hand, there were 35 micro-finance institutions (MFIs) operating in the country. These MFIs have mobilized a total saving deposit of around Birr 14.8 billion, which was 4.1 and 25.9 percent higher than the preceding quarter and a year earlier, respectively. Similarly, outstanding credit of the MFIs grew by 16.7 and 29.5 percent and reached Birr 21.8 billion during the same period. As a result, their total assets increased by 5.5 and 24.6 percent on quarterly and annual bases and stood at Birr 30.5 billion. From these indicators one conclude that MFIs are broadly contributing to the country’s efforts to reduce poverty and enhance savings mobilization for investment and growth.

Concerning resources mobilization, total resources mobilized by the banking system increased by 30.6 percent on annual terms due to 57.1 percent increase in deposits (net change) and 13.1 percent rise in loan collections.

Meanwhile, total disbursement of fresh loans by the banking system reached Birr 18.9 billion, showing a 5 percent annual increase, of which public banks disbursed 55.6 percent and private banks the remaining balance.

About 99.6 percent of the new loan disbursement by private banks and 54.5 percent of the loan by public banks went to the private sector.

At the same time, banks collected Birr 18.9 billion, about 13.1 percent higher than last year. Of the total loan collection, 50.3 percent was by private banks and 49.7 percent by public banks.

Total outstanding credit of the banking System (excluding credit to government and interbank lending) increased to Birr 217.3 billion at the end of June 2015, up by 5.6 percent on quarterly basis. About 99.8 percent of outstanding loan of private banks was claims on private enterprises including cooperatives, and 0.2 percent on public enterprises. Similarly, 58.1 percent of the total public banks outstanding loan (excluding credit to government and interbank lending) was claims on public enterprises and 41.9 percent on private enterprises.

External Sector and Foreign Exchange Developments

Total merchandise export (including electricity) decelerated by 18.3 and 2.5 percent compared to the same quarter last year and the preceding quarter, respectively and amounted to USD 800.3 million. The quarter-on-quarter decline was attributed to the fall in the export earnings from coffee (7.8 percent), oilseeds (13.0 percent), gold (56.4 percent), chat (21.0 percent), pulses (38.5 percent), live-animals (2.1 percent) and electricity (47.0 percent) on account of slow down in international price, volume of export or both.

The quarterly decline in the total export proceeds was due to the fall in the export earnings of major export items, mainly oilseeds (29.3 percent), gold (49.8 percent), chat (12.9 percent), pulses (38.2 percent), leather & leather products (0.03 percent) and electricity (37.0 percent).
Total value of merchandise import during the fourth quarter of 2014/15 stood at USD 4.2 billion, a surge of 16.4 percent compared to last year same quarter owing to the rise in import value of capital goods (28.9 percent), consumer goods (31.4 percent) and semi-finished goods (24.3 percent) despite fuel and raw material import bill decreased by 33.9 and 17.4 percent, respectively.

During the review quarter, total net transfer receipts decreased by 10.4 percent relative to last year same quarter and stood at USD 1.3 billion as net official transfers declined by 61.8 percent. Relative to last year same quarter, net private transfers increased by 5 percent during the review quarter and amounted to USD 1.2 billion on account of 16.8 percent surge in cash remittances and 56.2 percent rise in underground transfers from private individuals in spite of decline in transfers to NGOs by 15 percent.

The current account balance (including official transfers) registered USD 2.3 billion in deficit during the fourth quarter of 2014/15, higher than USD 1.2 billion deficit recorded a year ago. The widening of the deficit is attributed to the remarkable fall in net services receipts (4,065.1 percent), net official transfers (61.8 percent) and increase in trade deficit (29.3 percent).

In the review quarter, the capital account recorded USD 1.8 billion in surplus; about 12.8 percent lower than that of last year same quarter. This was due to the 74.1 percent decline in inflows of net official long-term capital, despite a 184.5 percent surge in other official long-term capital and 31.5 percent in foreign direct investment.

In the inter-bank forex market, the weighted average official exchange rate of Birr with respect to USD has depreciated by 5.2 and 1.2 percent compared to last year same quarter and the preceding quarter, respectively, to reach Birr 20.4466/USD. Similarly, the average exchange rate in the parallel market depreciated by 12.5 and 0.02 percent respectively during the review period to reach Birr 22.8914/USD. As the foreign exchange parallel market rate showed a relatively faster annual deprecation due to speculative practices, the premium between the parallel and official market widened in the review quarter to 12 percent from 4.7 percent in same quarter last year.

The REER appreciated both on quarter-on-quarter and quarterly basis mainly due to relatively higher domestic inflation and fast depreciation of trading partners' nominal exchange rate compared to that of Birr. Equally, NEER appreciated by 0.37 and 4.03 percent compared with the preceding quarter and last year same quarter, respectively.

Federal Government Fiscal Operations

Federal government tax and non-tax revenue amounted to Birr 39.2 billion during the fourth quarter of 2014/15 about 38.8 percent higher than last year same quarter. Tax revenue constituted 84.8 percent share while non-tax revenues accounted for the balance.

Similarly, total federal government expenditures including regional transfers registered growth rate of 40.5 percent compared to a year ago, and reached Birr 59.7 billion. Out of the total expenditure, regional transfers accounted for (Birr 29.1 billion or 48.7 percent) followed by capital expenditure (Birr 18.6 billion or 31.2 percent) and current expenditure (Birr 12.0 billion or 20.1 percent).

Year-on-year, recurrent expenditures went up by 40.9 percent as a result of the surge in its all components of expenditure, while , capital expenditure went down by 5.6 percent mainly as a result of lower out lay for in social development.

During the review quarter, federal government budgetary resulted in 20.4 billion deficit, about 78.2 percent higher than last year. The deficit was financed by net external borrowing, net domestic borrowing and others & residuals.

Investment

During the fourth quarter of 2014/15, 179 investment projects went operational with total investment capital of Birr 608.5 million. From last year same quarter, the number of investment projects and the amount of investment capital grew by a 145.2 and 51.2 percent, respectively.