I. OVERVIEW

II. OVERVIEW

Macroeconomic Developments in Ethiopia

International Economic Developments and their Impact on the Ethiopian Economy

Towards the end of 2011, signs of stabilization in global economic activity began to emerge. Nevertheless, structural impediments are expected to continue to restrain the pace of growth in the global economy over the medium term. These impediments mainly relate to weaknesses in the labour and housing markets in some major advanced economies as well as to the need for further repairs to both public and private sector balance sheets.

In an environment of improving financial markets, both business and consumer sentiment have shown signs of improvement. The Purchasing Managers' Index (PMI) for global all-industry output continued to increase, is reaching 55.5 in February. The improvement in business conditions was broadly based across sectors and countries.

Looking ahead, the recovery in 2012 is expected to proceed at a more robust pace than previously anticipated, given that the latest monthly data have surprised mainly on the upside and point to a continued economic expansion in the first quarter of 2012.

US non-farm payrolls were better than expected in January and employment growth was widespread in the private sector, including the construction industry. Moreover, jobless claims continued to decline in February, indicating a more resilient labour market in the first quarter. According to several housing market indicators, housing activity, which collapsed during the recession, appears to be bottoming out.

In the other non-euro area EU Member States, aggregate growth is expected to be relatively slow in the near term, with some countries at risk of a recession. In Sweden and Denmark, the outlook for economic activity has become more subdued. However, in the fourth quarter of 2011, growth and especially external trade dynamics were very diverse in the two economies.

Asia, economic growth held up well in the fourth quarter of 2011, despite worsening global economic conditions. Export growth slowed significantly in the last quarter of 2011, partly on account of a drop in global demand, while investment remained weak as a result of a heightened volatility of capital flows and the lagged effects of a tightening of domestic monetary policies. By contrast, private consumption remained strong.

Ethiopian external economic sector started to respond to the slow down of global economic activities, in particular of advanced economies. For instance, growth in total Ethiopia's export of goods slowed down to 8 percent annualized in the second quarter of 2011/12, from 33.7 percent in the preceding quarter mainly due to the reduction in volumes of major export products and the pace of international prices of the export products.

Inflation

During the second quarter of 2011/12 fiscal year, headline inflation slowdown to 4.6 from 6.6 percent in the previous quarter on account of 4 percentage point decline in food inflation which offsets a 1.2 percentage point surge in core inflation. Quarterly food inflation scaled down to 4.8 percent from 8.8 percent during the previous quarter whereas core inflation increased to 4.5 percent from 3.3 percent in the first quarter. Food inflation contributes 3.0 percent of the quarterly inflation while non-food took the remaining 1.6 percent share.

Fuel prices

During the review quarter, the average international price of the crude oil was USD 103.04 per barrel, down by 11.7 percent compared to the previous quarter. However, Addis Ababa average retail price of fuel has remained to be Birr 17.7 per liter during the quarter.

Monetary Developments

The stocks of broad money supply (M2), measure of monetary aggregate in Ethiopia stood at Birr 155.9 billion at the end of December 2011 showing 3.4 and 32.3 percent quarterly and annual grow, respectively. Net foreign asset was Birr 49.3 billion at the end of the quarter, revealing 11.1 percent quarterly decline whereas net domestic credit has scaled up by 32.9 and 8.7 percent vis-à-vis the balance in December 2010 and September 2011 to reach Birr 146.8 billion at the close of the review quarter, respectively. The surge in broad money supply on annual basis was on account of an increase in net foreign asset and net domestic credit which counterbalanced the rise in other items net over the same period by about 48.3 percent. Quarterly increase in broad money supply on the other hand, was due to 8.7 percent surge in net domestic credit offsetting the decline in net foreign asset by 11.1 percent and the surge in other items net by 14.9 percent.

The stock of reserve money/high powered money grew by 19.5 percent on annual basis to reach Birr 67.9 billion at the close of December 2011. Both currency in circulation and commercial banks' reserve at NBE surged compared to same quarter last fiscal year. Quarter-on-quarter however, reserve money declined by 0.5 percent due to 12.4 percent slowdown in banks deposit at NBE offsetting the surge in currency in circulation currency by 8.6 percent. The money multiplier, measured by the ratio of broad money to reserve money, increased slightly from 2.1 end of December 2010 to 2.3 percent a year later indicating the improvement in monetization process during the year.

Interest rate

Following the NBE's policy action that raised the minimum saving deposit rate from 4.0 percent to 5.0 percent effective from December 1, 2010, all banks have adjusted their deposit and lending rates. As a result, the minimum and maximum saving deposit rates at the end of the quarter were 5.0 and 5.75 percent, respectively while the minimum and maximum lending rates stood at 7.5 and 16.25 percent unchanged from the previous quarter levels. Considering 33.2 percent annual average headline inflation I December 2011, average saving deposit rate (5.4 percent) and average lending rate (11.9 percent) were negative[1] in real terms.

Financial Sector Developments

The number of banks operating in the country was 17 at the end of December 2011, of which 14 banks are privately owned.

During the review quarter, 110 new bank branches were opened, thereby raising the total number of bank branches to 1126. As a result, the ratio of total bank branch to total population has increased to 71,048[*] from 78,740 in the preceding quarter, revealing an improvement in financial service outreach.

|The total number of insurance companies operating in the country remained unchanged at 14 during the review quarter, of which 13 were privately owned. The number of their branches, however, increased to 227 from 213 the same period last year. Similarly the total number of MFIs remained at 31 during the quarter.

The total capital of the banking system reached Birr 16.9 billion[2] at the close of December 2011, of which private banks together possesses 48 percent. Commercial Bank of Ethiopia, the biggest state owned bank, accounted for 36.9 percent of the total capital of the banking system, implying high but slowly declining concentration in market share.

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[1] Benefits the borrowers but disadvantageous to the depositors and in fact affects financial development negatively.
[*] Computed based on the assumption that total population was 80 million
[2] About 1 billion USD and yet very small to mention considering a huge potential that the country endowed with.

Total resources mobilized by the banking system (as measured by the sum of net change in deposit, loans collected and net change in borrowings) surged by 9.3 percent to Birr 20.4 billion at the end of the second quarter from Birr 18.6 billion in the preceding quarter due to the surge in net deposit and net borrowing by 52 and 40.7 percent respectively counterbalancing the decline in loans collection by 26.9 percent.

During the second quarter of 2011/12, total disbursement of fresh loans by commercial banks including DBE was Birr 13.5 billion, witnessing a surge of 16.5 and 14.4 percent against the new loans granted in the preceding quarter and the same quarter of last year, respectively. Public Banks disbursed Birr 7.3 billion (54.5 percent) whereas the balance was made by the private banks.

About 98 percent of the new loans granted by the private banks went to the private enterprise while 56.3 and 30.4 percent of the loans by public banks disbursed to private enterprises and state enterprises, respectively. This surely indicates that public banks role in supporting public enterprises is very vital as that of private banks to the private sector.

During the review quarter, the banking system collected Birr 7.2 billion, slowdown by 26.9 percent against the preceding quarter, but increased by 3.8 percent on vis-à-vis the same quarter last fiscal year. Of the total loan collection, private banks collected Birr 3.7 billion (52.1 percent) while public banks collected the remaining balance.

Total outstanding credit of the banking system (excluding credit to central government and bond issued by CBE) increased to Birr 89.4 billion at the end of December 2011, up by 32.8 and 21.4 percent against last year same quarter and the preceding quarter, respectively.

Total deposits mobilized by the banking system reached Birr 157.7 billion at the close of the second quarter of 2011/12, indicating a quarterly and annual surge of 7 and 38.2 percent, respectively. The growth in deposit mobilization was partially attributed to the increase in the number of bank branches and the improvements in economic activities.

Similarly, MFIs mobilized a total of saving deposit of Birr 4.3 billion, which was 41.1 percent higher than the amount mobilized last year same quarter.

External Sector and Foreign Exchange Developments

Export earnings from merchandise goods grew by 8 percent annualized in the second quarter of 2011/12 and amounted to USD 594.5 million. The puny growth of total exports was ascribed to the increase in export earnings largely from oilseeds, gold, leather & leather products, live animals, flower, meat & meat products and fruits & vegetables, driven mainly by expansion of export volumes and improvement of international prices.

Total merchandise import bills during the second quarter of 2011/12 amounted to USD 2.8 billion, up vigorously by 24.2 percent and 22.1 percent with respect to last year same period and the preceding quarter correspondingly. The performance of total imports in annualized term was attributed to the increases in imports of consumer goods, fuel, semi-finished goods and raw materials.

In the second quarter of 2011/12, the service account recorded USD 51.4 million net payments against USD 121 million and USD 121.8 million net service receipts last year same period and the preceding quarter respectively. The increase in total service payments year-on-year basis surpassed the rise in service receipts and resulting net service payment.

The total service receipts in the second quarter of 2011/12 increased by 15.8 percent with respect to the same period last year mainly due to higher receipts from transport (33.8 percent) and travel (11 percent) services. The receipts, however, fell marginally compared to the preceding quarter mainly due to lower receipt from government service.

The current account balance (including official transfers) registered 946 million deficits during the second quarter of 2011/12 compared to a relatively marginal deficit of USD 13 million last year same period and USD 58 million in the preceding quarter; owing to trade deficit widening, net service payments and a significant reduction in official transfers.

In the review quarter, the average official exchange rate of the Birr weakened by 1 and 4.2 percent with respect to the previous quarter and last year same period, respectively, to reach Birr 17.1522/USD.

Meanwhile, the parallel average exchange rate stood at Birr 17.8333/USD, illustrating a 2.5 and 5.2 percent depreciation on quarter-to-quarter and annualized basis respectively. As a result, the average premium between the official and parallel market rates widened to 4 percent from 2.3 and 3 percent, respectively.

Federal Government Fiscal Operations

During the second quarter of 2011/12, total revenue and grant mobilized by the federal government surged by 4.1 percent on quarterly basis to Birr 21.6 billion. Year-on-year basis, it scaled up by 40.1 percent. The quarterly revenue and grant performance was 24.1 percent of the annual plan of fiscal year 2011/12.

Total Federal Government expenditures (including regional transfers) was Birr 26.4 billion, revealing annual and quarterly surge of 50.9 and 33.5 percent, respectively. The Federal Government budget (including grant) depicted an overall deficit of Birr 4.7 billion unlike a surplus of Birr 1.0 billion in the previous quarter. The quarterly deficit was remarkably higher relative to the deficit a year earlier, due to higher growth in expenditure which counterbalanced the surge in quarterly revenue and grant collection.

Investment

The Ethiopian Investment Agency (EIA) and the Regional Investment Offices licensed a total of 1,065 investment projects with an aggregate capital of Birr 32 billion during the second quarter of 2011/12. The number of approved investment projects was 25 percent higher compared to same quarter of last fiscal year albeit lower by about 12 percent against the preceding quarter. Similarly, the total registered capital of these projects grew by 164 percent annually, but declined by 2 percent on quarterly basis.