

**FOR  
AGENDA**

MASTER FILES

ROOM C-120

D1

SM/85/151

CONTAINS CONFIDENTIAL  
INFORMATION

May 23, 1985

To: Members of the Executive Board

From: The Secretary

Subject: Ethiopia - Staff Report for the 1985 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1985 Article IV consultation with Ethiopia, which will be brought to the agenda for discussion on a date to be announced. A draft decision appears on page 22.

Mr. Jiménez (ext. 6952) or Mr. Scheuer (ext. 6940) are available to answer technical or factual questions relating to this paper prior to the Board discussion.

Att: (1)

Other Distribution:  
Department Heads

INTERNATIONAL MONETARY FUND

ETHIOPIA

Staff Report for the 1985 Article IV Consultation

Prepared by the Staff Representatives for the 1985 Consultation  
with Ethiopia

Approved by G.E. Gondwe and S. Kanesa-Thasan

May 22, 1985

I. Introduction

A staff mission visited Addis Ababa during the period March 19-April 2, 1985 to conduct the Article IV consultation discussions with Ethiopia. The Ethiopian representatives included Mr. Mersie Ejigu, Head of Macroplanning in the Office of the National Committee for Central Planning with the rank of Minister; Mr. Tadesse Gebre-Kidan, Governor of the National Bank of Ethiopia, Mr. Bekele Tamirat, Vice-Minister of Finance, and other officials dealing with economic and financial matters. The staff team consisted of Messrs. J.M. Jiménez (Head-AFR), D. Scheuer (AFR), J. Modi (FAD), W. Nahr (BUR), and Ms. A. Wood (Secretary-AFR). Mr. G. Gondwe (AFR) participated in the policy discussions.

Ethiopia continues to avail itself of the transitional arrangements of Article XIV. A summary of Ethiopia's relations with the Fund and a table of World Bank loans and IDA credits are shown in Attachments II and III respectively.

II. Background

1. Structural and institutional features of the economy

Since 1974 the Government has made great strides to institute a socialist system with a centrally planned economy. The Government has acquired ownership of all financial institutions, major industrial enterprises, and large sections of urban and rural property. The Government's influence on economic decisions is extensive. Production in the large agricultural sector remains principally within the private sector, being dominated by smallholders with user rights on state-owned land. Peasants in the rural area are organized into peasants' associations and some of these into service and producer cooperatives. State farms account for about 5 percent of the estimated value of agricultural output, though a much higher proportion of marketed output. They are expected to grow in importance over the medium term. The Government also has control over the marketing of foodstuffs, exports, and imports.

It operates a marketing, distribution, and a price support system for food grains, pulses, and oilseeds through the Agricultural Marketing Corporation (AMC), which according to the present guidelines handles about 50 percent of the marketed surplus, through the use of obligatory delivery quotas from cooperatives and wholesalers.

2. Medium-term retrospective

Between 1978/79 and 1979/80 the economy expanded by 5.6 percent per year. A strong improvement in Ethiopia's terms of trade in the late 1970s, in conjunction with several years of good weather conditions, the introduction of annual development campaigns, and a more stable environment promoted a rapid recovery of the industrial and agricultural sectors, generating an improved growth performance. In the early 1980s, with the gains from the recovery of industrial capacity utilization fully realized, and with a major deterioration in the terms of trade, the growth performance deteriorated. In the three years ending 1982/83 the terms of trade declined by about 12.7 percent, and growth fell to an average of 3.1 percent per year. At the same time, the current account deficit of the balance of payments increased.

During these years the overall government deficit was kept within manageable limits. Between fiscal years 1979/80 and 1981/82 the deficit averaged 4.8 percent of GDP, with the equivalent of 2.1 percent of GDP financed domestically. However, domestic credit rose by the equivalent of 15.8 percent of the initial broad money stock per year. About 40 percent of the total expansion <sup>1/</sup> was taken up by the public enterprises, with credit to the private sector remaining stagnant. An overall balance of payments deficit was recorded in all but one year of this period. The exception was 1981/82 when an exceptional loan was secured late in the fiscal year. Broad money expanded by an average of about 8.7 percent.

During this period, prices rose by 7.1 percent per year, largely reflecting improved supply conditions, price controls, an appreciation of the birr, and a rise in imports exceeding the growth of nominal income. The Government maintained a cautious incomes policy during this period.

3. The current drought

The failure of the main 1984 harvest in particular created a significant food shortfall, estimated to affect about 8 - 10 million people or almost one quarter of Ethiopia's population. Accumulated grain stocks from a good crop in 1982/83 provided the basis for initial

---

<sup>1/</sup> Including bank credit to nonbanks, which was relent to public enterprises.

relief efforts, but nowhere in the quantities necessary. The main shortfall in grain production was accounted for by the disappointing outturn in the principle grain producing areas in the center of the country where grain surpluses are usually produced. The areas in the north of the country have been the hardest hit in terms of human suffering. These areas have suffered from shortages on a recurrent basis, and are characterized by a low per capita caloric intake, with a vast proportion of the population living in extremely precarious conditions. Shortages have resulted in price increases, which have hastened the rundown of the limited savings of the people, who have also disposed of most of their capital equipment, including seed, draft animals, and other livestock. Only after they have run down all their available resources, have the people in this area abandoned the land and sought assistance at the relief camps.

Ethiopia's relative underdevelopment has been a great impediment to the relief effort. The lack of roads and an inadequate truck fleet has multiplied the cost of relief and limited the flow of relief supplies. The weakened state of the people has hastened the spread of disease in the camps and added to the human toll.

The magnitude of the relief effort, valuation difficulties, and the large number of aid participants has made it impossible for comprehensive statements of assistance to be drawn up. For fiscal year 1984/85, the authorities estimate imports of cereal and other foodstuffs at 1.1 million metric tons. These quantities, apparently, will fall short of the estimated requirement of about 1.5 million metric tons. About 740 trucks are expected, plus about 257,000 metric tons of other goods, such as medicines, blankets, and tents. On the basis of available information, the staff has estimated the value of secured and unsecured pledged resources at about US\$640 million, of which almost US\$200 million corresponds to the inland transportation and distribution costs. The C & F cost of the foodstuffs is estimated at about US\$300 million. Thus, an important proportion of the cost of the relief effort is accounted for by capital equipment and transport. The Ethiopian authorities, however, believe that the donor cost estimates are inflated.

The Government meanwhile has been giving a high priority to the resettlement of the affected population. The authorities are aiming to resettle more than 300,000 people in the current year; thereby meeting in one year the targets set under the 10-Year Perspective Plan for the period through 1993/94.

Even under the assumption of adequate rains in the current year, donors estimate that 346,000 metric tons of grains and 73,000 metric tons of other supplies will be required in fiscal year 1985/86. Together with transport costs and ancillary capital equipment, the relief effort is projected at about US\$240 million in that year.

### III. Recent Economic Developments

In the two years since 1982/83 the rate of growth has turned negative reflecting the impact of drought. In 1983/84 real GDP fell by 1.1 percent, with agricultural sector value added declining by 8.1 percent (Table 1). Apart from foodstuffs, production of some industrial products and livestock were also affected. The growth trend was also influenced by a major reduction in government outlays. In 1984/85 the economy is expected to contract further by 7.0 percent, with agricultural sector output registering an estimated reduction of 16.0 percent. However, the relief activity is projected to bolster the transportation and government sectors. Under normal weather conditions, GDP could expand by about 10 percent in 1985/86 (relative to the depressed 1984/85 level), led by a possible 19.0 percent growth in agricultural sector value added.

The shortages related to the drought are projected to increase prices by about 16 percent in 1984/85, compared with 3.9 percent in 1982/83 and a reduction of 0.3 percent in 1983/84. This assumes a major slowdown in the price increases in the second half of the fiscal year with the improvement of supplies, as the annual rate of increase recorded in the first half reached 30 percent.

For many years Ethiopia has suffered from important internal and external imbalances. These have grown in intensity in the present decade. The current account deficit in the balance of payments has shown a rising trend, while almost continuous overall deficits have been recorded since 1976/77 (Table 2). Export earnings in local currency terms were 5 percent lower in 1983/84 than in 1979/80, in part reflecting a decline in the terms of trade, but also an inability to increase the volume of nontraditional exports. Ethiopia's exports are estimated to fall by a further 14 percent in 1984/85, partly as a result of the drought. The current account deficit has been financed by a rising debt and a drawdown of foreign reserves. There has been a continuous erosion of the country's net foreign assets and these are expected to become and remain negative by mid-1985. Gross official reserves are estimated at one-week's imports at the end of 1984/85.

The real appreciation of the birr has accelerated recently. At the current exchange rate, many nontraditional exports are not profitable and adequate producer prices cannot be fixed for export products.

In the two years ending with 1983/84 domestic credit grew by the equivalent of 17.5 percent of the initial stock of broad money per year. In 1982/83 the high growth of domestic credit was largely the result of a more than doubling of the overall budgetary deficit to 13.1 percent of GDP, which raised the level of domestic financing to the equivalent of 8.6 percent of GDP compared with an average of under 2 percent in the previous two fiscal years (Table 3). About

Table 1. Ethiopia: Selected Economic and Financial Indicators, 1977/78-1984/85

(Fiscal year ending July 7)

	1977/78- 1979/80 Average	1980/81	1981/82	1982/83	1983/84	1984/85 Prov.
	(Annual percentage change, unless otherwise specified)					
National income and prices						
GDP at constant prices	3.2	2.2	1.5	5.1	-1.1	-7.0
GDP deflator	4.3	2.1	1.4	3.9	1.5	7.1
Consumer prices	14.7	1.9	7.3	3.9	-0.3	16.1
External sector (in terms of SDRs)						
Exports, f.o.b.	16.1	-10.1	3.1	7.0	18.3	-8.9
Coffee	(6.6)	(-14.1)	(0.6)	(9.5)	(22.4)	(-20.1)
Noncoffee	(42.7)	(-2.9)	(7.1)	(3.2)	(11.9)	(11.2)
Imports, c.i.f.	9.7	5.1	22.6	6.0	23.7	26.6
Imports (excluding commodity aid)	9.7	6.5	24.6	6.0	21.7	17.0
Nonpetroleum imports	2.4	4.8	27.9	3.5	30.9	28.6
Export volume	13.4	1.9	-3.1	5.6	10.5	-20.7
Import volume	-0.2	-0.2	16.2	8.0	22.5	21.4
Import volume (excluding commodity aid)	-0.2	1.1	18.1	8.0	20.6	-20.4
Terms of trade (deterioration -)	-8.0	-16.1	0.8	3.2	9.7	16.8
Nominal effective exchange rate (depreciation -)	-4.2	8.8	17.2	11.7	11.5	14.7
Real effective exchange rate (depreciation -)	-0.5	-2.9	12.9	5.5	1.6	19.6
Government budget						
Revenue (excluding grants)	15.5	12.6	5.2	10.7	8.3	6.4
Revenue (excluding grants and drought relief)	...	...	...	...	...	0.1
Total expenditure	17.5	8.0	16.6	39.3	-12.8	7.3
Total expenditure (excluding drought relief)	...	...	...	...	...	-0.2
Money and credit						
Domestic credit 1/	29.1	9.3	12.4	22.6	14.2	16.2
Credit to Government 1/	(10.4)	(6.0)	(3.1)	(30.3)	(10.3)	(14.9)
Money and quasi-money	11.8	2.0	11.2	15.0	11.3	10.5
	(In percent of GDP)					
Current budgetary surplus	-0.4	1.1	0.3	-2.4	1.4	-0.1
Overall fiscal deficit (-)						
Including public grants	-4.5	-3.7	-6.2	-13.1	-6.2	-8.7
Excluding public grants	-5.2	-5.9	-7.3	-14.5	-8.3	-11.9
Excluding drought relief and grants	...	...	...	...	...	-11.8
Foreign financing	1.6	1.4	5.2	4.5	2.6	3.4
Domestic bank financing	2.5	1.6	0.7	8.3	3.3	5.0
Gross domestic investment	8.7	11.6	13.2	11.2	12.8	10.8
Gross domestic saving	3.4	4.2	3.6	2.7	1.6	-8.1
Current account deficit (-)						
Including public transfers	-3.4	-5.5	-7.1	-5.4	-5.6	-4.7
Excluding public transfers	-4.9	-6.8	-8.7	-7.3	-9.4	-16.3
Excluding public transfers, private transfers, and commodity aid	-5.4	-6.9	-9.4	-8.5	-10.1	-7.0
External debt (inclusive of use of Fund credit)	15.5	19.9	25.6	27.6	31.6	35.3
Debt service ratio 2/	6.5	7.1	12.9	16.2	16.1	37.1
Interest payments 2/	2.8	3.1	6.7	7.1	5.6	9.5
	(In millions of SDRs, unless otherwise specified)					
Overall balance of payments	-57.2	-47.5	53.2	-65.9	-40.3	-54.0
Gross official reserves (weeks of imports) 3/	12.4	9.7	16.3	13.0	5.4	1.0

1/ Changes expressed in percent of M2 at the beginning of the year.

2/ Expressed in percent of exports of goods and nonfactor services.

3/ Reserves at June 30 in weeks of fiscal year imports.

Table 2. Ethiopia: Balance of Payments, 1979/80-1984/85

Fiscal year <u>1/</u>	1979/80	1980/81	1981/82	1982/83	1983/84	1984/85 <u>2/</u>
(In millions of birr)						
Trade balance	-578.0	-731.7	-961.2	-962.4	-1,195.7	-1,725.9
Exports	981.8 <u>3/</u>	852.7	795.4	810.5	930.1	796.0
Imports	-1,559.8	-1,584.4	-1,756.6	-1,772.9	-2,125.8 <u>4/</u>	-2,521.9
Regular imports	(-1,422.9)	(-1,517.4)	(-1,716.8)	(-1,734.5)	(-2,046.9)	(-1,491.2)
Grains & commodity aid	(-136.9)	(-67.0)	(-39.8)	(-38.4)	(-78.9)	(-1,030.7) <u>5/</u>
Net services	55.1	70.3	60.2	85.9	87.1	-308.8
Of which:						
Emergency relief services	...	...	...	...	-24.9	-411.6 <u>5/</u>
Private transfers (net)	41.3	51.2	93.6	175.8	222.0	400.0
Current account balance	-481.6	-610.2	-807.4	-700.7	-886.6	-1,634.7
Public transfers (net) <u>6/</u>	124.0	123.9	139.8	191.4	335.2	1,159.7 <u>7/</u>
Nonmonetary capital	280.9	322.0	679.4	401.7	445.1	365.0
Public long term	310.6	334.5	640.2	421.4	422.5	350.0 <u>8/</u>
Short term	-29.7	-12.5	39.2	-19.7	22.6	15.0
Errors and omissions	-16.9	-27.8	68.9	-40.4	18.7	--
SDR allocation	10.0	10.0	9.7	--	--	--
Revaluation of reserves	--	58.5 <u>9/</u>	34.9	--	--	--
Overall balance	-83.6	-123.6	125.3	-148.0	-87.6	-110.0
Net monetary movements <u>10/</u>	83.6	123.6	-125.3	148.0	87.6	110.0
(In percent of GDP)						
Exports	11.5	9.6	8.7	8.1	9.3	7.9
Imports including drought relief	18.3	17.8	19.2	17.7	21.1	25.1
Imports excluding drought relief	17.5	17.2	18.9	17.5	20.5	16.0
Current account	-5.6	-6.8	-8.8	-7.0	-8.8	-16.3
Incl. pub. transfers	-4.2	-5.5	-7.3	-5.1	-5.5	-4.7
Excl. assist. and priv. transfers	5.5	-6.9	-9.4	-8.5	-10.1	-7.0
Gross capital inflow	4.0	4.3	7.7	5.2	5.5	6.0
Gross capital plus official transfers (excl. emergency relief)	5.4	5.7	9.2	7.1	8.3	7.2
Reserves in weeks of imports	10.8	9.7	16.3	13.0	5.4	1.0
Transfers plus capital (net; in birr per capita)	14	15	24	23	29	20

Sources: National Bank of Ethiopia; Ministry of Finance; Office of the National Council for Central Planning (ONCCP); and staff estimates.

1/ Data cover year ended July 7, where available, otherwise June 30.

2/ Revised provisional data.

3/ Includes Br 26.7 million from the sale of nonmonetary gold.

4/ Including one aeroplane not included in customs data.

5/ Estimate based on UN Relief Assistance Representative and OECD Development Assistance Committee data.

6/ Excludes technical assistance and similar transfers recorded in government budget.

7/ Based on information from major donors.

8/ Other public sector borrowing Br 10 million.

9/ A profit of Br 48.8 million from the sale of 48,430 ounces of nonmonetary gold plus a revaluation gain of Br 9.7 million.

10/ Increase in net assets denoted by minus sign.

Table 3. Ethiopia: Summary of Government Finance, 1979/80-1984/85

(In millions of birr)

Fiscal Year Ending July 7	Actual	Preliminary Actual				Budget	Official Est.	Staff Est.
	1979/80	1980/81	1981/82	1982/83	1983/84	1984/85	1984/85	1984/85
Revenue and grants	1,623.0	1,826.1	1,945.0	2,189.0	2,437.0	2,709.1	2,540.0	2,668.0
Revenue	(1,567.5)	(1,756.9)	(1,848.0)	(2,046.6)	(2,217.4)	(2,401.1)	(2,260.0) <u>1/</u>	(2,360.0) <u>1/</u>
Grants	(55.5)	(69.2)	(97.0)	(143.3)	(219.4)	(308.0)	(280.0)	(308.0)
Expenditure and equity investment	2,003.5	2,160.4	2,518.0	3,507.1	3,057.0	3,948.3	(3,280.0) <u>2/</u>	3,543.0 <u>2/</u>
Current expenditure	(1,560.3)	(1,655.3)	(1,816.4)	(2,290.6)	(2,075.9)	(2,364.5)	(2,365.0)	(2,365.0)
Of which: arrears payment	--	--	--	343.7	59.1	...	...	...
Capital expenditure	(443.2)	(505.1)	(701.6)	(972.6)	(963.1)	(1,583.8)	(915.0)	(1,178.0)
Equity investment <u>3/</u>	(--)	(--)	(--)	(243.9)	(18.0)	(...)	(...)	(...)
Overall deficit	-383.5	-334.3	-573.0	-1,317.2	-620.0	-1,239.2	-740.0	-875.0
Including grants	142.3	128.0	477.8	450.7	264.6	498.7	340.0	340.0
External financing (net)	(158.3)	(142.9)	(495.8)	(472.2)	(293.7)	(553.5)	(445.5)	(445.5)
Gross borrowing	(-16.0)	(-14.9)	(-18.0)	(-21.6)	(-29.1)	(54.8)	(105.0)	(105.0)
Less: amortization	241.2	206.3	95.2	866.5	355.4	740.5	400.0	535.0
Domestic financing	(199.3)	(142.0)	(62.2)	(829.4)	(336.5)	(508.5)	(370.0)	(505.0)
Bank	(16.2)	(50.0)	(26.0)	(19.0)	(25.0)	(...)	(30.0)	(30.0)
Nonbank	(25.7)	(14.3)	(7.0)	(18.1)	(-6.1)	(232.0) <u>4/</u>	(--)	(--)
Residual								
Memorandum items:	(Ratios to GDP)							
Revenue and grants	19.0	20.5	21.3	21.9	24.2	27.0	25.3	26.7
Of which: revenue	(18.4)	(19.7)	(20.2)	(20.4)	(21.1)	(24.0)	(22.6)	(23.6)
Total expenditure and equity investment	23.5	24.2	27.5	35.0	30.4	39.4	32.7	35.4
Current expenditure	(18.3)	(18.5)	(19.8)	(22.9)	(20.6)	(23.6)	(23.6)	(23.6)
Capital expenditure	(5.2)	(5.7)	(7.7)	(12.1)	(9.8)	(15.8)	(9.1)	(11.8)
Overall deficit (including grants)	-4.5	-3.7	-6.2	-13.1 <u>5/</u>	-6.2 <u>5/</u>	-12.4	-7.4	-8.7
Foreign financing	1.7	1.4	5.2	4.5	2.6	5.0	3.4	3.4
Domestic financing	2.8	2.4	1.0	8.6	3.6	7.4	4.0	5.3

Sources: Data supplied by the Ethiopian authorities and staff estimates.

1/ Of which the drought-relief levy is estimated to amount to Br 100 million as per official estimate and Br 140 million as per staff estimate.

2/ Of which the drought-related expenditure is estimated to amount to Br 230 million.

3/ Relates to additional capital injected into a number of public enterprises.

4/ Most of this amount was expected to be raised by additional revenue measures during the year.

5/ 7.3 percent without clearance of arrears and payment of additional equity in 1982/83 and 5.4 percent in 1983/84.



5 percentage points of the deficit in that year resulted from capital subscriptions and the payment of arrears to public enterprises. Despite the large nonrecurrent element in the budgetary deficit, the underlying deficit, at 8 percent of GDP, was still considerably in excess of the average of 5 percent recorded in the two previous fiscal years. The large transfer of resources from the budget to the public enterprises allowed them to reduce their own liabilities to the banking system by the equivalent of almost 8 percent of the initial broad money stock, thereby offsetting to an important degree the overall expansion of net credit to the budget. Broad money expanded by 15 percent during the year, compared with an average of 9 percent in the previous three years, with most of the increase occurring in narrow money (Table 4).

An important adjustment was carried out during fiscal year 1983/84. The overall deficit was reduced from the underlying level of 8 percent of GDP in 1982/83, to about 6 percent of GDP, largely reflecting a moderation in the growth of current expenditure (excluding payment of arrears), and the maintaining of capital expenditure virtually unchanged. However, net foreign financing was also sharply reduced and domestic financing was equivalent to almost 4 percent of GDP. While this was an improvement over the previous year, it was still about double the level recorded in 1980/81-1981/82.

The 1984/85 budget projected an overall deficit equivalent to 12.4 percent of GDP on the basis of an increase in overall expenditures of 29 percent (from about 30 percent of GDP to nearly 39 percent). Most of the increase was allocated to capital outlays. The budget foresaw domestic financing equivalent to more than 7 percent of GDP. In the course of the year, expenditure was scaled down, in part because of a shortfall in revenue, including Br 232 million that was anticipated from new (unspecified) revenue measures. Data for the first half of the year also revealed that revenues were falling significantly below the budgeted level as a result of the slowdown in the economy, and particularly the fall in nonrelief imports. Consequently, in March, the Government announced a drought relief levy on personal income and private enterprise turnover. For the remainder of the year, the levy is expected to yield the equivalent of 1.0 percent of GDP. Even with this levy, however, revenues are expected to fall short of the budgetary estimate, excluding the unfinanced gap that was expected to be met by new revenue measures, by about 0.4 percent of GDP. Overall expenditures have also been reduced by 10 percent, largely by a massive reduction in capital outlays; expenditure on projects and programs was reduced from 15.8 percent of GDP to 9.1 percent, and special outlays for drought relief, largely the resettlement scheme, equivalent to 2.3 percent of GDP, were added to the capital budget. The reduction in capital outlays has resulted in a slower utilization of available external financing. On the basis of half yearly data, the staff feels that these targets are underestimated and that the overall deficit is likely to reach almost 9 percent of GDP,

Table 4. Ethiopia: Monetary Survey, 1980-85

(In millions of birr)

	1980	1981	1982	June 1983	1984	1985 (Forecast)
Foreign assets (net)	<u>368.1</u>	<u>244.5</u>	<u>369.8</u>	<u>221.8</u>	<u>134.2</u>	<u>-15.8</u>
Domestic credit	<u>2,612.3</u>	<u>2,829.7</u>	<u>3,125.1</u>	<u>3,722.5</u>	<u>4,155.3</u>	<u>4,704.2</u>
Claims on Government (net)	<u>968.1</u>	<u>1,107.9</u>	<u>1,180.8</u>	<u>1,980.9</u>	<u>2,293.4</u>	<u>2,798.4</u>
Claims on other sectors	<u>1,644.2</u>	<u>1,721.8</u>	<u>1,944.3</u>	<u>1,741.7</u>	<u>1,861.9</u>	<u>1,905.8</u>
Long-term foreign liabilities	<u>-17.3</u>	<u>-15.2</u>	<u>-13.0</u>	<u>-10.8</u>	<u>-8.7</u>	<u>-6.6</u>
Other assets (net)	<u>-631.0</u>	<u>-681.4</u>	<u>-838.2</u>	<u>-893.0</u>	<u>-897.1</u>	<u>-943.0</u>
Broad money	<u>2,332.1</u>	<u>2,377.6</u>	<u>2,643.7</u>	<u>3,040.5</u>	<u>3,383.7</u>	<u>3,738.8</u>
Money	<u>1,722.0</u>	<u>1,715.3</u>	<u>1,892.2</u>	<u>2,180.4</u>	<u>2,379.3</u>	<u>...</u>
Quasi-money	<u>610.1</u>	<u>662.3</u>	<u>751.5</u>	<u>860.1</u>	<u>1,004.4</u>	<u>...</u>
(Changes in percent beginning period money stock)						
Foreign assets (net)	<u>-4.1</u>	<u>-5.3</u>	<u>5.3</u>	<u>-5.6</u>	<u>-2.9</u>	<u>-4.4</u>
Domestic credit	<u>25.6</u>	<u>9.3</u>	<u>12.4</u>	<u>22.6</u>	<u>14.2</u>	<u>16.2</u>
Claims on Government (net)	<u>5.1</u>	<u>6.0</u>	<u>3.1</u>	<u>30.3</u>	<u>10.3</u>	<u>14.9</u>
Claims on other sectors	<u>20.5</u>	<u>3.3</u>	<u>9.3</u>	<u>-7.7</u>	<u>2.9</u>	<u>1.3</u>
Long-term foreign liabilities	<u>0.1</u>	<u>0.1</u>	<u>0.1</u>	<u>0.1</u>	<u>0.1</u>	<u>0.1</u>
Other assets (net)	<u>-8.6</u>	<u>-2.1</u>	<u>-6.6</u>	<u>-2.1</u>	<u>-0.1</u>	<u>-1.4</u>
Broad money	<u>13.0</u>	<u>2.0</u>	<u>11.2</u>	<u>15.0</u>	<u>11.3</u>	<u>10.5</u>
Money	<u>8.0</u>	<u>-0.3</u>	<u>7.4</u>	<u>10.9</u>	<u>6.5</u>	<u>...</u>
Quasi-money	<u>5.0</u>	<u>2.3</u>	<u>3.8</u>	<u>4.1</u>	<u>4.8</u>	<u>...</u>

Sources: National Bank of Ethiopia; IMF Data Fund; and staff estimates.

with domestic financing of over 5 percent of GDP. Total revenue is underestimated by 4.4 percent, and total expenditure by about 8 percent. The underestimation of revenue arises mainly from import duties and the surtax on coffee, which, on the basis of projected levels of imports and exports, should be somewhat higher, and from staff estimates of the yield from the special relief levy. The underestimation of expenditure arises from the momentum of capital and drought relief expenditure already undertaken in the first half of the year. The Ethiopian authorities project the overall deficit at about 7 percent of GDP, and domestic financing at 4 percent of GDP.

Credit to the public enterprises is expected to rise by less than half the rate recorded in 1983/84. The lower resort to bank borrowing is the result of increased liquidity arising from the Government's policy of forcing public enterprises to reduce their inventories. Despite the reduced demand for credit by public enterprises, on the basis of the current trends in the budget, overall net domestic credit from the banking system could rise in excess of 16 percent of the initial money stock in fiscal year 1984/85, largely as a result of an almost 15 percent rise in net credit to the Government similarly measured. Broad money could rise by 10.5 percent. However, if the authorities succeed in limiting the deficit to their projected level of 7 percent of GDP, the overall credit expansion would amount to 12.2 percent, and the increase in broad money to 7.0 percent.

The large number of public enterprises are clustered into a smaller number of corporations, which in turn report to certain ministries, mainly Industries, Energy, Construction, Transport, and Agriculture. Although enterprises are required to report to their supervising ministry on a regular basis, and the ministry in turn reports to the Office of the the National Committee for Central Planning (ONCCP), financial data on public enterprises have not been consolidated. Available information, reflecting only the enterprises supervised by the Ministry of Industries, indicate that the profitability of these enterprises has declined from an average of about 13 percent of sales in 1978/79-1979/80 to about 5 percent in 1982/83-1983/84.

Ethiopia's external debt in relation to GDP has been rising rapidly, from an estimated 20 percent at the end of fiscal year 1980/81 to a projected almost 35 percent in 1984/85 (Table 5). The debt service ratio is estimated to more than double in the latter year when it reaches over 37 percent compared with an average of about 16 percent in the previous two fiscal years. On the basis of the projected current account deficits and known undisbursed balances, but excluding the projected unfinanced gap over the next three years, the debt service ratio is expected to peak in 1985/86 at about 41 percent, and to fall to about 30 percent in 1987/88.

Table 5. Ethiopia: External Public Debt Service, 1979/80-1987/88

Fiscal Year Ending July 7	Prin- cipal <u>1/</u>	Inter- est <u>2/</u>	Total	Receipts From Goods and Non- factor Services	Debt Service Ratio (Percent)	Outstanding Debt in Relation to GDP
(In millions of birr)						
1979/80	39.7	30.7	70.4	1,209.6	5.8	18.1
1980/81	45.6	36.3	81.9	1,148.4	7.1	19.9
1981/82	67.4	72.2	139.6	1,076.4	12.9	25.6
1982/83	103.0	81.6	184.6	1,142.0	16.2	27.6
1983/84	134.1	70.3	204.4	1,266.6	16.1	31.7
(Projections) <u>3/</u>						
1984/85	317.9	110.1	428.0	1,154.8	37.1	35.3
1985/86	358.0	124.8	482.8	1,266.3	38.1	...
1986/87	335.0	139.2	474.2	1,317.0	36.0	...
1987/88	261.0	155.6	416.6	1,411.1	29.5	...

Sources: Ministry of Finance data; and staff estimates.

1/ Includes repayments of Trust Fund loans.

2/ Includes IMF interest and charges.

3/ Based on present debt and expected gross drawings.

The Ethiopian birr has been pegged at birr 2.07 = US\$1 since 1973. This policy has led to a major appreciation of the birr. Between 1980 and 1983, this resulted in a real appreciation of 23 percent against a tradeweighted basket of currencies (Chart 1). In this period, the nominal appreciation of the birr reached 38 percent, and the lower appreciation of the real exchange rate reflects a lower inflation in Ethiopia than in the main trading partners. However, in 1984, prices in Ethiopia increased much faster and a real appreciation of 29 percent is estimated for that year, bringing the real appreciation since 1980 to over 50 percent.

Since 1978, Ethiopia has maintained a comprehensive system of import controls involving exchange restrictions. The tightening of controls at that time was a response to balance of payments pressures and largely done through administrative procedure. However, the authorities have administered the system in a flexible manner with regard to essential imports according to foreign exchange availabilities. Payments for invisibles and outward capital movements are also restricted. The authorities have avoided the incurrence of payments arrears.

#### IV. Report on the Discussions

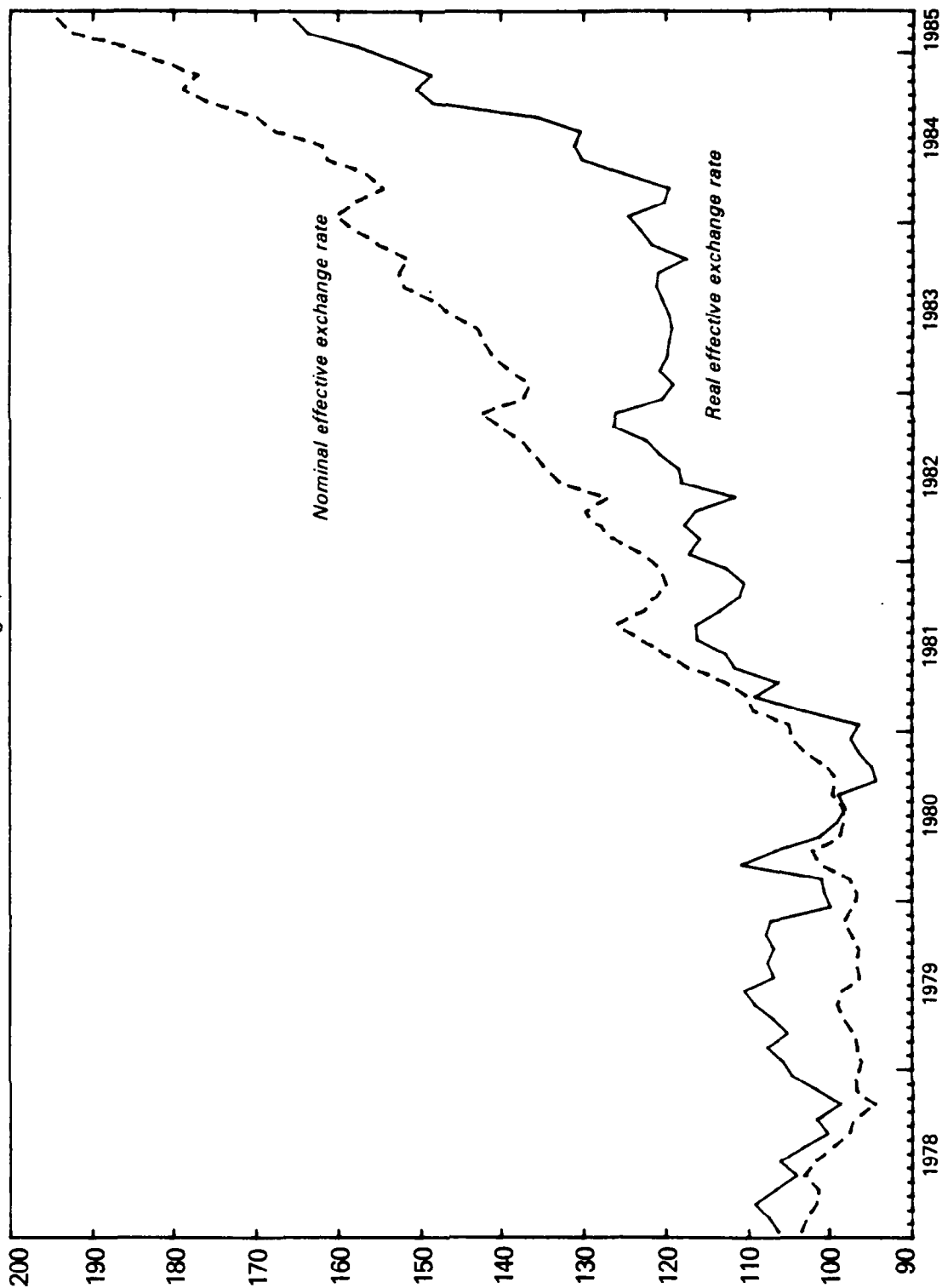
The consultation discussions were held at a time when the Ethiopian authorities were facing a most critical and difficult period. As has been detailed in an earlier section, the impact of the drought has been significant and the future outlook is clouded by continued uncertainties with respect to the weather. The assistance derived from the rest of the world has been substantial. The foreign exchange needs and many domestic costs are largely being met from foreign private and official grants. The Government is spending an important amount of its own resources domestically for grain distribution and the resettlement program, which it views as an important long-term solution to the crisis.

After many years of balance of payments deficits, Ethiopia's official reserves are projected to fall to about one week's imports during 1985. The external debt service burden has also reached a high level. This will be the culmination of internal and external imbalances which have been unattended for a long period of time. The need for a policy package to deal with these problems provided the main focus of the discussions.

##### 1. Resource allocation and production policies

The Ethiopian representatives feel that the economy has faced many structural disadvantages and has operated in an extremely unfavorable international environment over a number of years. Ethiopia remains one of the least developed countries in Africa, with a per capita income of only SDR 117, with limited infrastructure, and with recurring droughts.

CHART  
ETHIOPIA  
REAL AND NOMINAL EFFECTIVE EXCHANGE RATES, JAN. 1978-MAR. 1985  
(Period averages; 1980=100)



Source: IMF, *International Financial Statistics*, and staff estimates.



Ethiopia's low savings rate reflects the present level of development and is a major hindrance to more rapid growth. The Ethiopian representatives felt that the country had not received adequate support from the international community in supplementing its savings capacity, with the exception of the aid received during the present drought crisis. The representatives were concerned, that despite a major effort by the Government, a higher growth rate had not been attainable in the recent past. Government policy has been focused on resolving this issue.

The Ethiopian representatives said that objectives of the Government included raising the standard of living of the population, while achieving a sustained growth in productive capacity through a substantial increase in the rate of savings and investment. They stated that these objectives were to be attained through a socialist model of development which, in their view, was the best strategy for the country. The Ethiopian representatives explained that, in order to attain these objectives, a 10-Year Perspective Plan had been prepared for implementation beginning with fiscal year 1984/85. The Plan itself has been divided into shorter periods thereby permitting adjustments and revisions as necessary. Among the specific targets of the Plan are a 6.5 percent average annual growth rate, a savings rate of 15 percent of GDP by the end of the Plan period, with an expected investment rate of about 24 percent of GDP, the attainment of food self-sufficiency by the end of the Plan with food stocks equivalent to at least 3 month's consumption, implying an annual growth rate of 6 percent in food output. The Plan gives priority to projects based on domestic raw materials and with strong backward linkages.

The Ethiopian representatives said that although the implementation of the Plan had been affected by the onset of the drought, the Government would not be revising the objectives. Consequently, there would be a need for catching up later in the plan period, if the original plan targets were to be met.

The Ethiopian representatives stated that, in order to meet the present emergency, a "drought action plan" had been formulated for which international assistance had been sought. The drought had underscored the need for the Government to focus on development issues. In the view of the Ethiopian authorities, per capita aid flows to Ethiopia have been low in the past, and there is a strong case for increasing concessional aid flows on the grounds of both equity and a demonstrated capacity for efficient utilization.

The immediate outlook was heavily affected by the drought and the possibility of continued inadequate rainfall. Assuming that the rains were adequate in the rest of 1985, the Ethiopian representatives felt that there would be a major recovery in the agricultural sector, which would push GDP growth to a high level. In their view, the improved



agricultural position would also significantly reduce inflationary pressures, helping to increase activity in the other sectors, and to reduce some of the pressures on the balance of payments and on the budget, through increased exports and higher revenue collections.

The staff representatives, while recognizing the laudable nature of the Plan's objectives and the dedication of the authorities to its implementation, wondered whether the Plan was consistent with the present reality, and if it was comprehensive enough in its policy content to reach its objectives. For example, savings have traditionally been less than 5 percent of GDP, and in 1984/85 they were negative. Unless specific policies were to be implemented, it was difficult to see how the savings ratio would grow to 15 percent of GDP. It was also problematical whether the resource gap, projected at 9 percent of GDP by the end of the plan period, could be financed. It appeared to the staff representatives that policies were needed to reduce the resource gap. They recalled that the World Bank had reviewed the Plan late in 1984. While the Bank had endorsed the Plan's priorities, it had also suggested that the size of the Plan was overambitious and beyond available resources. The Ethiopian representatives expressed optimism that the savings rate would rise as expected and that the resource gap could be filled with increased concessional assistance. In this regard, they were hopeful that foreign donors, who had responded to the emergency, would continue with a high level of assistance for development purposes, as this was the key in avoiding other drought emergencies. With respect to the debt servicing capacity, the Ethiopian representatives said that what was important was the productive uses to which the borrowed resources were put and not any absolute ratio. In this regard they felt Ethiopia's record was exemplary. Moreover, they stressed that the Government had tried to avoid commercial indebtedness. The authorities believe that the outlook for increasing agricultural output is good, as the productivity in this sector is low and the adoption of better agricultural practices would yield significant results. Thus, emphasis is being placed on the increased use of fertilizer and on extension services. The authorities recognize that the immediate revival of the sector will be hampered by the lack of seeds and draft animals in the drought-afflicted areas, and a special program, financed by donors, has been established to provide seeds in these areas. Consequently, the main thrust of economic policy will be to promote a quick recovery of output. It was noted by the staff representatives that real producer prices have declined over a number of years and that these may retard the recovery of output. The Ethiopian representatives responded that prices are kept under continuous review.

## 2. Pricing policies

The Ethiopian representatives said that the recent acceleration in inflation was mainly tied to the shortages arising from the current

drought. The relief efforts had not been sufficient to maintain the level of supply, particularly in urban areas. They noted that, prior to the drought, prices had been kept relatively stable for a number of years. Consequently, it was their view that, as soon as the supply of foodstuffs was normalized, the inflation rate would fall rapidly to its previous level. They pointed out that price stability was helped by a restrained wage policy, while the appreciation of the exchange rate had helped to maintain import prices stable.

The Ethiopian representatives explained that a system of price controls over essential commodities was maintained. The aim was to promote reasonable prices and an adequate supply. Until the recent shortages, there were no parallel markets for essential commodities. The pricing decisions for the state corporations were made by the ONCCP, on the basis of recommendations from the ministries overseeing the individual enterprises. The Ethiopian representatives pointed out that, although there are a series of controlled prices, the Addis Ababa price index is an adequate proxy for price developments, as it in effect measures prices in the market place.

The Ethiopian representatives explained that all price adjustments needed to be reviewed and approved by the ONCCP before they could be effected. Public enterprises and others are free to submit price adjustment requests as often as they wish, but these requests must be fully documented. The authorities said that in many cases price increases were requested to hide inefficiencies in the firms. By refusing such adjustments, the authorities were forcing the enterprises to improve their management and performance. Corporations in difficulty have been reviewed on a case by case basis.

The Ethiopian representatives stressed that in centrally planned economic systems, the major role in the allocation of resources was in the physical planning of the use of real resources. Prices played a secondary role.

### 3. Financial policies

It was the Ethiopian representatives' view that, with the exception of 1982/83, financial policies have tended to be prudent and adequate for Ethiopia's needs. The large deficit in 1982/83 was due to special provisions to clear outstanding Government arrears and to strengthen the capital base of certain corporations. These actions themselves were prudent, as they re-established the financial position of the enterprises and the budget. At the present time, the budgetary deficit for 1984/85 is being affected by the drought and by the need to limit imports. Revenues were falling short of expectations, and therefore expenditures had been reduced, and the overall deficit and domestic financing should be comparable to the previous year's level. According to the authorities, current expenditure would approximate the budgetary estimate, but savings on capital outlays would lead to

a lower budgetary deficit and reduced domestic financing. Capital expenditures were to be kept to Br 685 million (excluding Br 230 million for drought relief activities), or a level 30 percent less than the previous year. The mission endorsed the authorities' estimate of the likely outturn of recurrent expenditure, which in fact represented an acceleration (17 percent) over the growth in the previous three years (8 percent). With respect to capital expenditures, however, in the first half of the budgetary year, which traditionally has accounted for about one third the of outlay, capital expenditures had already reached Br 302 million, about 7 percent higher than the previous year's first half. These outlays set the pace for project implementation in the second semester. Consequently, in the staff representatives' view capital outlays (excluding Br 230 million for drought relief) could be about Br 948 million, or about equal to the previous year's level. The mission also cautioned that a shortfall in capital outlays of the magnitude suggested by the authorities would result in a concomitant reduction in foreign financing, without a major reduction in domestic financing. Net credit use in the first half of the fiscal year also suggested that the official expectations on the bank credit requirement for financing the budget deficit may be surpassed. Given the remaining months in the fiscal year, it was difficult to see how a cutback could be made in order to constrain expenditure and financing to the level foreseen by the authorities. The staff representatives pointed out that, despite the differences that emerged in the estimates, the policy implications were the same. The size of the overall deficit, and the amount of domestic financing, were unsustainable and over-expansionary, and required further cutbacks.

The Ethiopian representatives explained that the Government had been reviewing a series of revenue measures over the last three years. An important element of the reform included a changeover from specific to ad valorem rates for excise and sales taxes. However, they felt that the present circumstances were not propitious for their introduction, especially as the drought levy had been recently instituted. There was, however, the possibility that some selected measures of the revenue reform package could be introduced. The Ethiopian representatives were firm in their belief that with the return of normal weather conditions a boost in economic growth would promote a large enough increase in revenues to reduce significantly the danger of an overexpansionary budget. In this regard they felt that additional foreign resources would also emerge, providing the margin by which to reduce domestic financing. At any rate, detailed planning for the next fiscal year had not taken place yet, and the authorities were not in a position to discuss the details of the budget.

The Ethiopian representatives explained that a credit program was prepared each year that was consistent with the budgetary requirements and the agreed needs of public enterprises. Interest rates had recently become negative in real terms, but no action was contemplated, as the current inflationary situation was viewed as temporary.

#### 4. External policies

The Ethiopian representatives were concerned at the prospects of virtually exhausting their gross official reserves in the course of 1985. However, in their view, this was a by-product of the current crisis, which had reduced exports and required emergency imports. While they recognized that the depletion of their reserves had significantly reduced their margin for maneuver, they felt that normal weather conditions would promote the growth of exports, and there was room for a further reduction in imports. Moreover they were confident that additional foreign assistance would become available in the course of the next fiscal year. However, the Ethiopian representatives did recognize that the exchange rate of the birr was overvalued and could hinder export growth. Some exports could only take place on the basis of financial losses. The Ethiopian representatives were cognizant that there had already been a substantial reduction in the level of imports, excluding drought relief, during the current fiscal year, and that an additional cutback from this level would have a major negative impact on the productive sectors. They also felt that a cutback would be difficult to administer given that public enterprises had been forced to reduce their inventories to a minimum level in the current fiscal year.

The Ethiopian representatives explained that the exchange rate was kept under periodic review and that the most recent movement in the real effective exchange rate indicated an overvaluation of the birr. However, in their view, this was not a good time to reverse the overvaluation as it would have a significant impact on the inflation rate. Consequently, the authorities felt that any adjustment that needed to be undertaken on the exchange rate should await a more appropriate time.

The Ethiopian representatives felt that given the present and prospective pressures on the balance of payments, it was not possible to relax the import controls at this time. What was needed was more careful planning on their part to ascertain that essential items flowed in as needed, so that the productive sectors did not suffer unduly as a result of the balance of payments difficulties.

The staff representatives pointed out that, even with adequate rains, the balance of payments would show a large financing need, given the overvaluation of the exchange rate and the difficulties in further constraining imports. The financing need was expected to increase in the medium term if adjustment measures were not implemented.

The staff projections indicated that once the drought emergency is surmounted the current account deficit of the balance of payments would revert to a level comparable to that in the immediate predrought years. The estimate assumes a recovery in the coffee exports lost as a result

of the drought, but only relatively slow growth in exports of other commodities, given the lack of competitiveness resulting from the overvalued exchange rate. On the import side, it is assumed that imports, excluding emergency commodity assistance, will expand over the next two years to attain the traditional ratio of imports to GDP of about 18 percent. Assuming that the gross capital inflows and official transfers, excluding drought relief, are maintained at about 7 percent of GDP, an overall deficit of Br 150 million emerges in 1985/86, rising to Br 300 million in the subsequent two years. Given repayments to the Fund and the need to reconstitute reserves the financing to be secured would be even greater (Table 6). The magnitude and trend of the financing gap clearly emphasized the seriousness of the balance of payments prospects. It also underlined the urgency of adopting an adjustment strategy. However, the Ethiopian representatives felt that it was not appropriate to look into the medium term at the present time, given the current drought difficulties. In their view the resurgence of the economy would be sufficient to reduce the financing gap significantly. Moreover, the increased foreign assistance which they were expecting would reduce the magnitude of the problem to a manageable level. They felt that it would only be possible to review the medium-term after the drought conditions had been surpassed and the economy was again functioning at a normal level.

#### V. Staff Appraisal

Ethiopia is currently passing through an extremely trying and difficult time when the underlying domestic and external imbalances have been accentuated by the impact of a prolonged and massive drought. The overall balance of payments deficits since 1976/77, with the exception of 1981/82 when a surplus was achieved, have resulted in the virtual exhaustion of Ethiopia's official reserves. At the same time, the country's debt service burden has become relatively severe.

The authorities are dealing with the drought-related problems, with the support of a wide variety of international relief agencies and donors. They are hopeful that the return of normal weather conditions will provide the main avenue through which internal and external imbalances can be reduced and economic growth resumed. Satisfactory progress in this direction would, however, be facilitated if the authorities also implemented corrective actions in those areas where past policies have contributed to the emergence of underlying financial imbalances, which were evident even before the onset of the drought. In this respect, priority should be given to improving resource allocation through major adjustments in producer and other controlled prices, the investment program, the budget, interest rates, and the exchange and trade system.

The lingering effects of the drought will continue to have an important impact over a number of years on agricultural production,

Table 6. Ethiopia: Balance of Payments Forecast,  
1984/85-1987/88

	1984/85	1985/86	1986/87	1987/88
(In millions of birr)				
Exports	796.0	873	887	940
Imports	-2,521.9	-2,173	-2,093	-2,255
Regular imports	(-1,603.5)	(-1,823)	(-2,093)	(-2,255)
Emergency relief commodity aid	(-918.4)	(-350)	(--)	(--)
Trade balance	-1,725.9	-1,300	-1,206	-982
Net services	-308.8	-39	141	173
of which: emergency relief services	(-411.6)	(-150)	(--)	(--)
Net private transfers	400.0	237	150	160
Current account	-1,634.7	-1,102	-915	-982
Net public transfers	1,159.7	537	160	187
Net capital	365.0	415	455	495
Gross borrowing	(622.5)	(703)	(690)	(739)
Repayments	(-257.5)	(-288)	(-235)	(-244)
Overall balance	-110.0	-150	-300	-300
Financing	110.0	150	300	300
Official reserves	100.0	-40	-31	-33
IMF (net)	-60.8	-70	-29	-17
Commercial bank assets (net)	70.8	--	--	--
To be secured	--	260	360	350
(In percent of GDP, unless otherwise specified)				
Exports	7.9	8.1	8.0	7.5
Imports including commodity aid	25.1	20.0	17.9	17.9
Imports excluding commodity aid	16.0	16.9	17.9	17.9
Current account deficit	-16.3	-10.2	-7.8	-7.8
Incl. public transfers	-4.7	-5.2	-6.3	-6.3
Excl. emergency assistance private, and public transfers	-7.0	-8.8	-9.1	-9.1
Gross capital inflow	6.0	6.5	5.9	5.9
Gross capital plus official transfers excluding drought relief	7.2	7.2	7.2	7.3
Reserves in weeks of regular imports	1.0	1.8	2.3	2.8
Private and public transfers plus capital flow (gross) per capita	20	22	22	23
Memorandum items: (In percent)				
Export value change	-14.4	9.7	1.6	6.0
Coffee volume change	-28.0	24.0	--	--
Unit value change	4.0	2.2	-1.5	1.6
Petroleum products volume change	2.4	-8.0	--	5.0
Unit value change	-9.6	2.0	2.0	2.0
Other export volume change	0.8	-11.2	5.4	8.2
Unit value change	6.5	-1.1	2.9	5.9
GDP growth (nominal)	-0.4	8.0	8.0	8.0
Import volume excl. commodity aid	-20.4	7.7	9.9	4.5
Import unit value excl. commodity aid	-2.4	4.5	4.5	4.5
(In millions of birr)				
Services (net excluding aid)	102.8	111	141	173
Emergency relief services	-411.6	-150	--	--
Private transfers	400.0	237	150	160
Underlying	124.0	140	150	160
Emergency aid	276.0	97	--	--
Public transfers	1,159.7	537	160	187
Underlying	105.7	134	160	187
Emergency aid	1,054.0	403	--	--

Sources: Data provided by Ethiopian authorities; and staff forecasts.

and therefore on the economy's ability to gain development momentum quickly. The objectives of the 10-Year Perspective Plan are laudable, but appear unattainable. According to the World Bank, the investment program contains the correct priorities but the magnitude of the program appears to be beyond the resources that are likely to be available. A realistic public investment program, which accurately takes account of prevailing circumstances and resources, needs to be prepared, so as to ensure the optimal allocation of available resources. Such a program, in conjunction with a meaningful macro-economic adjustment program, could be the basis for generating additional foreign assistance.

Over a number of years, the fiscal deficits have grown and domestic credit expansion has been excessive, with unfavorable effects on domestic prices and on the balance of payments. While the return of normal weather conditions should improve the domestic availability of goods, its possible favorable effect on the domestic price situation, and on the balance of payments, could be presumed only if, inter alia, the budgetary deficit and its domestic financing are reduced significantly. In this respect, revenue reforms have been studied over a number of years, and should be implemented at the earliest date, in order to avoid an excessive burden of adjustment on the expenditure side. Simultaneously, the financial situation of the public enterprises needs to be reviewed thoroughly with a view toward improving their financial position and reducing their access to domestic bank credit or budgetary transfers. While the authorities rightly believe that the management and efficiency of these enterprises could be improved, their overall financial position is likely to remain weak if adequate and timely price adjustments are not allowed.

An improvement in the financial position of the public sector should also make it possible to keep the overall credit expansion well below its high historical rate, and consistent with a significant improvement in the balance of payments.

In an effort to limit inflationary pressures, prices have been controlled by the authorities, with adverse effects on profitability and incentives to invest and produce. Accordingly, prices for major products should be pitched at levels that promote the increased use of fertilizers and other inputs and thus raise output. Adequate producer prices will necessarily also involve higher consumer prices, particularly as the need to improve the budgetary position would preclude budgetary subsidies. The domestic prices of many export products also need to be raised by a significant amount if they are to attract the resources to expand production. In bringing about the necessary adjustment in prices, economic producing units need to be given greater freedom of action in production and pricing policies, while additional gains could be reaped if the energy and experience of the private sector are properly harnessed to contribute to production gains. Cautious financial and incomes policies will help limit the inflationary impact of the required price adjustments.

The above action, especially relating to the increase in prices for export commodities, will only be possible to attain if the authorities would reverse the appreciation that the birr has experienced in the last five years. Such an exchange rate action, complemented by more restrictive financial policies, would go a long way in re-establishing the competitive position of exports, and in promoting the needed diversification of production and exports. It should also allow the progressive liberalization of the existing severely restrictive exchange and trade system.

The retention by Ethiopia of comprehensive restrictions on the making of current payments is subject to approval under Article VIII, Section 2(a). Generally speaking, the importation of goods and payments for services are subject to availability of exchange under periodic import and exchange budgets. The exchange restrictions on payments and transfers for invisible transactions are maintained by Ethiopia in accordance with Article XIV, Section 2. There are no payments arrears on commercial or financial obligations. Notwithstanding the approval granted upon the completion of the 1984 Article IV consultation with respect to restrictions on import payments, no progress has been made by Ethiopia in reducing its reliance on comprehensive controls on international transactions for balance of payments reasons. Therefore, the staff does not recommend approval of the exchange measures at this time.

It is expected that the next consultation discussions will take place on the basis of a twelve-month cycle.



VI. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. The Fund takes this decision relating to Ethiopia's exchange measures subject to Article VIII, Section 2(a), in concluding the 1985 Article XIV consultation with Ethiopia and in the light of the 1985 Article IV consultation with Ethiopia conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Ethiopia continues to maintain restrictions on the making of payments and transfers for current international transactions as described in SM/85/. The Fund urges the authorities to implement such policies and measures as will facilitate the withdrawal of remaining restrictions.

ETHIOPIA - Basic Data

Area, population, and GDP per capita

Area	1.2 million square kilometers
Population:	
Total (mid-1984 estimate)	42.0 million
Growth rate	2.9 percent
GDP per capita (1983)	SDR 117

	<u>1979/80</u>	<u>1980/81</u>	<u>1981/82</u>	<u>1982/83</u>	<u>1983/84</u>	<u>1984/85</u>	<u>1/</u>
	<u>Fiscal year ended July 7</u>						
<u>Gross domestic product (GDP)</u>	<u>(In millions of birr unless otherwise specified)</u>						
Expenditure on GDP							
GDP at current							
market prices	8,533.9	8,906.5	9,169.4	10,015.9	10,054.5	10,010.3	
GDP at 1980/81							
factor cost	7,855.4	8,100.3	8,186.3	8,607.1	8,404.5	7,835.4	
Agriculture (per-							
cent of total)	50.6	50.3	49.1	48.9	45.7	41.2	
Manufacturing (per-							
cent of total)	6.8	7.0	7.2	7.4	7.8	8.2	
Distribution							
services (per-							
cent of total)	15.1	15.1	15.4	15.5	16.1	17.7	
Public admini-							
stration (per-							
cent of total)	7.2	7.2	7.4	7.4	7.8	8.6	
Annual real growth							
rate (percent)	5.6	3.1	1.1	5.1	-2.4	-6.8	
Investment (percent							
of nominal GDP)	11.1	11.5	13.3	11.2	12.8	10.8	
<u>Prices</u>	<u>(Annual percent change)</u>						
GDP deflator	2.0	2.1	1.4	3.9	1.5	7.1	
Consumer price index	12.5	1.9	7.3	3.9	-0.3	16.1	<u>2/</u>

1/ Provisional.

2/ For the eight months ending February 1985.

ETHIOPIA - Basic Data (continued)

	<u>1979/80</u>	<u>1980/81</u>	<u>1981/82</u>	<u>1982/83</u>	<u>1983/84</u>	<u>1984/85</u> <u>1/</u>
	<u>Fiscal year ended July 7</u>					
<u>Government finance</u>	<u>(In millions of birr)</u>					
Recurrent revenue	1,567.5	1,756.9	1,848.0	2,046.6	2,217.4	2,360.0
Foreign grants	55.5	69.2	97.0	143.3	219.4	308.0
Expenditure and net lending	2,003.5	2,160.4	2,518.0	3,507.1	3,057.0	3,543.0
Current	(1,560.3)	(1,655.3)	(1,816.4)	(2,290.6)	(2,075.9)	(2,365.0)
Capital	(443.2)	(505.1)	(701.6)	( 972.6)	(963.1)	(1,178.0)
Overall deficit (-) and financing	-383.5	-334.3	-573.0	-1,317.2	-620.0	-875.0
External financing (net)	(142.3)	(128.0)	(477.8)	(450.7)	(264.6)	(340.0)
Domestic financing (net)	(241.2)	(206.3)	(95.2)	(866.5)	(355.4)	(535.0)
Banking system (net)	199.3	142.0	62.2	829.4	336.5	505.0
	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1984</u>
			<u>End of June</u>			<u>End Dec.</u>
<u>Money and credit</u>	<u>(In millions of birr)</u>					
Domestic credit	2,612.3	2,829.7	8,125.1	3,722.5	4,155.3	4,311.8
Claims on Government (net)	(968.1)	(1,107.9)	(1,180.8)	(1,980.8)	2,293.4	(2,497.1)
Other credit	(1,644.2)	(1,721.8)	(1,944.3)	(1,741.7)	(1,861.9)	(1,814.7)
Money and quasi-money	2,332.1	2,377.6	2,643.7	3,040.5	3,389.7	3,378.0
	<u>1979/80</u>	<u>1980/81</u>	<u>1981/82</u>	<u>1982/83</u>	<u>1983/84</u>	<u>1984/85</u> <u>1/</u>
	<u>Fiscal year ended July 7</u>					
<u>Balance of payments</u>	<u>(In millions of SDRs unless otherwise specified)</u>					
Exports, f.o.b.	364.3	327.5	337.9	362.4	427.8	390.7 <u>1/</u>
Of which: coffee	(234.5)	(201.4)	(202.7)	(221.9)	(271.5)	(216.9)
Imports, c.i.f.	-579.1	-608.6	-746.2	-790.6	-977.6	-1,237.7
Trade balance	-214.6	-281.1	-408.3	-429.2	-549.9	-847.1
Services (net)	20.5	27.0	25.6	38.3	40.1	-151.6
Private unrequited transfers	15.3	19.6	39.8	78.4	102.1	196.3
Current account balance	-178.8	-234.4	-343.0	-312.2	-407.7	-802.3

1/ Provisional.

ETHIOPIA - Basic Data (concluded)

	<u>1979/80</u>	<u>1980/81</u>	<u>1981/82</u>	<u>1982/83</u>	<u>1983/84</u>	<u>1984/85</u> <u>1/</u>
	<u>Fiscal year ended July 7</u>					
<u>Balance of Payments (cont.)</u>	<u>(In millions of SDRs unless otherwise specified)</u>					
Official unrequited transfers	46.0	47.6	59.4	85.4	154.2	569.2
Capital account (net)	104.3	123.7	288.6	179.1	204.7	179.1
Errors and omissions	-6.3	-10.6	29.3	-18.0	8.6	--
SDR allocation	3.7	3.8	4.1	--	--	--
Revaluation of reserves	--	22.5	14.8	--	--	--
Overall balance (deficit -)	<u>-31.0</u>	<u>-47.5</u>	<u>53.2</u>	<u>-66.0</u>	<u>-40.3</u>	-54.0
Current account deficit (percent of GDP)	-5.6	-6.8	-8.8	-7.0	-8.8	-16.3
<u>Exchange rate (Br/SDR, period average)</u>	2.6931	2.6033	2.3541	2.2424	2.1743	2.0375
<u>Gross official reserves (end of period)</u>	121.1	124.7	243.7	200.3	106.7	64.1 <u>2/</u>
In weeks of imports	11.6	11.4	18.4	13.2	6.4	...
<u>External public debt (end of period)</u>						
Outstanding	562.3	742.9	1,036.4	1,248.1	1,491.0	1,778.8
Debt service payments (as percent of exports of goods and nonfactor services)						
Including the Fund	5.8	7.1	12.9	16.2	16.1	37.1
Excluding the Fund	5.8	7.0	10.2	13.1	11.5	29.6

1/ Provisional.

2/ December 1984.

ETHIOPIA: Relations with the Fund  
(As of April 30, 1985)

I. Membership Status:

- |     |                    |                   |
|-----|--------------------|-------------------|
| (a) | Date of membership | December 27, 1945 |
| (b) | Status             | Article XIV       |

A. Financial Relations

II. General Department

- |     |  |   |
|-----|--|---|
| (a) | Quota  | SDR 70.6 million                                |
| (b) | Total Fund holdings of Ethiopian currency                  | SDR 140.59 million<br>(199.14 percent of quota) |
| (c) | Fund holdings of Ethiopia's currency subject to repurchase | SDR 69.98 million<br>(99.12 percent of quota)   |
|     | Credit tranche   | SDR 27.87 million<br>(39.48 percent of quota)   |
|     | E.A.R.   | SDR 30.86 million<br>(43.71 percent of quota)   |
|     | C.F.F.   | SDR 11.25 million<br>(15.94 percent of quota)   |

III. Current Stand-By or Previous Arrangements

and Special Facilities

- |     |  |   |
|-----|--|---|
| (a) | Current stand-by:  | None  |
| (b) | Previous arrangements:   | Stand-by arrangement (SDR 67.5 million) approved in May 1981. |
| (c) | Special facilities approved included Trust Fund loans, SFF subsidy account, and compensatory financing facilities for export shortfalls (SDR 36 million in 1979 and SDR 18 million in 1981). |   |

IV. SDR Department

- |     |                             |   |
|-----|-----------------------------|---|
| (a) | Net cumulative allocation - | SDR 11.16 million   |
| (b) | Holdings -                  | SDR 1.20 million, or 10.79 percent of net cumulative allocation |

ETHIOPIA: Relations with the Fund (concluded)

V. Administered Accounts

(a) Trust Fund loans:

(i) Disbursed - SDR 26.39 million

(ii) Outstanding - SDR 22.40 million

(b) SFF Subsidy Account:

(i) Payments by Fund - Nil

VI. Overdue Obligations to the Fund - None

B. Nonfinancial Relations

VII. Exchange system: Pegged to the US\$ at Br 2.07 = US\$ 1;  
the SDR/local currency equivalent is SDR 1 = Br 2.0517.

Intervention currency and rate: U.S. dollar; Br 1 = US\$ .48309

VIII. Last Article IV Consultation

Article IV, March 3-17, 1984 (SM/84/102), discussed by the Executive Board on June 8, 1984 (EBM/84/90). The following decision was adopted:

1. The Fund takes this decision relating to Ethiopia's exchange measures subject to Article VIII, Section 2(a), in concluding the 1984 Article XIV consultation with Ethiopia and in the light of the 1984 Article IV consultation with Ethiopia conducted under Decision No. 5392(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Ethiopia continues to maintain restrictions on payments and transfers for current international transactions as described in SM/84/102. The Fund encourages the authorities to take steps to relax and to remove existing restrictions as the balance of payments situation improves. In the meantime, the Fund grants approval of the retention of the exchange restrictions subject to approval under Article VIII, Section 2(a), until the completion of the next Article IV consultation with Ethiopia or May 31, 1985, whichever is earlier.

IX. Technical Assistance in 1984:

Bureau of Statistics technical assistance in trade price and quantum statistics.

Bureau of Computing Services technical assistance.

Ethiopia: Relations with the World Bank Group

Table I. Gross Disbursements and Net Transfers

(Fiscal year ending June 30; in millions of U.S. dollars)

Lending program - 1984	105.0
Gross disbursements	35.2
Net transfer <u>1/</u>	29.3
 Lending program - 1985 (approved)	 166.0
Gross disbursements <u>2/</u>	41.0
Net transfer <u>2/</u>	34.5
 Lending program - 1986 (proposed) <u>2/</u>	 115.0
Gross disbursements	65.0
Net transfer	57.0

---

1/ Disbursements less amortization, interest, and charges.

2/ Provisional.

Ethiopia: Relations with the World Bank Group

Table II. IBRD Loans and IDA Credits by Sector

(As of February 28, 1985; in millions of U.S. dollars)

	Total			Disbursed			Undisbursed		
	Total	IBRD	IDA	Total	IBRD	IDA	Total	IBRD	IDA
Agriculture	266.71	4.00	262.71	178.59	4.00	174.59	88.12	--	88.12
Education	150.41	--	150.41	74.73	--	74.73	75.68	--	75.68
Energy	52.82	46.50	6.32	50.88	46.50	4.38	1.94	--	1.94
Urban develop- ment <u>1/</u>	28.09	10.80	17.29	11.35	10.80	0.55	16.74	--	16.74
Transportation	201.75	33.50	168.25	142.15	33.50	108.65	59.60	--	59.60
Communications	87.07	13.70	73.37	47.07	13.70	33.37	40.00	--	40.00
Other	4.00	--	4.00	--	--	--	4.00	--	4.00
Total	790.85	108.50	682.35	504.77	108.50	396.27	286.08	--	286.08

Source: Data provided by the World Bank.

1/ Including urban water supply.



Ethiopia--Statistical Issues

1. Outstanding statistical issues

There are no major statistical issues outstanding at present. However, the following points are worth noting:

a. Government finance

Government finance data have been reported regularly to the Bureau of Statistics, but with long lags, reflecting about a five-year delay in the closing of the government accounts.

b. Monetary accounts

The balance Sheets of the Commercial Bank of Ethiopia have been revised. The resulting changes for IFS data, which include an improved sectorization of domestic credit and an appropriate classification of provisions for doubtful debt, will be presented in an early issue of IFS.

c. Trade indices

The trade indices have been uncurrent for some time. This is related to ongoing work by the national compilers on the preparation of new indices. Recommendations bearing on this work were included in the report of the Bureau's technical assistance mission of April 1984.

2. Coverage, currentness, and reporting of data in IFS

The table below shows the currentness and coverage of data published in the country page for Ethiopia in the April 1985 issue of IFS. The data are based on reports sent to the Fund's Bureau of Statistics by the National Bank of Ethiopia, which during the past year have been provided on a fairly regular basis. The currentness of the data has improved in recent months.





Status of IFS Data

		<u>Latest Data in</u> <u>April 1985 IFS</u>
Real Sector	- National Accounts	1983
	- Prices	October 1984
	- Production	n.a.
	- Employment	n.a.
	- Earnings	n.a.
Government Finance	- Deficit/Surplus	1979
	- Financing	1979
	- Debt	1979
Monetary Accounts	- Monetary Authorities	January 1985
	- Deposit Money Banks	December 1984
	- Other Financial Institutions	September 1984
External Sector	- Merchandise Trade: Values	Q1 1984
	Export Prices	Q1 1981
	Import Prices	1981
	- Balance of Payments	Q4 1983
	- International Reserves	February 1985
	- Exchange Rates	February 1985

