ETHIOPIA

Table 1	2020
Population, million	115.0
GDP, current US$ billion	107.4
GDP per capita, current US$	934.6
International poverty rate ($1.9)[a]	30.8
Lower middle-income poverty rate ($3.2)[a]	68.9
Upper middle-income poverty rate ($5.5)[a]	90.2
Gini index[a]	35.0
School enrollment, primary (% gross)[b]	90.0
Life expectancy at birth, years[c]	66.2

Source: WDI, Macro Poverty Outlook, and official data.
Notes:
(a) Most recent value (2015), 2011PPPs.
(b) Ethiopia LSMS (2018/19).
(c) Most recent WDI value (2018).

After a better-than-expected outturn in FY20, the economy is expected to slow down further in FY21. While employment levels have recovered, a quarter of households still reported reduced income in October, and firm revenue has been hit. Base money expansion has presumably helped ease liquidity constraints and fuel credit growth, but it may have also contributed to inflation, which reached 19.2 percent in January 2021. The Ethiopian economy would rebound in the medium term as macroeconomic and structural reforms are completed.

Key conditions and challenges

Ethiopia has been among the fastest growing countries in the world, with GDP expanding at an average rate of 10.3 percent during 2004-2019. Growth has been driven by large-scale public investment in infrastructure. While poverty declined by about 10 percentage points during 2004-2016, gains are modest when compared to other countries that saw fast growth, and there is evidence that rural dwellers and the poorest have not equally benefited from growth in recent years.

The limitations of the state-led development model in Ethiopia have become apparent. Structural transformation remains incipient, and the role of the private sector is constrained by SOE dominance and an uneven playing field. The financing of the large capital investments coupled with a loss in competitiveness, caused by an overvalued exchange rate, have put the country at high risk of debt distress. Acknowledging these shortcomings, the authorities launched a Homegrown Economic Reform Agenda in September 2019, which aims to foster efficiency and introduce competition in key growth-enabling sectors (energy, logistics, telecom), improve the business climate, and address macroeconomic imbalances. Among other measures, authorities are expected to adopt a market-determined exchange rate and introduce a modern monetary policy framework by end-2022.

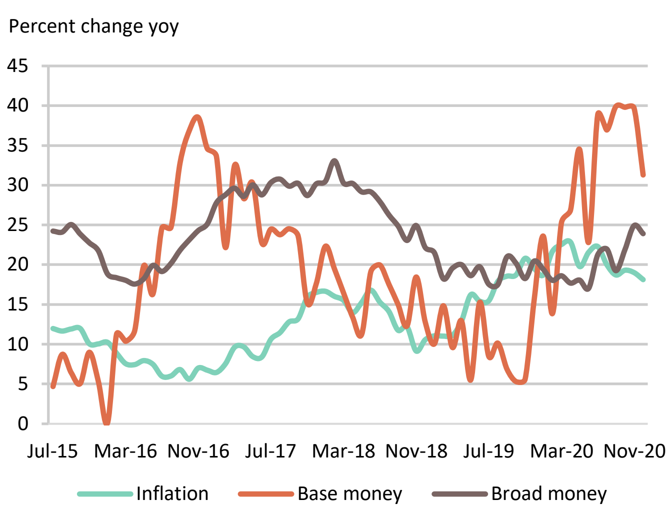
Ethiopia is facing formidable challenges. While the armed confrontation in the North of the country seems to have been geographically contained so far, risks of a protracted and more widespread conflict persist. The humanitarian situation is reported to be dire, with thousands of people displaced. The desert locust invasion could affect crops, threatening food security. And there is risk that poverty increases due to the COVID-19 impacts given the high levels of vulnerability to shocks.

Recent developments

Ethiopia grew at 6.1 percent in FY20, as the impact of the COVID-19 pandemic took place largely in the final quarter of the fiscal year. Crop production improved, while growth in services and manufacturing eased to single digits.

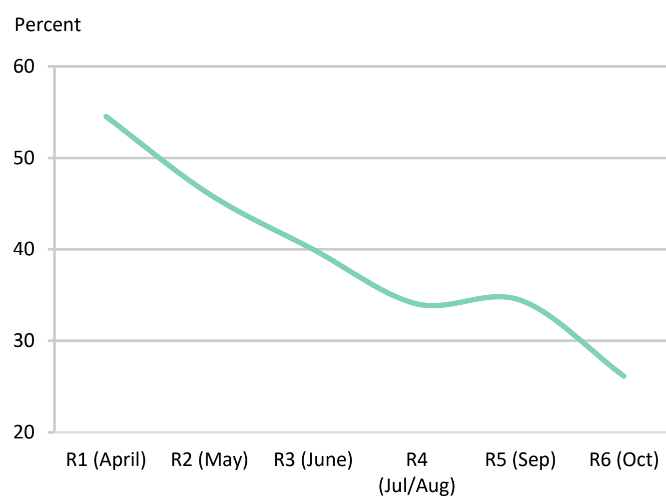
While external demand remains depressed due to COVID-19, it is showing some signs of recovery. Merchandise exports excluding gold declined by 4.1 percent during July-December 2020 (year-on-year), while most items (except garments) showed signs of recovery in the second quarter of the fiscal year. Including gold, merchandise exports grew at 21 percent. Exports of services (including air travel) dropped by 9.2 percent. An even sharper drop in imports, driven down by limits in SOE spending and currency depreciation has resulted in the narrowing of the current account balance. Remittances, which dropped by 10 percent in FY20, rebounded during the first half of FY21 (19.1 percent). Meanwhile, net

FIGURE 1 Ethiopia /Inflation and monetary aggregates



Source: National Bank of Ethiopia.

FIGURE 2 Ethiopia / Share of respondents who reported income reduction or loss.



Source: Wieser et al., 2020.

foreign direct investment remains depressed, dropping by 1.7 percent during the same period.

While healthcare spending increased significantly as part of the response to the pandemic, total expenditure dropped in FY20. Revenue collection deteriorated mainly due to the drop in indirect tax collections as demand has weakened. Overall, the general government deficit is estimated to have increased to 2.8 percent of GDP in FY20, compared to 2.5 percent of GDP in FY19.

Reserve money surged by 37 percent during July-December 2020 (year-on-year), and bank credit has continued to expand strongly (28.7 percent nominal growth, yoy). A 5 percent decrease in payment collection by commercial banks suggest some firms and households are struggling to repay their loans. Inflation, which had slightly eased in recent months, picked up again, reaching 19.2 percent in January, possibly pushed by seasonality factors and monetary expansion. Faster nominal depreciation resulted in a reduction in real overvaluation during the first half of FY21, although the still elevated parallel market premium suggest foreign exchange shortages persist.

The COVID-19 pandemic has had severe economic impacts, resulting from reduced employment and income. Employment rates plunged in the early days of the pandemic, with 8 percent of respondents losing their jobs by April 2020. While employment levels have recovered (except for some persistent job losses in urban areas), the situation faced by households remains challenging. According to the high frequency phone surveys, more than half of the households reported in April 2020 that their incomes were either reduced or had totally disappeared. While the proportion of those who reported reduction of income decreased in subsequent months, it remained high as of October 2020, at 26 percent.

Outlook

Growth is expected to decelerate further in FY21, to about 2 percent, impacted by reduced income reported by firms and households and a slowdown in crop production. Continued import compression and favorable terms of trade are expected to contain the current account deficit in FY21. The fiscal deficit is expected to reach about 3 percent of GDP in FY21, slightly above FY20 outturn. Inflation would remain elevated in FY21, while trending down in the medium term as a tighter macroeconomic stance is implemented once the pandemic abates. As key macroeconomic and structural reforms are fully implemented by 2022, foreign direct investment, exports, and economic growth are expected to strengthen in the medium term.

The effects of the COVID-19 pandemic on livelihoods are expected to be severe. Household incomes, as shown by the high -frequency phone surveys, are impacted through a reduction in aggregate demand that affects low-income households disproportionately. Results from the phone survey of firms show that Covid-19 and related containment measures have substantially impacted firms' operations. With formal firms not hiring, a reduction in aggregate demand will also affect the self-employed. Casual laborers and self-employed (44 percent of urban households) are hit particularly hard with an expected downturn of the economy. Moreover, reduced fiscal space will put pressure on the provision of social services during and after the economic downturn, potentially having detrimental long-term effects on the poor.

TABLE 2 Ethiopia / Macro poverty outlook indicators (annual percent change unless indicated otherwise)

	2017/18	2018/19	2019/20 e	2020/21 f	2021/22 f	2022/23 f
Real GDP growth, at constant market prices	7.7	9.0	6.1	2.3	6.0	7.5
Private Consumption	5.3	5.1	5.0	2.5	4.0	6.5
Government Consumption	3.6	7.2	0.6	17.6	9.0	14.0
Gross Fixed Capital Investment	6.8	12.4	6.3	-3.5	5.2	4.8
Exports, Goods and Services	5.0	3.0	-0.9	7.0	12.0	5.7
Imports, Goods and Services	0.2	0.6	-2.3	1.5	2.2	2.5
Real GDP growth, at constant factor prices	7.7	9.0	6.1	2.3	6.0	7.5
Agriculture	3.5	3.8	4.3	4.0	4.0	4.0
Industry	12.2	11.5	9.6	3.5	9.0	16.0
Services	8.7	12.0	5.2	0.1	5.5	4.1
Inflation (Consumer Price Index)	14.5	12.5	19.9	19.0	10.0	9.0
Current Account Balance (% of GDP)	-6.2	-5.1	-4.1	-3.3	-3.7	-3.7
Fiscal Balance (% of GDP)	-2.9	-2.5	-2.8	-3.2	-2.2	-1.9
Debt (% of GDP)	59.6	57.3	56.5	56.6	55.6	53.3
Primary Balance (% of GDP)	-2.4	-2.0	-2.3	-2.5	-1.5	-1.1
International poverty rate ($1.9 in 2011 PPP)[a,b]	27.6	26.5	25.9	25.9	25.4	24.6
Lower middle-income poverty rate ($3.2 in 2011 PPP)[a,b]	65.6	64.4	63.7	63.8	63.1	62.2
Upper middle-income poverty rate ($5.5 in 2011 PPP)[a,b]	85.8	84.2	83.4	83.4	82.6	81.4

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.
Notes: e = estimate. f = forecast.

(a) Calculations based on 2010-HICES and 2015-HICES. Actual data: 2015. Nowcast: 2016-2020. Forecast are from 2021 to 2023.

(b) Projection using point to point elasticity at regional level with pass-through = 0.87 based on GDP per capita in constant LCU.