CareEdge Global assigns Long Term Foreign Currency Rating of D (Unsolicited) to the Federal Democratic Republic of Ethiopia

Credit Profile

In recent times, social unrest coupled with several shocks have led to Ethiopia's macroeconomic pressures, with the public investment-led growth model reaching its limit. Strained liquidity has led to a deterioration of both the fiscal space and external balance (exacerbated by the recent default on a USD 33 million coupon payment). The maturity of the associated USD 1 billion Eurobond at the end of 2024, now presents a risk of a debt crisis due to the economy's inadequate foreign reserve position.

The conclusion of a USD 3.4 billion extended credit facility (ECF) programme with the IMF has now enabled debt restructuring, where the government aims to reach an agreement as per the Common Framework (CF) debt treatment. This may lead to stability on both the fiscal and external sides. However, this also adds layers of complexity. For example, reforms under the IMF programme, including the unification of the exchange rate could worsen social risks due to higher inflation, where food security is already a concern.

On the positive side, we note the implementation of the Homegrown Economic Reform Agenda (HGER) which aims to achieve sustained high growth of the previous decade by facilitating a shift towards a more private-sector-driven economy.

Strengths

- High potential growth
- Strong FDI and official donor assistance (ODA)
- Secured IMF funding and potential to unlock additional concessional funds

Weaknesses

- Delay in debt restructuring
- Low revenue-to-GDP
- High contingent liabilities due to inefficiencies in SOEs
- Low levels of reserves and liquidity
- Social unrest and geopolitical tensions

Key Monitorables

- Debt restructuring under the G20s Common Framework (CF)
- Adherence to committed IMF programme reforms
- Economic reform developments under the homegrown agenda
- Sustained exchange rate flexibility

Key Rating Drivers

Economic Structure & Resilience

Ethiopia's economic structure is classified by low-income levels (USD 3070 in 2023, constant PPP per capita terms). Growth has averaged around 6% between 2020-2022, below pandemic levels (8%-10%), mainly due to a series of external shocks, as well as the shortcomings of the public sector investment growth model. For example, the model was mostly debt-financed and created macro-economic imbalances. The implementation of the HGER agenda is poised to drive future growth of around 7% over the medium-term.

From a sector perspective, agriculture (33% of GDP) is expected to rebound on the back of better weather conditions, the privatization of state-owned sugar factories, and government initiatives in areas such as irrigation. Services growth (40% of GDP) is expected to remain strong particularly in tourism, and the liberalization of the banking sector. Industry (29% of GDP) is expected to be driven by investments in industrial parks and transport infrastructure. Investment in alternative energy sources (such as wind) will see energy production increase, which will in turn boost energy exports. However, headwinds related to recurrent internal conflicts and poor execution of desired reforms, may lead to high inflation, continued fiscal pressures and challenges in doing business.

Fiscal Strength

Ethiopia has one of the lowest revenue-to-GDP ratios in Africa (7.3% in FY23/24) due to a large informal sector and small private sector. Nonetheless, fiscal consolidation is ongoing through decreased expenditure-to-GDP and the gradual reduction in the fuel subsidy. Under the IMF programme the government aims to raise revenue and thereby enhance capacity to increase space for pro-poor, social and capital expenditures. A key risk to sustained fiscal consolidation will be the impact of inflationary pressures following exchange rate unification. However, an IMF disbursement will ensure pro-poor spending capacity and provide temporary subsidies for key imported goods affected by exchange rate reform.

Public sector debt is projected at around 34% in FY23/24. Of the total debt stock, around 32% is in external debt, thereby exposing the government to foreign exchange risk. Liquidity constraints saw the country apply for the G20s debt service suspension initiative (DSSI), enabling debt service suspension agreements with bilateral creditors, including China. However, due to equal treatment of creditors, the country defaulted on a USD 33 million coupon payment. However, since agreeing to the new IMF programme, debt restructuring is currently underway as per the G20s Common Framework (CF). Another crucial risk to the government's finances is the high exposure of contingent liabilities. The HGER agenda and commitment to reforms under the IMF programme seeks to address inefficiencies of SOEs.

External Position & Linkages

The current account deficit (CAD) is expected to decline to around 2.6% in FY23/24, from 2.8% in FY22/23. This is partly due to import compression (from FX restrictions) and the loss of duty-free access to the US market (due to social unrest). These developments have also negatively impacted foreign exchange revenues.

Forex reserves are scarce and sufficient to cover less than 1 month of imports. The new IMF programme has enabled the rebuilding of reserves and may even unlock additional concessional funding streams for which the country is reliant to fund any balance of payments deficits. The government only has one outstanding Eurobond of USD 1 billion maturing in December 2024. With a now secured IMF agreement, a deal could be reached under the CF and ahead of the principal payment coming due. However, this may be a lengthy process as was the case for Zambia and Ghana.

Monetary & Financial Stability

Although the country has liberalised its exchange rate, there are still interventions to manage liquidity. Inflation remains elevated at around 26.9% in FY23/24, although it is expected to fall, it will remain in double-digit territory (around 16% projected for FY25/26).

The National Bank of Ethiopia (NBE) announced new monetary measures to control inflation, including increasing its emergency lending rate to commercial banks, imposing caps on credit growth, restrained fiscal spending and removing the practice of monetizing its fiscal deficits completely. The banking sector is highly concentrated, with the two public banks accounting for a significant majority of total assets. There are plans to liberalize the banking sector, which could increase deposit growth significantly.

Institutions & Quality of Governance

Despite the holding of the Pretoria agreement, social unrest remains in some of the regions of Ethiopia. Social unrest is also responsible for delays in policy implementation and securing concessional loans. There is limited scope for independent bodies in the policy-making process, and there is no monitoring of government by civil society. Economic and fiscal data are often released with significant delays. Lastly, the country's monetary and macro-economic policy has struggled to manage price stability. On a positive note, under the IMF programme, the government has agreed to take steps towards strengthening its institutional framework.

Ethiopia – Select Indicators									
	Unit	2018	2019	2020	2021	2022	2023	2024 F	2025 F
Economic Indicators									
Nominal GDP	USD Billion	80.2	92.6	96.6	99.3	119.0	159.7	205.1	236.0
GDP Per Capita (Constant-PPP)	USD	2,426	2,588	2,687	2,794	2,909	3,070	3,210	3,364
Real GDP Growth	%	7.7	9.0	6.1	6.3	6.4	7.2	6.1	6.5
GFCF/ GDP	%	34.7	35.3	30.6	28.0	25.3	22.2	-	-
Gross Domestic Savings/ GDP	%	24.1	22.1	20.8	18.9	15.3	14.8	-	-
Exports (G&S)/GDP	%	8.4	7.9	7.1	7.6	8.2	6.6	-	-
Working-Age (15-64) Population (% Share in Total)	%	55.9	56.2	56.6	56.9	57.2	57.5	57.8	58.1
Old-Age (65+) Population (% Share in Total)	%	3.1	3.1	3.1	3.1	3.1	3.2	3.2	3.3
Fiscal Indicators – General Government									
Fiscal Balance/ GDP	%	-3.0	-2.5	-2.8	-2.8	-4.2	-2.6	-1.7	-1.7
Revenue/ GDP	%	13.1	12.8	11.7	11.0	8.1	7.9	7.3	8.3
Expenditure/ GDP	%	16.1	15.4	14.5	13.8	12.7	10.8	9.4	11.3
GG Gross Debt/ GDP	%	58.4	54.7	53.7	53.8	48.9	40.2	34.4	42.9
GG External Debt (by Creditor)/ GG Gross Debt	%	32.8	32.8	36.9	36.3	34.6	32.1	-	-
Interest/ Revenue	%	5.0	5.2	4.5	7.6	12.8	-	-	-
External Indicators									
Current Account Balance/ GDP	%	-6.5	-5.3	-4.6	-3.2	-4.0	-2.8	-2.6	-4.3
FDI, Net Inflows/ GDP	%	4.2	2.8	2.5	4.3	2.6	2.1	1.6	2.7
Import Cover	Months	2.4	1.8	2.0	4.1	0.8	0.5	0.5	1.2
External Debt/GDP	%	33.8	30.0	31.0	29.7	24.0	18.1	15.4	28.3
Monetary and Financial Indicators									
CPI Inflation	%	13.8	15.8	20.4	26.8	33.9	32.5	26.9	30.1
Exchange Rate (Average)	LC per USD	27.4	29.1	34.9	43.7	51.8	54.6	-	-
Non-Performing Loans/ Total Gross Loans	%	3.6	2.7	3.4	5.4	3.9	3.6	-	-
Private debt, loans and debt securities/ GDP	%	20.2	21.1	21.3	19.6	18.7	-	-	-

Sources: International Monetary Fund, World Bank, Bank for International Settlements, National Sources, CareEdge Global

Note: F - Forecast; PPP – Purchasing Power Parity; GFCF – Gross Fixed Capital Formation; Exports (G&S) – Exports of Goods and Services; GG – General Government; FDI – Foreign Direct Investment; FII – Foreign Institutional Investment; NIIP – Net International Investment Position; Data refers to fiscal/calendar year and actual/estimate as reported by the source; Where general government data is unavailable, central government data is used; Latest available data for 2023

Rating History

Instrument	Type	Rating	Date
Issuer Rating	Long Term Foreign Currency (Unsolicited)	D	October 3, 2024

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Criteria Applied

CareEdge Sovereign Rating Methodology

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