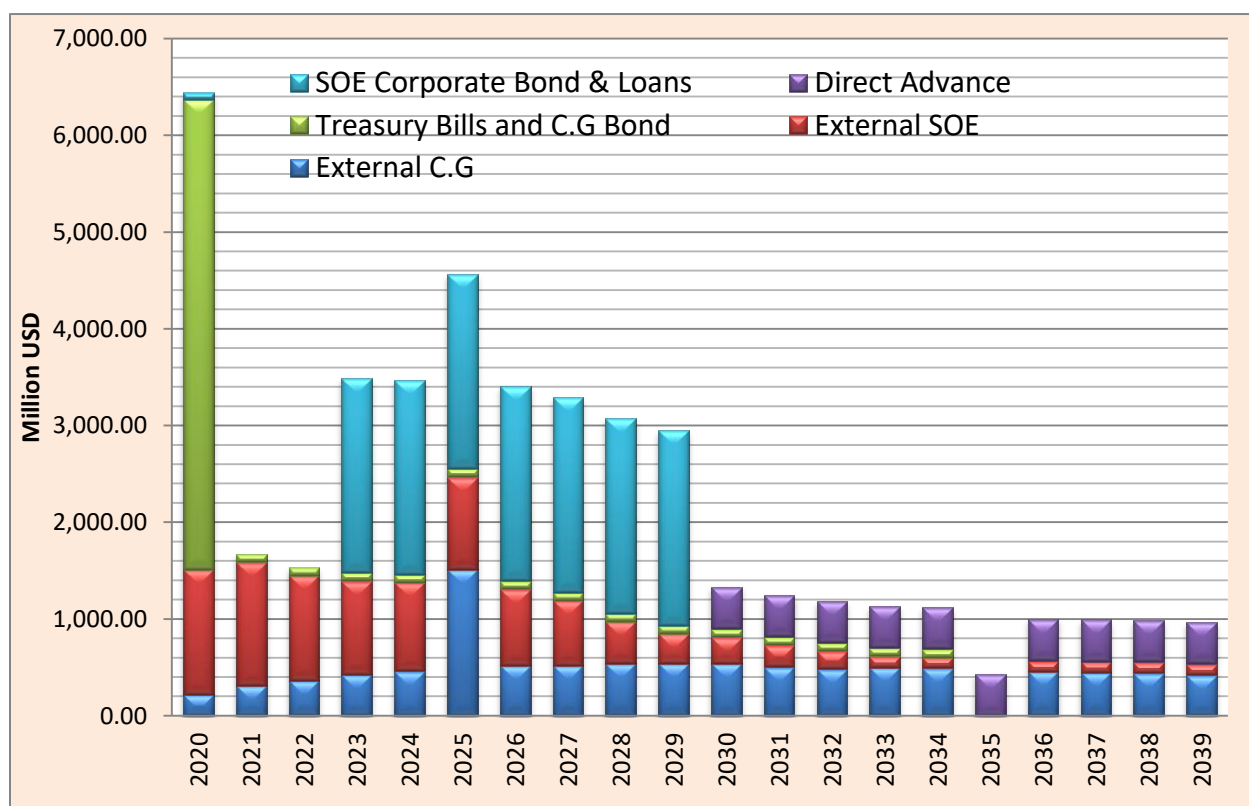


ANNUAL PUBLIC SECTOR DEBT PORTFOLIO ANALYSIS FOR THE YEAR 2018/19

NO. 20

Total Public Sector Debt Redemption Profile



DEBT MANAGEMENT DIRECTORATE
MINISTRY OF FINANCE
FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA

Forward

The principles of public debt management in Ethiopia are enshrined in the Financial Administration Proclamation No. 648/2009 (as amended by Proclamation No. 970/2016) and the Financial Administration Regulations. The legal framework is meant to promote prudent and sound debt management practices for both Federal Government and State Owned Enterprises with the aim of enhancing public finance effectiveness and transparency in management of public resources. The 2019 Annual Debt Portfolio Analysis is part of the reporting requirement under the legal framework of the country. The Debt Management Directorate (DMD) within the Ministry of Finance is mandated to manage the public debt in the country

Public debt management is the process of establishing and executing a strategy for managing the public sector's debt to raise the required amount of funding, pursue its cost/risk objectives, and meets any other public debt management goals the government may have set, such as enhancing debt monitoring and management of the country including developing and maintaining an efficient and liquid market for government and corporate securities.

The Ministry of Finance is the primary agent of Government of Ethiopia responsible for managing and conducting various cost-risk analyses of the country's public debt portfolios. It prepares, manages and follows up the country's Medium Term Debt Management Strategy. In addition, it is responsible for compilation and dissemination of public debt statistics and Annual Public Sector Debt Portfolio Analysis. It also prepares the country's Debt Sustainability Analysis every fiscal year and disseminates to the policy makers for decision.

Hence, this Twentieth Annual Public Sector Debt Portfolio Analysis (DPA) is an annual report prepared by the Debt Management Directorate aiming to provide a broader view of the public debt portfolio, dealing with the volume of the public debt and its breakdown, variations in stocks as well as detail analysis of some key debt variables.

The current Twentieth editions, comprehensively examines the five years' total public debt composition, magnitude and trends beginning from 2014/15 to 2018/19.

Preparation of comprehensive and timely DPA allows Government and other users to monitor the evolution of the public sector's debt accumulation and its debt-service obligations over time. This DPA is considered an essential inputs, for forecasting, and for compiling other macroeconomic statistics and serve as an indicator of the sustainability of government and public corporations' policies.

The Government is considering this report in line with the Financial Administration Act, as a tool for evaluating and managing the risk involved with different debt compositions; facilitating coordination with fiscal and monetary management; and enhancing transparency. In addition, the Government is expects through this action of preparing annual debt report will support efforts that aim for the government's financing needs and payment obligations are met at the lowest possible cost consistent with a prudent degree of risk.

Similarly, the report will not only provide the senior management of the country with details of the debt dynamics in 2018/19, but will also serve as a useful repository of information for public, academicians, researchers, the media and all other relevant stakeholders. An electronic version of this report is available on the website of Ministry of Finance in PDF format and in Debt Management Directorate. All queries on the contents of the report should be addressed to the Debt Management Directorate in the Ministry of Finance through the address below.

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**Mission Statement
Of
Debt Management Directorate**

To ensure sound external and domestic debt management by effectively and efficiently co-negotiating and renegotiating external loans, properly administering disbursements and repayments of external and domestic debts, follow up of on-lent debts, designing and updating appropriate debt management strategy of the country.

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ACRONYMS

AfDB	African Development Bank
AfDF	African Development Fund
BADEA	Arab Bank for Economic Development in Africa
CBE	Commercial Bank of Ethiopia
DA	Direct Advance
DBE	Development Bank of Ethiopia
DS	Debt Service
EAL	Ethiopian Airlines
EEP	Ethiopian Electric Power
EEU	Ethiopian Electric Utility
EIB	European Investment Bank
ESC	Ethiopian Sugar Corporation
ETB	Ethiopian Birr
EUR	Official Currency for 19 member countries of European Union
ERC	Ethiopian Railway Corporation
GDP	Gross Domestic Product
HIPC	Highly Indebted Poor Countries
ICBC	Investment and Construction Bank of China
IDA	International Development Association
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
JPY	Japanese Yen
MDRI	Multilateral Debt Relief Initiatives
MoF	Ministry of Finance
NBE	National Bank of Ethiopia
NDF	Nordic Development Fund
OFID	OPEC Fund for International Development
POESSA	Private Organization Employees Social Security Agency
PSSSA	Public Servants Social Security Agency
SOEs	State Owned Enterprises
SDR	Special Drawing Rights
TBs	Treasury Bills

EXECUTIVE SUMMARY

Ethiopia's vision, committed leadership and diligence of its people, has now created the necessary foundation for the country to reach lower middle income status. In the run up to the current state of affairs of the Ethiopian economy, output grew continuously for more than a decade and half, poverty was reduced by more than half, and the economy remained resilient despite multiple shocks arising from drought, political instability and global external sector performance slowdown. Recently, as highlighted above, the new economic reform namely Home-Grown Economic Reform has been launched to address the pertinent challenges in the sphere of macroeconomic, structural and sectoral those help to achieve the required transformation in the economy over the next three years. In this regard prudent public debt management and ensuring sustainability of public debt over the medium term will continue to be one of key functions of the Ministry of Finance.

Following the implementation of the HIPC initiative which culminated in successfully Reaching Completion Point in 2006, the country benefited from significant debt burden reduction. Since then it is evident that a significant buildup of debt has materialized, reaching the current level of about 49 percent in PV terms of GDP in June 2019.

By end June 2019, Ethiopia's total public external and domestic debt stock including publicly guaranteed debt amounted to USD 53,705 million compared to USD 49,340 million reported at the end June 2018 representing an increase of 9 percent. Domestic debt increased by 13 percent to USD 26,676 million while external debt increased by 5 percent to USD 27,029 million at end June 2019 from June 2018.

Out of Ethiopia's total external debt outstanding, multilateral agencies which provide highly concessional loan held about 43 percent while bilateral creditors have 31 percent share out of the total debt stock and the remaining owed by Private creditors. Out of

private creditors commercial banks and suppliers held about 14 percent and about 7 percent respectively while Eurobond held 3.7 percent.

As at June 2019, the stock of treasury bills, government bonds and direct advances accounted for about 18 percent, 5 percent and 24 percent of total domestic debt, respectively. As far as the SOEs stock of domestic debt is concerned, corporate bond and long term loans accounted 39 percent and 14 percent respectively.

The currency composition of the Ethiopia's external debt stock comprised of the United States Dollar (USD) at 73 percent, Euro at 15 percent and Chinese Yuan at 5 percent while other currencies accounted for 7 percent of the portfolio.

The total public debt service payments in 2018/19 was USD 3,264 million with external debt service standing at USD 2,011 million while domestic debt service was at USD 1,253 million. As a percentage of the total public debt service, external and domestic debt service were 62 percent and 38 percent respectively.

The Present value external debt in percent of Export, as per 2018 DSA was about 249 percent while the threshold for Ethiopia is 180 percent so this ratio breach at the baseline .The other export related ratio which is breached by Ethiopia is the external debt service to export ratio which is about 24 percent but the threshold is 15 percent due to these two export related ratios the country debt distress level become high risk, but this may improve in the subsequent years as a result of a reduction in non-concessional borrowing by SOE's and the expected improvement in the export sector.

Overall, Ethiopia's total public debt (External plus Domestic debt) remain sustainable over the medium term and it is well within the threshold of 55 percent in Present value terms as percent of GDP in line with the threshold set by the World Bank and IMF, currently Ethiopia's Present Value of total Public Debt in percent of GDP is about 49 percent.

Public Debt to GDP ratio is expected to stabilize in the medium term and come down gradually as the government implements prudent fiscal policy commitments aimed at reducing the fiscal deficits as well as limiting contracting loans from Non-Concessional sources to implement strategically important projects.

Ethiopia, cognizant of debt accumulation, has put in place a Public Private Partnership (PPP) framework in order to fund infrastructure development as a catalyst to foster economic growth. To minimize exposure and risks associated with debt accumulation the government has embraced new innovations in financing infrastructure development off balance sheet without impacting heavily the debt portfolio. Towards this end, the country is working to increase private financing of public investments through the PPP initiatives. This is one of the MoF key strategies to maintain reduction of the fiscal deficits in order to ensure that debt accumulation remains at prudent rates and that public debt remains within sustainable levels.

1. Introduction

Debt Portfolio Analysis, which provides an update on Ethiopia's public debt as at June 2019, critically assesses trends and developments on Central Government external and domestic debt, SOE government-guaranteed and non-guaranteed external and domestic debt. It also brings to the fore the risks, issues and challenges related to debt management and the forward looking strategy that the Government is committed to adhere to while supporting the country's future economic and social development path. Ethiopia, after launching its new Home-Grown Economic Reform Agenda, is preparing to implement wide-ranging of reforms to create the enabling environment that will enable the economy to grow at a sound pace and achieve middle-income status. The Government, side by side with macroeconomic reforms, needs continuous reviews its public debt portfolio in the light of efforts to address emerging challenges.

Conducting a review of the country's public debt portfolio is an important element of a debt management strategy - which is itself a crucial component of sound economic management. With debt management a core component of Ethiopia's Public Financial Management (PFM) framework, it is important for the Debt Management Directorate (DMD) to regularly carry out such a review to monitor on a continuous and consistent manner the level of indebtedness of the economy, and ensure an optimum borrowing policy, compatible with the country's economic and financial situation. In particular, it will show whether the structure and composition of the country's debt is optimum in terms of maturities, interest rate, exchange rate exposure and other related items. Such a review will also help identify opportunities for improving the debt portfolio, reducing future costs of borrowing and ensure that the right policies and strategies are taken so that future financing needs to support the Home-Grown Economic Reform Agenda remain sustainable at all times.

Against this backdrop, the specific objectives of this exercise have been:

- to review the debt situation in the light of recent macroeconomic developments,

- to critically examine the debt stock and flows with respect to major creditors and creditor types, major borrower types, commitment and disbursement trends, currency composition and, maturity structure of the debt and debt service and
- to propose elements of a strategy that would ensure the pattern and structure of borrowing are compatible with the country's development strategy while all along taking measures to avoid situations of debt and debt service stress in the future.

In view of that, the central government external debt refers to all external loans contracted between external creditors and Ministry of Finance while government-guaranteed external debt comprises of loans and suppliers credits contracted by public enterprises, mainly the Ethiopian Electric Power (EEP), Ethiopian Electric Utility (EEU), Sugar Corporation (SC), Ethiopian Railways Corporation (ERC) and Ethiopian Shipping and Logistics Services Enterprises (ESL) guaranteed by MoF.

The non-guaranteed external debt, on the other hand, includes loans contracted by public enterprises, mainly the Ethiopian Airlines (EAL) and Ethio-Telecom without government or government-owned bank guarantee. Domestic debt covers the debt of the central government in forms of government bonds, treasury bills and direct advance from National Bank of Ethiopia. In addition, the assessment covers State Owned Enterprises (SOEs) borrowing from both domestics as well as external sources including on-lent loans transferred to SOEs

The primary governing law for debt management is the Financial Administration Proclamation No. 648/2009 (as amended by Proclamation No. 970/2016) and the Financial Administration Regulations. Accordingly, debt shall be managed in such a manner as to prevent any negative impacts on the general economy, such as creating instability in monetary policy or balance of payments.

Accordingly, this report is issued by the Ministry of Finance in pursuant to section 52 of the Financial Administration law which requires the report to include inter alia:

- Annual government borrowings and debt management operations,
- Guarantee and lending activities of government,
- Debt management strategy and the rationale for the strategy,
- Debt accumulation trends,
- Outstanding amounts and beneficiaries of the loans and an assessment of the risks associated with the accumulation of debt.

This 2018/19 annual public sector debt report is structured as follows: part 1 introduces the report contents, part 2 analyzes macroeconomic performance in 2018/19, part 3 looks at the Medium Term Debt Management Strategy and its implementation and initiatives designed to ensure a well-structured portfolio and public debt sustainability, part 4 presents Government borrowings in 2018/19 and debt accumulation trends in public debt, part 5 presents contingent liabilities and on-lending loans, part 6 presents cost and risk analysis of Ethiopia's public and publicly guaranteed debt, and part 7 concludes the report with an outlook and forward-looking. A glossary part 8 is presented at the end of the report to facilitate a greater understanding of this report by the general public.

2. Macroeconomic Development in 2018/19

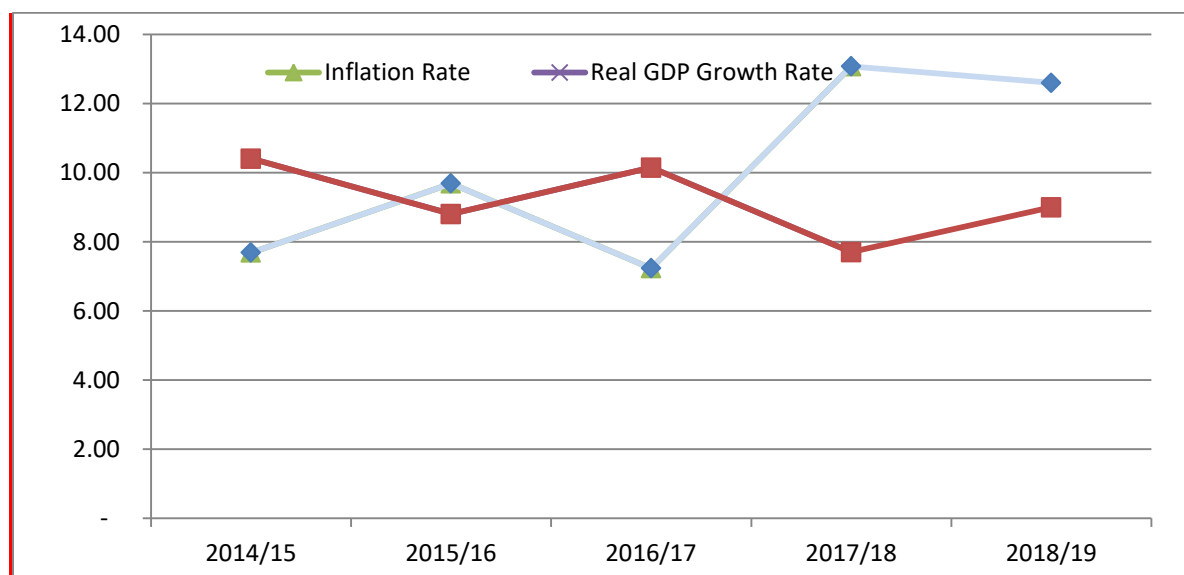
2.1. Gross Domestic Product (GDP)

Ethiopia's Gross Domestic Product has been grown by 9 percent in 2018/19 from 7.7 percent in 2018. Trends of economic activity growth continued in 2018/19, has shown improvement compared to the previous year. The economy has remained resilient despite multiple shocks arising from prolonged drought, lengthy political instability and global particularly external sector economic slowdown. This poor performance of the Ethiopian economy was largely due to the low growth of agriculture, external sector and industry.

GDP growth is still broad based, i.e. all sector recorded positive growth rates. Industrial production continued its positive trends registering 12.6 percent growth, as a result of

the growth of the manufacturing industry and construction sector's significant expansion of 6.8 percent and 20.3 percent respectively in 2018/2019. Services sector experienced an 11 percent growth while agriculture rose by 3.8 percent.

Figure –1 Real GDP Growth and Inflation Rate



2.2. Fiscal Policy

The level and financing of the budget deficit is designed in view of promoting the desired macroeconomic goals such as controlling inflation, boosting private investment and growth and maintaining external credit worthiness. The main thrust of fiscal policy in Ethiopia is to strengthen domestic revenue generation, effective and efficient allocation and utilization of the resources and maintaining fiscal deficit consistent with macroeconomic objectives. As a result during the years 2008/09-2018/19 on average over 80% of the government budgetary revenue has been mobilized from domestic revenue sources.

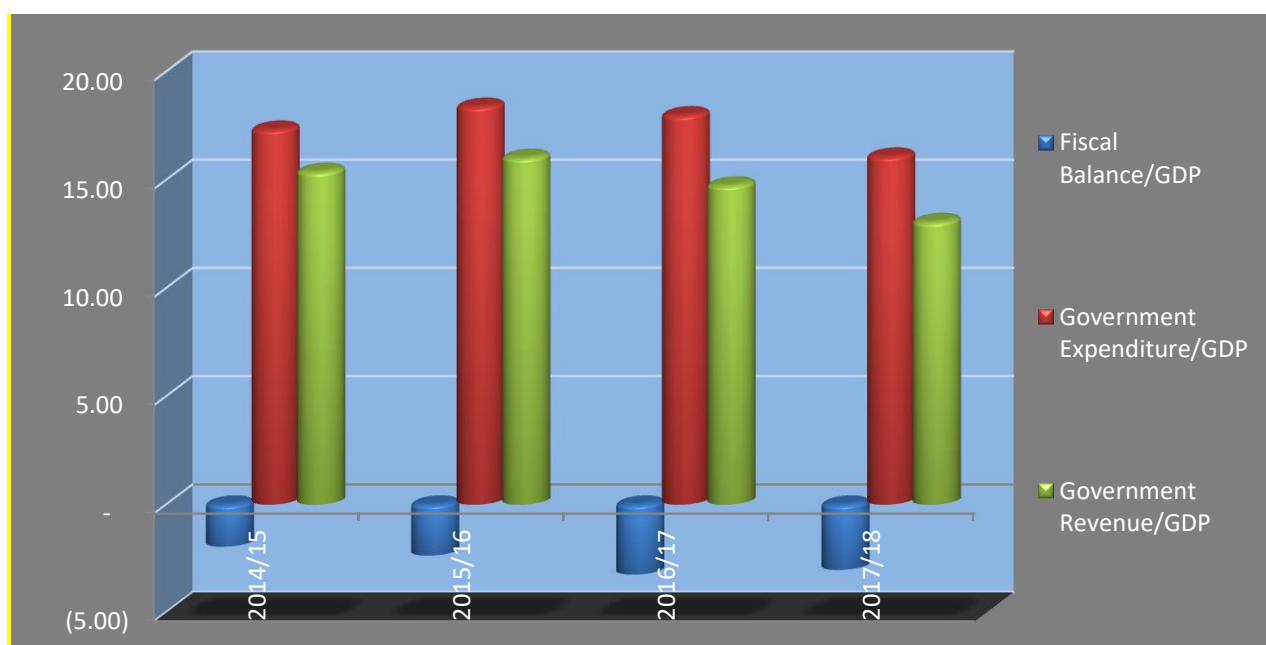
On the other hand, Government expenditure has been an important driver of Ethiopia's economy. The expenditure pattern was mainly focusing on allocating more resource for building economic and social infrastructure to provide basic services. To this end, in the

last many years the lion's share of the annual budget was devoted to capital expenditures which are critical in bringing future benefits through building physical assets and infrastructures, as well as promoting human resources development and research and development.

The Government over the past years capped the overall budget deficit at about 3 percent of GDP through a general fiscal rule. In fiscal year 2018/19, the overall budget deficit including grant turned out to be 2.5 percent of GDP. This was against a deficit target of 3.7% of GDP.

Figure 2. Fiscal Balance/GDP

MN USD



2.3. Inflation

Average moving consumer price index inflation rate in 2019 is amounted to 12.6%. Prices of food products had the most significant contribution to the increase of consumer prices.

2.4. External Sector

During 2018/19, total export of goods and service earnings reached USD 7.7 billion, showing 8.4 percent increased to last year. It shows an average growth rate of 6

percent in the last five years. Import of goods and service in 2018/19 was USD 20.7 billion increasing by 5 percent over the last year same period. Net private transfers increased by 4 percent over last year same period and amounting to USD 6.4 billion . The 2018/19 current account deficit amounted to USD 6.6 billion, higher than USD 6.4 billion of last year's same periods.

As figure 3, below shows overall balance in percent of GDP in 2018/19 is about 1.02 percent and current account in percent of GDP is about 4.9 percent and consistently shows modest change over the last five years

Figure 3. Overall Balance /GDP

In MUSD



3. Implementation of Medium Term Debt Management Strategy (2016-2020)

The ongoing GTP II needs huge resources. Accordingly, one of the sources to finance GTP II is borrowing from both, external and domestic sources. These borrowing activities need to be guided by internationally recognized framework for developing a

debt management strategy while ensuring that the public debt remains within sustainable levels.

In Ethiopia there is a clear coordinating mechanism at the political and technical levels as well as legislation and implementation circulars defining the parameters for debt contraction, guarantees and servicing. The existence of a clear legal framework is an important enabling element for formulating a debt management strategy.

To this effect, this (2016-2020) Medium Term Debt Management Strategy (MTDS), designed by the Ministry of Finance with the technical support of the International Monetary Fund (IMF) and a World Bank team provides a framework for developing an effective public sector debt management strategy that aims to achieve a desired composition of the public sector debt portfolio that reflects a cost-risk analysis and captures the government's preferences with regard to the cost-risk trade-off.

The objectives of the strategy remains two-fold: to raise resources through borrowing to meet central government budgetary requirements at minimum cost and prudent level of risk; and to promote the development of domestic debt markets. Potential sources of financing from abroad were identified by focusing from concessional sources, and strategies were designed in order to ensure that funding plans are achieved while minimizing the possible impact on the costs and risks of the debt portfolio.

This MTDS guided the past several years central government borrowing and providing guarantee to state owned enterprises in the medium term while providing a path for sustainable level of debt over the medium term. Accordingly, the Governments' fiscal strategies were geared towards maintaining a sustainable level of debt.

Moreover, the governments has put in place a robust system for monitoring and closely following up mechanism in order to maintain the transparency and accountability of public borrowing so that it is possible to ensure the level of public debt is consistent with the overall fiscal framework aimed at safeguarding macro-economic stability over the medium term.

The implementation of this strategy in the past several years including 2019 has led to some mixed results in the costs and risks factors associated with the debt portfolio. Accordingly, the Average Time to Maturity (ATM) of the public debt portfolio declined, the share of debt portfolio requiring refixing in one year increased, government exposure to debt denominated in foreign currency also increased and the proportion of debt maturing in a year increased.

The government has been taking appropriate measures to improve the debt situation of the country including curtailing borrowing from non-concessional sources. The measure underway with MoF leadership will lessen the burden of public debt both at the national level so as not to undermine economic growth.

4. Development of the Debt Portfolio in 2018/19

As illustrated in table below (Table 1) the total public and publicly guaranteed debt for FY 2018/19 rose USD 53,705 million which is 49 percent (in Present Value terms) of GDP of which 21 percent is external and 28 percent domestic. When we looked at the past five years trends total public debt outstanding (external and domestic), which was USD 34,322 million in 2014/15 has significantly increased to USD 53,705million (1.55 trillion ETB) in 2018/19 which is an increment of 56 percent over the period.

Table 1. Total Public Sector Debt Outstanding

MN USD

	2014/15	2015/16	2016/17	2017/18	2018/19
Total Public Sector Debt	34,321.66	39,401.50	45,782.53	49,340.39	53,705.83
External Debt	18,601.91	21,276.29	23,337.24	25,799.10	27,029.38
Domestic Debt	15,719.75	18,125.20	22,445.29	23,541.28	26,676.45

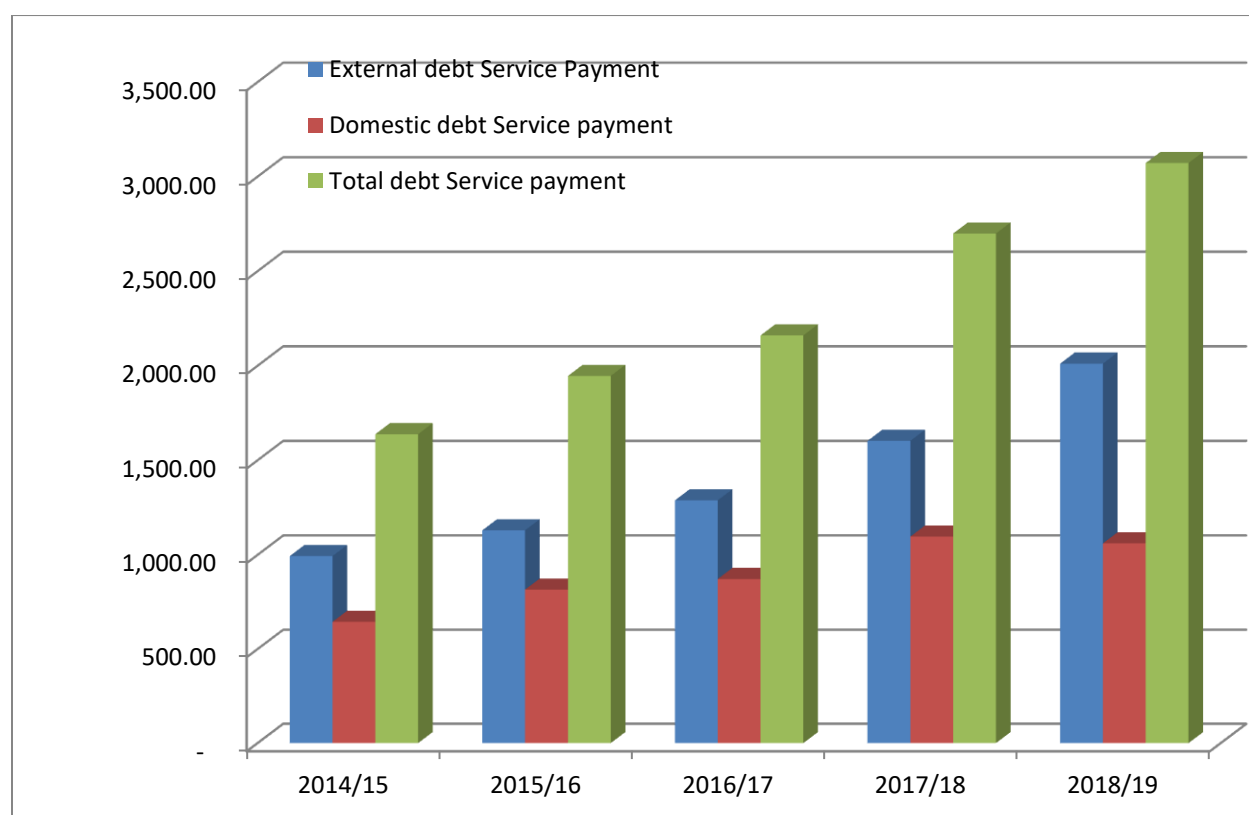
The average increment of total public sector debt during the observation period was 12% per annum the highest increment being recorded in 2016/17 where there was a

relatively higher external resources disbursement towards Central government, government guaranteed SOE projects and from domestic front there was a new issuance of 10 year non-interest bearing domestic bond to raise the capital of commercial bank of Ethiopia during the period. The exchange rate variation between 2014/15 and 2018/19 also have an impact on the change of stock of total public debt between each period.

The relative share of External debt out of the total public sector debt was about 54 percent in 2014/15 and consistently declined and currently it is about 50 percent. In FY 2018/19 the,external debt comprises 50.34 percent and of total public debt while the share of domestic debt is 49.66 percent. Over the period the total public sector debt outstanding magnitude increases and its composition changes from time to time and as a result of these the total public sector debt both external and domestic debt service payment almost doubled in the past five years by twofold.

Figure .4 Total Public sector Debt Service payment

MN USD



The table below shows two solvency indicators, present value of external debt to GDP, present value of External Debt to export and two liquidity indicators; external debt service to exports and external debt service to government revenues and Total public debt burden indicator total Public debt to GDP.

The rise in the external and Domestic Debt outstanding and change in the relative share of the total public debt deteriorated debt distress level of Ethiopia from moderate risk country to high risk country specially those export related debt ratios breached the threshold in the base line during the last three year, this can be partly explained as result of low performance in the export sector.

Table 2. Public Sector Debt Sustainability Baseline Scenario results¹

	2014	2015	2016	2017	2018
PV of External debt-to-GDP ratio	14.1	14.7	20.2	21.9	21.4
PV of External debt-to-Export ratio	109.1	125.6	206.1	280.9	247.9
PV of External debt-to-Revenue ratio	90	102	129.1	143.9	
External debt service -to-Export ratio	8.5	10.5	16.1	22.2	24.4
External debt service -to-Revenue ratio	5.4	5.7	6.4	9.1	16.4
PV of Public Debt-to-GDP ratio	30.9	33.8	42.6	46.3	49.7

As depicted in the above table Ethiopian baseline Debt sustainability result for 2018 shows that the PV of External Debt to GDP ratio is about 248 percent ,as Ethiopian Debt carrying capacity as assed by LIC-DSF is “medium”, and the tresholds for this group is 180 percent and Ethiopia’s baseline ratio breached the threshold of the group but it shows some improvement compared to last year’s ratio . The other ratio that

¹ **Thresholds to asses Ethiopia’s External Debt Distress Rating**

Present value of PPG external debt-to-GDP: 40 percent External debt service-to-exports: 15 percent

External debt service-to-revenue: 18 percent Present value of PPG external debt-to-exports: 180 percent

breached the threshold is also related to export ,the liquidity ratio , External debt service to export ratio for which the threshold is 15 percent while the result for Ethiopia is about 24 percent.Except this export related ratios the result for other ratio is well below the thresholds.

4.1 External Debt

This section covers trends in debt outstanding, a breakdown in debt by major creditor source and by borrower category. It also dwells upon trends in new commitments and disbursements as well as trends in net flows and transfers.

External Debt Outstanding:- Ethiopia's external debt stock which stood at US 18,601.91 million as of June 30, 2015 rise consistently and rose to US 27,044.73 million by end June 2019 which shows an increment of 45 percent . The increment of external debt stock in the last five years is partly attributable to larger net resource flows to both central government and state owned enterprises development projects.

Compared to the previous year in 2018/19 the stock of external debt increases only by 5 percent, as a result of declined government guaranteed external debt and only minimal increase on non-government guaranteed external debt. This can be partly explained by the recent government measure, to reduce external debt vulnerability, by reducing external borrowing from non-concessional sources to finance some of the state owned enterprise projects

4.1.1 External Debt Outstanding by Major Creditors Groups

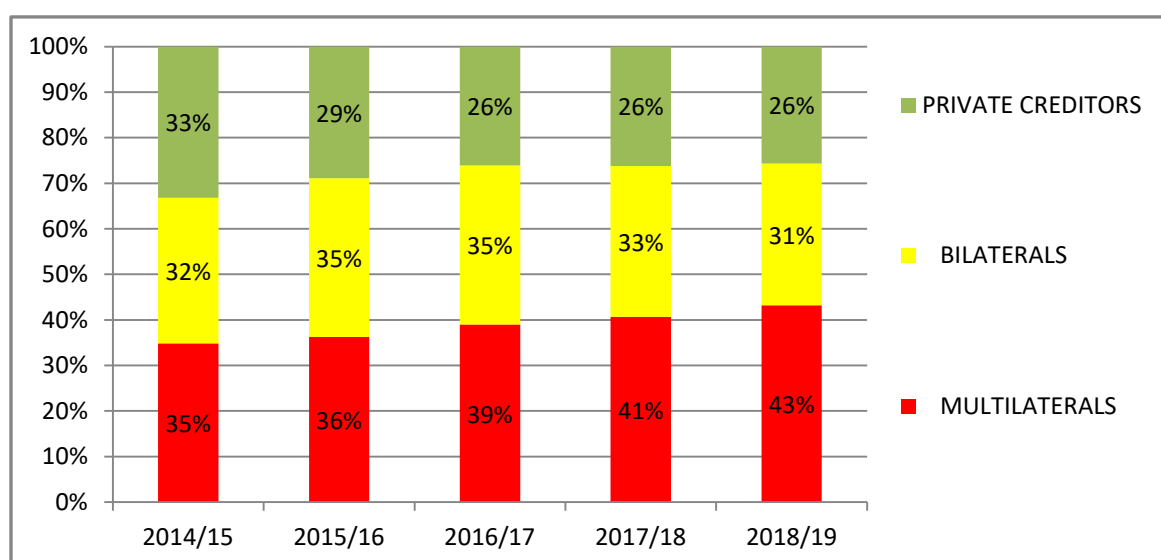
Over the years, Ethiopia has traditionally relied on official resources from multilateral and bilateral donors to finance its development projects and/or programs. Out of the total external debt outstanding as at June 30, 2019 USD 20,094.05million (74.4 percent) was owed to official creditors, of which 58 percent was owed to multilateral

and 42 percent to bilateral creditors. The rest USD 6,935.35 million (25.6 percent) was owed to private creditors, which constitute commercial banks and suppliers.

Between 2014/15 and 2018/19 the relative share of multilateral creditors has slightly increased while the relative share of bilateral and private creditors declined, as most of the SOEs owed debt are sourced from Bilateral and Commercial creditors in recent years borrowing from non-concessional sources of Bilateral and Commercial creditors is declining as the government limits its borrowing with its guarantee from these sources to contain debt vulnerabilities.

Multilateral Creditors:- The external debt stock owed to the multilateral financial institutions, which was USD 6,485.81 million in 2014/15 has consistently increased throughout the period and reached to USD 11,673.35 million in 2018/19 constituting an average growth rate of 13 percent. Currently this portion of debt currently represents 43 percent of the total external debt stock, among the multilateral creditors, IDA is still the dominant institution in terms of volume, making up almost 76 percent of the group and 33 % of the total External debt stock, followed by AfDF contributing 18 % of the group and 7 % the total debt stock.

Figure 5. Public Sector External Debt Stock by major Creditors in percent



Bilateral creditors:- The external debt stock owed to bilateral creditors has on average increased by 9.5 % per annum throughout the observation period. It has increased from USD 5,938.20 million 2014/15 to USD 8,530.95 million in 2017/18 then after it decline ,and in 2018/19 the external debt stock of Bilateral creditor amounted to USD 8,420.71.This was mainly attributed to decline in disbursement from the non-Paris club creditors specially from Exim-Bank of China.

Paris Club Creditors: - The debt owed to the Paris Club creditors as at June 30, 2019 amounted to USD 672.11 million. The share of the debt outstanding of this group is relatively very small and it shows very minimal change during the observation period. In recent years only Italy , France, South Korea and Japan are the only official creditors from the group that provide concessional loans.

Non-Paris Club Creditors: The debt owed to the non-Paris Club creditors has steadily increased from its level of USD 5,512.52 million in 2014/15 to USD 7,748.59 million in 2018/19. The average increase over the period was about 11 percent per annum and this was mainly due to an increase in new disbursements from different commercial creditors for EEP and ERC. But the relative share of the group out of the total debt stock is declining.

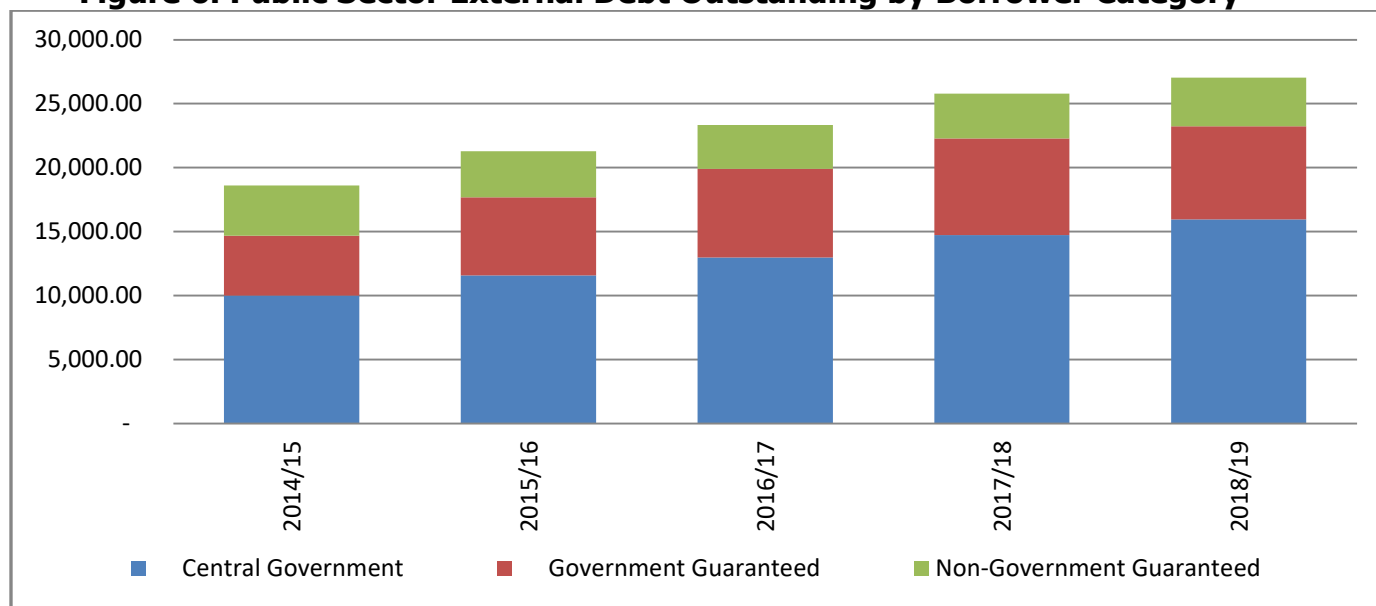
Private Creditors:- Private creditor outstanding, which was USD 6,117.90 million as at June 30, 2015, has steadily increased through the observation period and reached to USD 6,935.35 million in 2018/19. The reason for this rise is mainly due to new disbursements for Ethio-Telecom, suppliers' credits to EEP and ERC and new aircrafts purchase by EAL.

4.1.2 External Debt Outstanding by Borrowers' Category

The relative share of central government external debt stock was 54 percent in 2014/15 and has increased to 59% in 2018/19. As it is indicated in the figures below, it shows a persistent increment in absolute terms during the period. The share of the stock of government guaranteed increased up to 2017/18 and then in the next one year a

decline in its relative share has been observed as a result of less new borrowings from external sources, particularly by EEP, ERC and SC.

Figure 6. Public Sector External Debt Outstanding by Borrower Category



The non-government guaranteed external debt stock contracted by, Ethio –telecom and EAL showing a persistent decline over the last five year from a high of about 21 percent between in 2014/15 to a low of 14 percent in 2018/19 this as a result of less new borrowing by Ethio-telecom in recent years. The nominal external debt in percent of GDP is between 29 percent and 32 percent over the observation period while the PV of External debt in percent of GDP is about 22.1 percent which is much lower than the 40 percent threshold of the country.

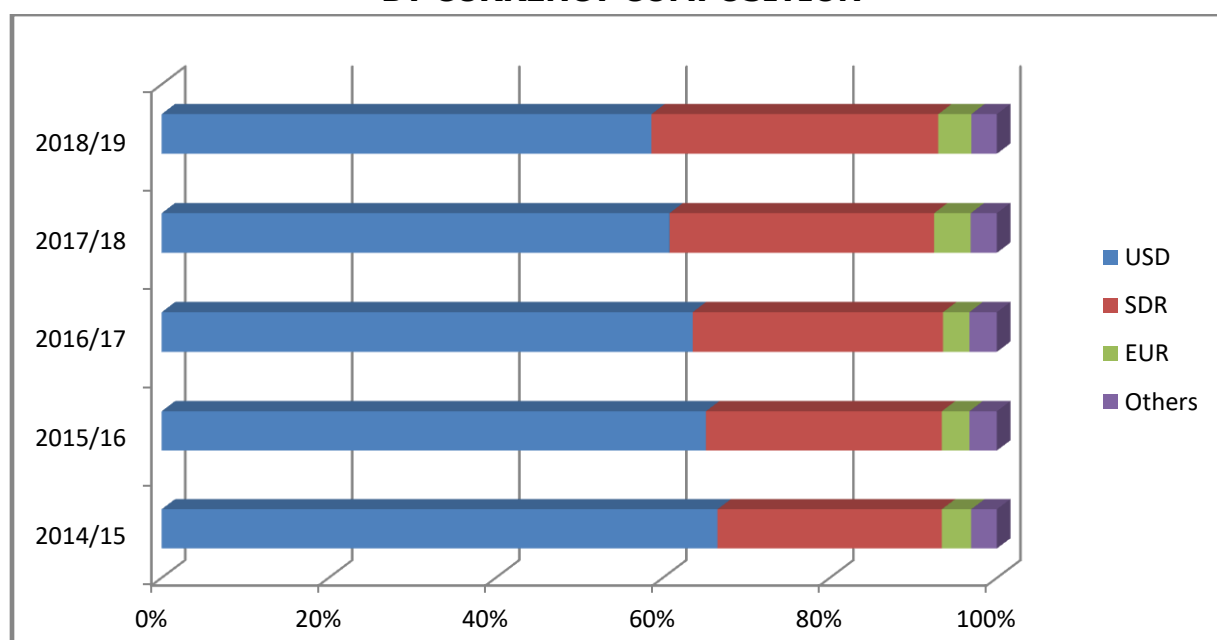
4.1.3 Public Sector External Debt Outstanding by Contracting Currency

External loans are contracted from different creditors and in different currencies. Since the currency composition of any debt portfolio can have a serious bearing on a country's debt obligations, it is considered appropriate for borrowing to take place in a proper mix of currencies, hence minimizing the exchange rate risks. In order to mitigate the negative impact of the volatility of exchange rates, countries usually prefer to match

as close as possible the currency composition of their external debt with that of their foreign earnings or reserves.

Accordingly, out of the total debt outstanding in 2018/19, 59 percent, 34 percent, and 4 percent was denominated in USD, SDR and EURO, respectively, while the remaining 3 percent was denominated in various currencies including Japanese Yen, Kuwaiti Dinar and Chinese Yuan (CNY). During the period the relative share of SDR denominated has increased between 2014/15 and 2018/19 mainly due to huge disbursement from IDA which use SDR² as a loan currency, while that of USD declined. The share of USD denominated debt has declined from 67 percent in 2014/15 and reached about 59 %, as a result of a decline ,in recent years , the new borrowing and disbursement for the EEP, ERC, SC and Ethio Telecom, that are denominated in USD.

**Figure 7. PUBLIC SECTOR EXTERNAL DEBT OUTSTANDING
BY CURRENCY COMPOSITION**



4.1.4 Terms of Borrowing

The terms of borrowing generally refer to the maturity period, the grace period and the interest rate of a loan. Taken together, they determine the level of concessionality of a

² SDR is a basket of five currencies USD, EUR, CNY, JPY and GBP with a weight of 41.73, 30.93, 10.92, 8.33 and 8.09 respectively and the share of these five currencies is much higher than the above chart.

debt portfolio. In this regard, an analysis of the evolution of the average terms of borrowing is important in evaluating a country's pattern and cost of borrowing.

4.1.4.1 External Debt Outstanding by Interest Rate Composition

Determining the interest rate structure of the debt portfolio is important in order to assess the possible impact of any change in interest rates. This is particularly the case for a debt portfolio which has a large proportion of the debt bearing variable interest rates. The variable interest rates which are linked to market rates such as LIBOR may be attractive when the base rates are low or are expected to take a declining trend, they may also suddenly rise following changes in economic fundamentals and result in an increase in the debt service burden.

As at June 30 2019, 66 percent of the outstanding loan was contracted on fixed interest rate while the remaining 34 percent was contracted on variable interest rates. It is important to note that more than 83 percent of the stock of external debt of SOEs is on a variable interest rate namely on LIBOR six months and LIBOR three months with some margin. Similarly, about 99.7 percent of the that of Central government is on fixed interest rate only 0.3 percent of central government external debt stock is with LIBOR 6 months with margin .Most of the external debt of EAL is with three month Libor rate plus margin while other SOEs borrow on six month Libor rate plus margin. In recent months, as the LIBOR is declining thus external debt service payment of SOE's to their respective creditors is relatively lower than their payments before six months.

Table 3. External Debt Outstanding by Interest rate Composition

MN USD

	2014/15	2015/16	2016/17	2017/18	2018/19
Central Government Total	9,994.91	11,581.52	12,981.38	14,742.54	15,931.58
Fixed Interest rate	9,994.91	11,581.52	12,980.82	14,709.64	15,887.09
0 % - 0.99 %	6,340.02	7,696.06	8,965.90	10,443.49	11,735.36
1% - 1.99%	1,011.66	1,019.01	996.78	967.12	914.24
2% - 2.99 %	1,430.70	1,656.03	1,809.70	2,091.56	2,031.90
3% - 5%	167.63	165.53	163.55	162.57	160.70
Above 5%	1,044.90	1,044.90	1,044.90	1,044.90	1,044.90
Variable Interest Rate	0	0	0.56	32.90	44.49
Libor 6 Months + Margin	0	0	0.56	32.90	44.49
Other Public sector Total	8,607.06	9,694.85	10,355.90	11,056.56	11,097.80
Fixed Interest rate	1,034.80	1,184.92	1,236.63	1,464.28	1,878.66
0 % - 0.99 %	243.56	194.96	141.93	91.33	38.10
2% - 2.99 %	-	-	31.48	34.11	57.03
3% - 5%	733.64	938.46	1,025.54	1,177.56	1,613.97
Above 5%	57.61	51.50	37.69	161.29	169.56
Variable Interest Rate	7,572.26	8,509.93	9,119.28	9,592.28	9,219.14
Libor 3 Months + Margin	2,048.83	1,788.74	1,690.21	1,620.79	1,624.67
Libor 6 Months + Margin	5,523.43	6,721.19	7,429.07	7,971.50	7,594.46
Grand Total	18,601.97	21,276.37	23,337.28	25,799.10	27,029.38

The proportion of external debt with fixed interest rate was 59 percent in 2014/15 and has since increased to 66 percent in 2018/19 as a result of a relatively huge disbursement towards Central government from its multilateral and bilateral creditors, who mostly lends on fixed interest terms as a result the outstanding debt with fixed interest rate has increased, while the share of external debt with floating interest rate declined in the observation period declined continuously from 41 percent in 2014/15 to

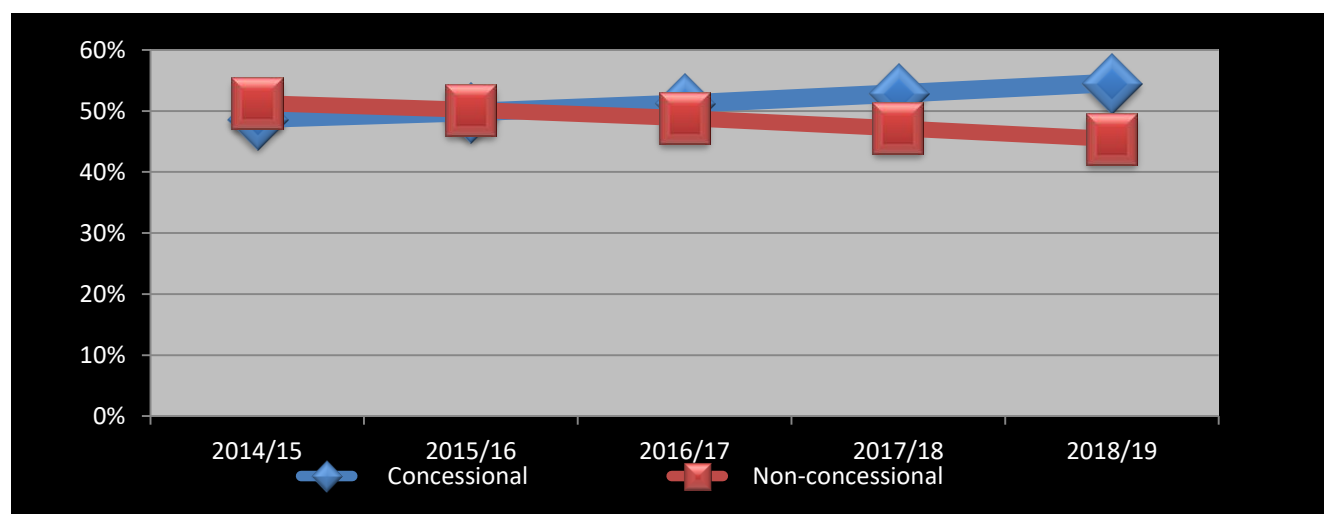
34 percent, and this can be explained partly by the reduction in borrowing by SOE's from their creditors with guarantee of the government. Out of the total debt outstanding in 2018/19, about 47 percent carries interest rates below 2.0%.

4.1.4.2 External Debt Outstanding by Concessionality.

A conventional measure of the concessionality of a loan is the grant element, which is influenced by the following three main factors: the maturity period, the grace period and the interest rate on the loan. Loans with long grace and maturity periods, and low interest rates usually have high grant elements. By convention, loans with a grant element of 35% or above are considered to be concessional.

During the observation period not only the magnitude of the external debt outstanding changed but also a significant change in its composition also occurred. Out of the total external debt outstanding the percentage share of concessional debt as at 2014/15 was 49 percent and that of non-concessional was about 51 percent. Then after the relative share of concessional debt increased, while that of the non-concessional debt decline continuously. It is important to note that in 2014/15 the share of non-concessional debt was higher due to the issuance of Eurobond and higher disbursement to SOEs from commercial creditors. Currently the relative share of concessional loan out of total external public debt is about 55 percent, this could be explained partly by the recent measure taken by the government towards decreasing borrowing from non-concessional sources, as per the non-concessional borrowing limit of the world bank.

Figure 8 Public Sector External Debt Outstanding by Concessionality



4.1.5 New Commitments from External Sources

During the past five year, which coincide with the last year of GTP I and the first four years of GTP II, the total amount of external loans contracted from multilateral, bilateral and private creditors amounted to USD 17,837.89million of which 69 percent for the central government and the remaining 31 percent for SOEs to implement various mega projects .

The commitments from multilateral source mostly contracted from IDA and ADF which is about 44 percent, with highly concessional terms while the majority of bilateral were secured from the concessional and non-concessional windows of Exim-Bank of China and ICBC . On the other hand the external debt commitments from the private creditors are mostly from suppliers of China, and commercial creditors of EAL and the debut Eurobond issued in 2014.

External new loan commitment has declined from its highest in 2014/15 which was about USD 4,693 million to the lowest USD 2,633.12 million in 2018/19, this is the result of the government measure to reduce non-concessional borrowing by SOE through government guarantee, particularly during 2018/19 declined visibly that is

due to decline in new commitment by SOEs from their non-concessional bilateral, commercial and supplier's creditors.

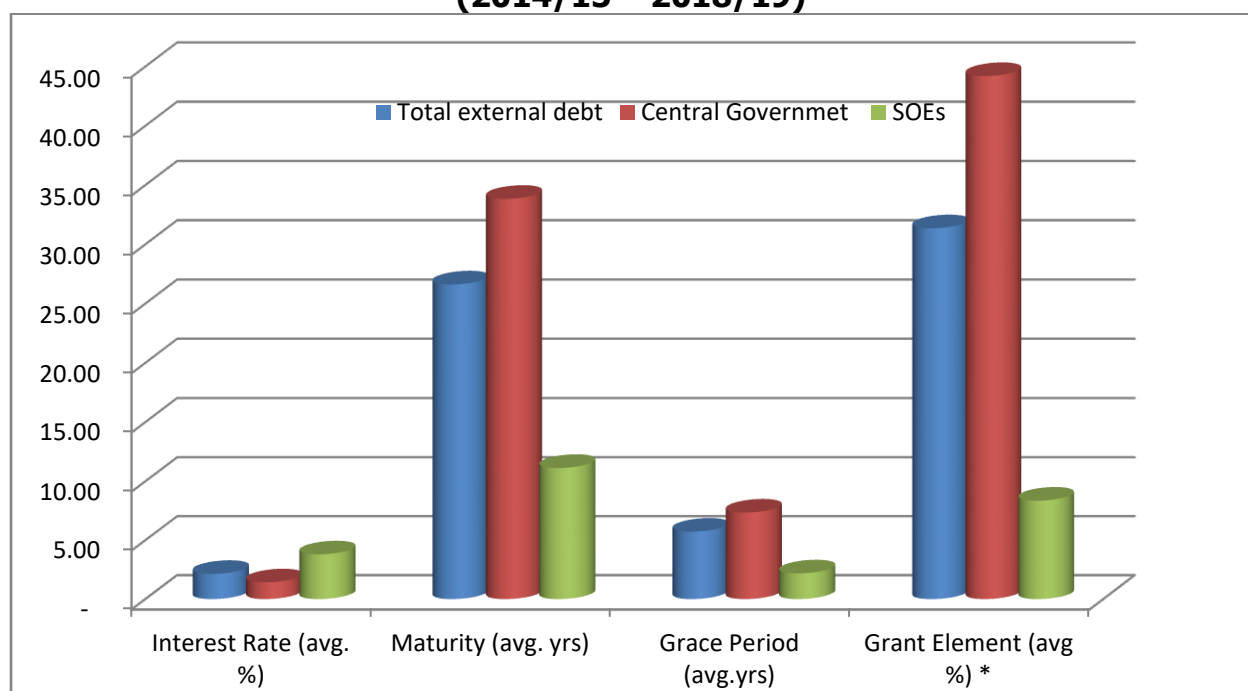
As depicted in the Table 3 below, about 48 percent, 26 percent and 26 percent of the committed amount in the past five years was from multilaterals, bilateral and private creditors respectively. IDA is the dominant development partner for the country in the past five years. The total new commitment from this development partners is about USD 7.2 million of which is about 41 percent of the total external new commitment during the period. Of course, AfDF contribution is about 4 percent and about 6 percent from Paris club creditor with ODA terms. This shows that about half of the borrowings in the past five years are made from highly concessional sources.

Table 4 New External Debt Commitments by Creditors

	MN USD				
CREDITOR	2014/15	2015/16	2016/17	2017/18	2018/19
CENTRAL GOVERNMENT	2,681.64	2,388.59	3,162.12	2,165.87	1,832.51
MULTILATERAL	1,544.21	2,189.85	1,445.02	1,831.02	1,419.21
ADF	131.51	254.83	72.69	86.77	
ADB		76.11	104.61		
EIB		42.4	77.79		34.01
IDA	1,374.70	1,773.27	1,006.17	1,744.25	1,343.20
IFAD		43.24	98.76		
BADEA	13	0	35.00		20
OFID	25	0	50.00		22
BILATERAL	1,137.43	198.74	1717.10	334.85	413.30
NON-PARIS CLUB	50	0	1470.97	251.28	0
GOVERNMENT OF CHINA	0	0.00	0	84.28	0
SAUDI FUND	0	0.00	0	0	0
EXIM-BANK OF CHINA	0	0.00	1,470.97	167	
GOV. OF POLAND	50	0.00			
PARIS CLUB	87.43	198.74	246.13	83.57	413.3
GOV. OF FRANCE (AFD)	62.83	22.06	175.58	83.57	95.7
GOV. OF ITALY	24.6	49.33	21.95		53.6
GOVERNMENT OF JAPAN	0	0.00	48.6		
EXIM-BANK OF KOREA	0	127.35			264
BOND HOLDERS	1,000.00				
STATE OWEND ENTERPRISE	2,012.19	880.29	779.12	1,134.95	800.61
MULTILATERAL	0	0	158.82	0	0
ADB	0	0	158.82	0	
BILATERAL	0	580.00	38.26	171.22	0
NON-PARIS CLUB	0	580	38.26	171.22	0
CHINA DEVELOPMENT .BANK	0	30.00	0	0	
EXIM-BANK OF CHINA NON-CONCESSIO	0	0.00	38.26	171.22	
IDUSTRIAL AND CONSTRUCTION BANK OF CHINA		550.00	0	0	
PARIS CLUB	0	0.00	0	0	0
GOV. OF FRANCE (AFD)	0	0	0	0	
PRIVATE CREDITORS	2,012.19	300.29	582.04	963.73	800.61
BANK OF CHINA LIMITE	0.00		18.29		
ZTE	0	0			
ERICSSON	400	0			
HUAWEI	0				
JP MORGAN BANK	335.17				
EXPORT CREDIT BANK OF TURKEY	300				
CREDIT SUISSE AG	865		466.45		
CHINA ELECTRIC POWER	74.81	74.49			
UNICREDIT	0			402.76	
KFW	37.21	0			
TD SECURITIES (USA)	0				
BANK HAPOLIN B.M. (ISRAEL)	0	225.8			
STANDARD BANK OF SOUTH AFRICA	0		97.3		
STANDARD CHART BANK(GB & AIRLAN	0			120	
THE EXPORT PK				125	
CREDIT AGRICOL TOKYO(JAPAN)	0			144.54	
EXPORT NOVUS AVATION(UAE)	0			15	
ING CAPITAL LLG(USA)	0			121.43	248.37
EXPORT INVESTEC BANK				35	10
MUFG BANK LTD					272
NAT WEST BANK	0			0	270.24
GRAND TOTAL	4,693.83	3,268.88	3,941.24	3,300.82	2,633.12

The chart below shows average loan terms and the average grant element of total external debt contracted in the past five years shows about 32 percent grant element which is lower than the IMF 35 percent benchmark. But the grant element for the central government which constitutes 67 percent of the total new borrowing from external source in the past five years was about 44 percent which is well above the IMF's concessionality benchmark.

**Figure 9 Average Loan Terms of External Public Debt
(2014/15 – 2018/19)**



4.1.6 Public Sector External Debt Disbursements in the Period

An analysis of the disbursement profile is important in debt management as it provides an indication of the magnitude of actual resource inflow to a country and the rate at which such resources have been actually used. In assessing the flow of investment resources, two important parameters are used, namely Net-Flows, i.e. disbursements less principal repayments in a given period; and Net-Transfers, i.e. disbursements less principal repayment less interest payments, includes other charges. If the two parameters are positive, it means that the country is a net recipient of external

resources and vice versa. Countries with a large share of commercial debt usually experience low or negative net resource transfers as a result of large interest payments.

In this regard, the knowledge of evolving trends in both net resource flows and transfers can be very useful in developing sound borrowing strategies.

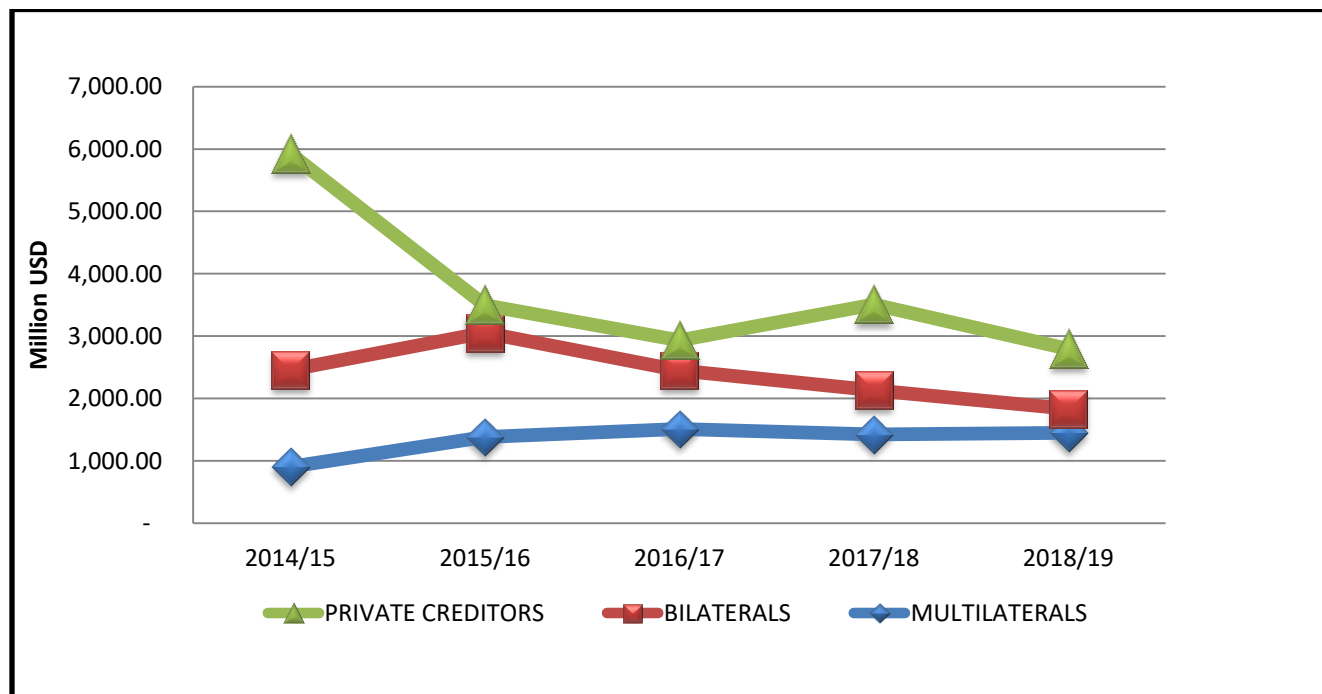
When we look at the trends the external debt disbursement to various projects of the central government and state owned enterprises it increased by USD 18,655.00 million over the five years. External resource inflow to projects has exhibited a decline in the past five years; on the average it declined annually by 14 percent. During 2014/15 there was the highest external debt disbursement (USD 5,925 million) that has been recorded in the debt data of the country. This was mainly associated with significant disbursements from bilateral and private creditors including issuance of USD 1 billion Eurobond.

Out of the total amount disbursed during the period, USD 2,780.7182 million disbursed in 2018/19, out of which about 66 percent were from official creditors while the remaining balance 33 percent was from the private creditors. The beneficiary of the disbursement of external loans during 2018/19 was central government with 55 percent and the remaining 45 percent was for SOE's.

4.1.6.1 Public Sector External Debt Disbursement by Major Creditors

Out of the total disbursement during the fiscal year of 2018/19, USD 1,432.95 million (52%) was from multilaterals sources while USD 386.00 million (14%) was from bilateral creditors with the balance 34 percent coming from commercial banks and suppliers. During 2018/19 the largest disbursement was obtained from IDA and creditors from China making up 45 percent and 11 percent of total external debt disbursement respectively.

Figure 10. Gross Public Sector External Debt Disbursement by Major Creditor



4.1.6.2 Disbursement by Economic Sector

The main objective of analyzing the composition of disbursement and debt by economic sector is to identify the sectors to which the contracted loans have been channeled, and in particular, to examine whether they are compatible with the country's development strategy.

Accordingly, in the last five-year period, the largest proportion of the disbursed resource was allocated to highway and railway transport infrastructure (28%) followed by electricity gas and steam (17%), air transport and telecommunication, disbursement to Ethio-telecom and EAL (17.5%) sector, Industrial sector the major being sugar (13%), agriculture 8.7% and basic services (4.3%). This shows that the external resource inflow allocation mainly for the development of infrastructure so as to enhancing expansion and ensuring quality of the infrastructural capital of the country as stipulated in both GTP I and II.

Table 5. Public Sector External Debt Disbursement by Major Economic Sector

Economic Sector	2014/15 ^R		2015/16 ^R		2016/17 ^R		2017/18 ^R		2018/19 ^P	
	USD	%	USD	%	USD	%	USD	%	USD	%
GRAND TOTAL	5,925.47	100.00	3,498.05	100.00	2,930.55	100.00	3,505.11	100.00	2,804.43	100.00
<i>Agriculture</i>	109.60	1.85	502.42	14.36	519.76	17.74	237.50	6.78	249.84	8.91
<i>Financial Sector</i>	-	-	30.00	0.86	-	-	12.32	0.35	607.26	21.65
Transport & communication	1,408.59	23.77	111.91	3.20	262.50	8.96	581.63	16.59	900.46	32.11
Highway and Railway Transport-Infrastructure	1,784.80	30.12	1,597.63	45.67	823.37	28.10	728.44	20.78	262.96	9.38
Electricity, Gas & Steam	951.71	16.06	510.73	14.60	498.73	17.02	998.66	28.49	199.75	7.12
<i>Industry & Tourism</i>	1,142.69	19.28	387.53	11.08	422.99	14.43	255.82	7.30	215.49	7.68
Education & Capacity Building	15.13	0.26	27.47	0.79	106.93	3.65	134.44	3.84	56.91	2.03
<i>Health</i>	26.72	0.45	5.40	0.15	6.55	0.22	74.58	2.13	30.48	1.09
Public and Social Admin	169.99	2.87	90.65	2.59	104.39	3.56	100.92	2.88	112.06	4.00
Water Works & Supply	90.78	1.53	121.96	3.49	94.09	3.21	125.25	3.57	58.82	2.10
<i>PBS</i>	225.46	3.80	112.36	3.21	91.25	3.11	255.53	7.29	110.41	3.94

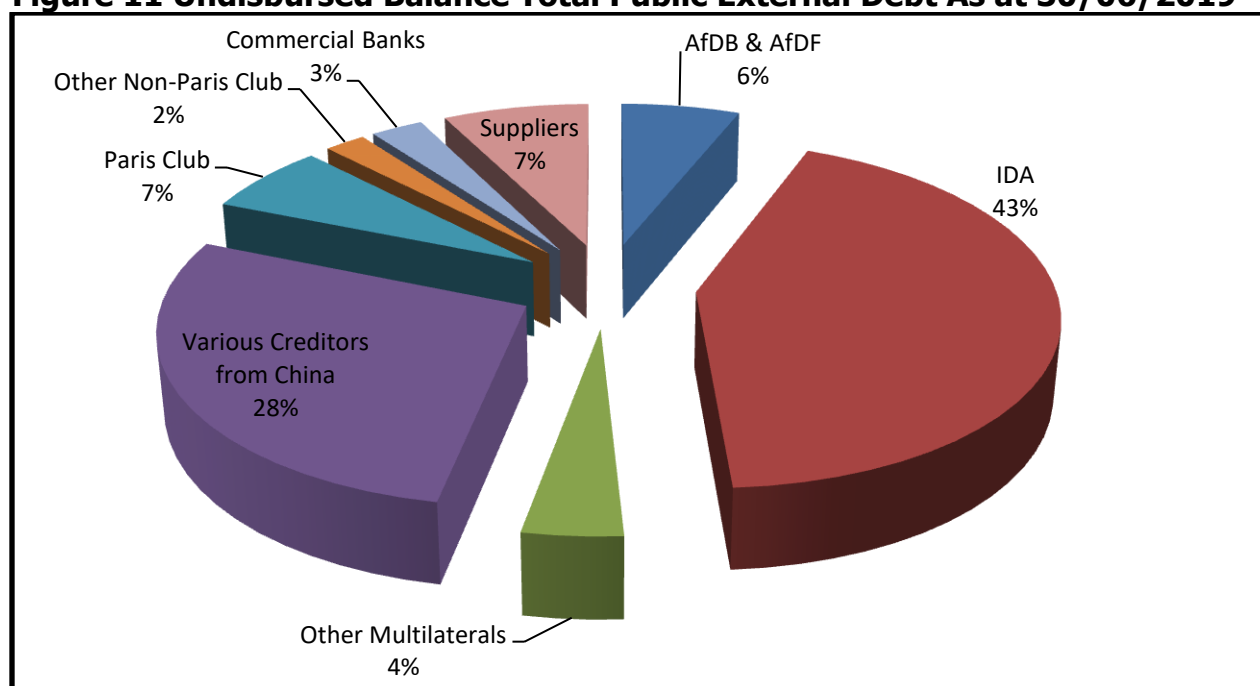
4.1.7 Public Sector External Debt Undisbursed Balances

The disbursement rate (or rate of loan utilization) is determined by several factors - institutional and non-institutional. This rate varies depending on the use of the borrowed funds as well as the creditors involved. In terms of use of funds, programme, commodity and cash loans normally take a short period to disburse. By contrast, the disbursement period for project loans is usually longer.

Delays in loan utilisation can be costly both in terms of the payment of commitment charges on the undisbursed balance, and delayed economic benefits from the projects being implemented. It is therefore important for a debt manager to review the rate of loan utilisation in order to verify whether the low rate of utilisation is because of genuine disbursement problems that require action to be taken, or it is simply a result of incomplete information on the level of disbursement that actually took place.

As at the end of June 2019, the undisbursed balance from external loan commitments was USD 9,041.49 million of which from multilateral creditors IDA and AfDB have very large undisbursed balances, amounting to USD 3,884.38 million (43 %) and USD 553.51 million (6%), respectively. Out of bilateral creditors the undisbursed amount from different Chinese Banks including Exim-Bank China, CDB, ICBC and Government of China) is the second highest and was about USD 2,542.22 million (28%). The accumulation of undisbursed balance from creditors such AfDB, Exim-Bank of China, Exim-Bank of India, Exim-Bank of Korea and AFD needs strict follow up because the delay of projects financed by these creditors may entail extra commitment fee payments.

Figure 11 Undisbursed Balance Total Public External Debt As at 30/06/2019



As indicated earlier, one implication of a low overall disbursement rate is delayed project completion and hence delayed economic benefits to the country. Given this relatively low disbursement rate for most creditors, executing agencies will be consulted to examine the cause for the slow pace at which the borrowed resources have been utilised, and in particular implementation issues such as those pertaining to:

- allocation of matching funds in the budget for externally funded projects: budgetary constraints usually lead to unavailability of matching funds for externally funded projects;
- procurement procedures: complex procurement procedures may not be easily understood by implementation agencies and can result in unnecessary delays in the implementation process; and
- country's implementation capacity, especially in line ministries.

4.1.8 External Debt Service

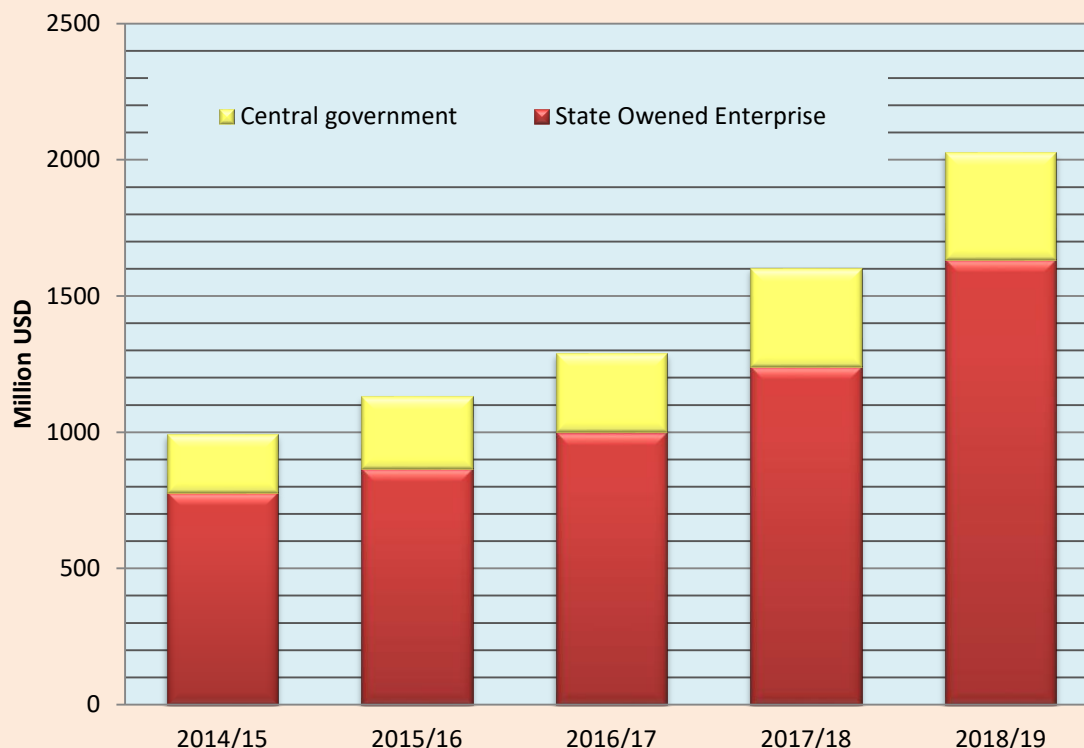
So far this review has dwelled specifically on the evolution of the structure and composition of Ethiopia's existing external debt stock, inflows and new commitments. This section highlights the recent trends in the country's external debt service profile and analyses its debt service obligations in the medium-term, with respect to its existing debt (and commitments).

Accordingly, total external debt services that have been effected in the last five years amounted to USD 7,040.36 million (ETB 174,090.64 million). Out of the total external debt service payment only USD 1,519.17 million (21.5%) is central government's payments to its multilateral, bilateral creditors and interest payment to the Eurobond holders, while the remaining 78.5 percent payment was done by SOEs to their respective creditors. The total public sector debt service during the past five years shows an average annual growth rate of 19 percent, for this big overall annual growth the contribution of SOEs debt service payments increment is much higher than that of central government. In recent years the external debt service payment by the SOE is

rising up as a result of maturing principal payments of most SOE's external loans. Out of the total Debt Service payment effected in the past five years 70 percent is made up of principal and the remaining 30 percent for interest, commitment fees and other Payments.

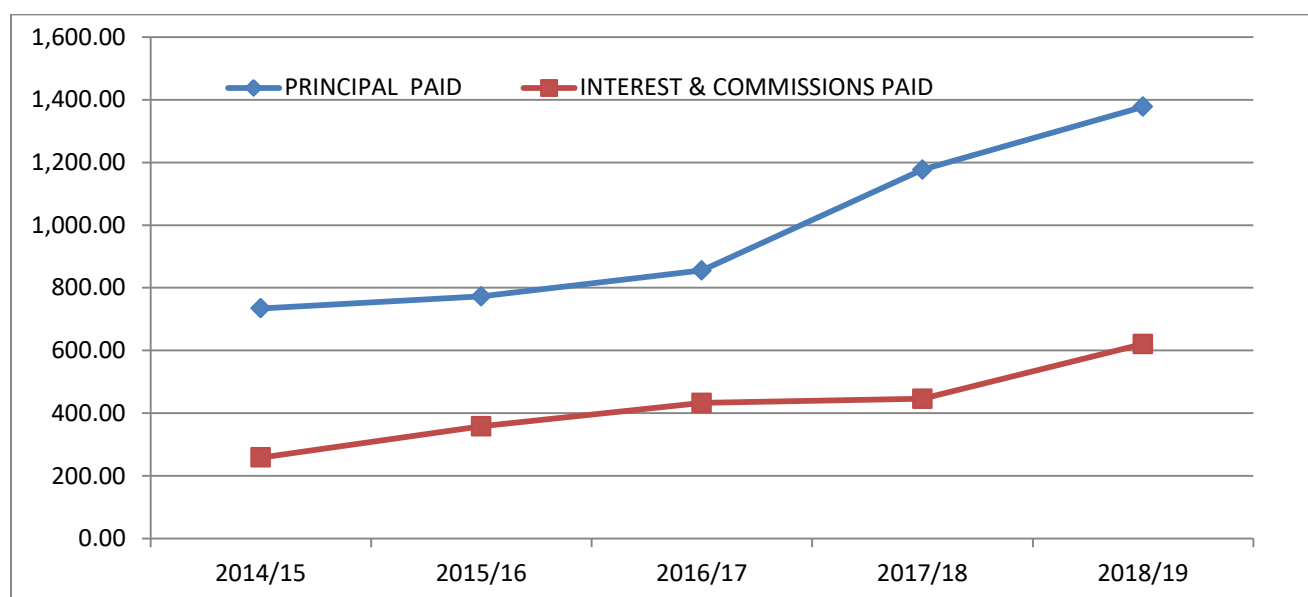
Figure 12. Public Sector External Debt Service Payments

Mn USD



Total external debt service payment in 2018/19 amounted to USD 2,026.16 Million (ETB 57,850.62 million) of which principal payment was USD 1,403.46 million (69 %) while the payment for interest and commission was USD 622.61 million (31%). As a result of the ETB devaluation against USD in October 2017, the external debt service in terms of ETB has risen significantly since 2017/18. As indicated in the Figure 12 the general trend in debt service payment shows significant increase throughout the observation period. Especially since 2016/17 the principal payment increment was visible this can be partly explained by maturing of most of SOE's borrowing from their commercial creditors.

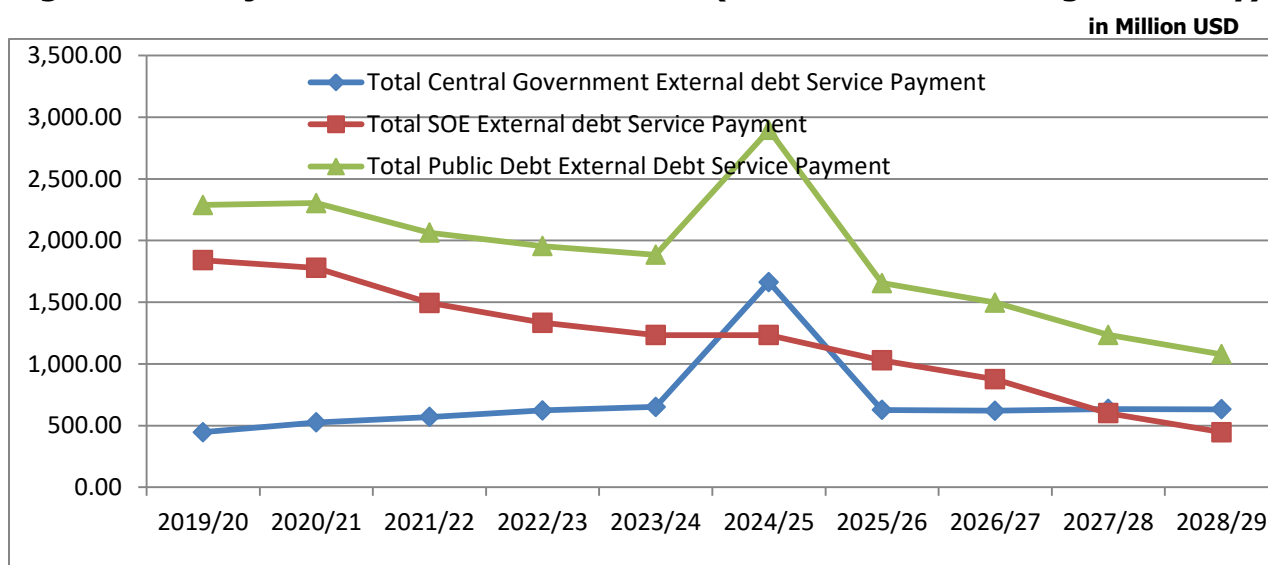
Figure 13. External Debt Service Payment by Principal and Interest



4.1.8.1 Projected External Debt Service

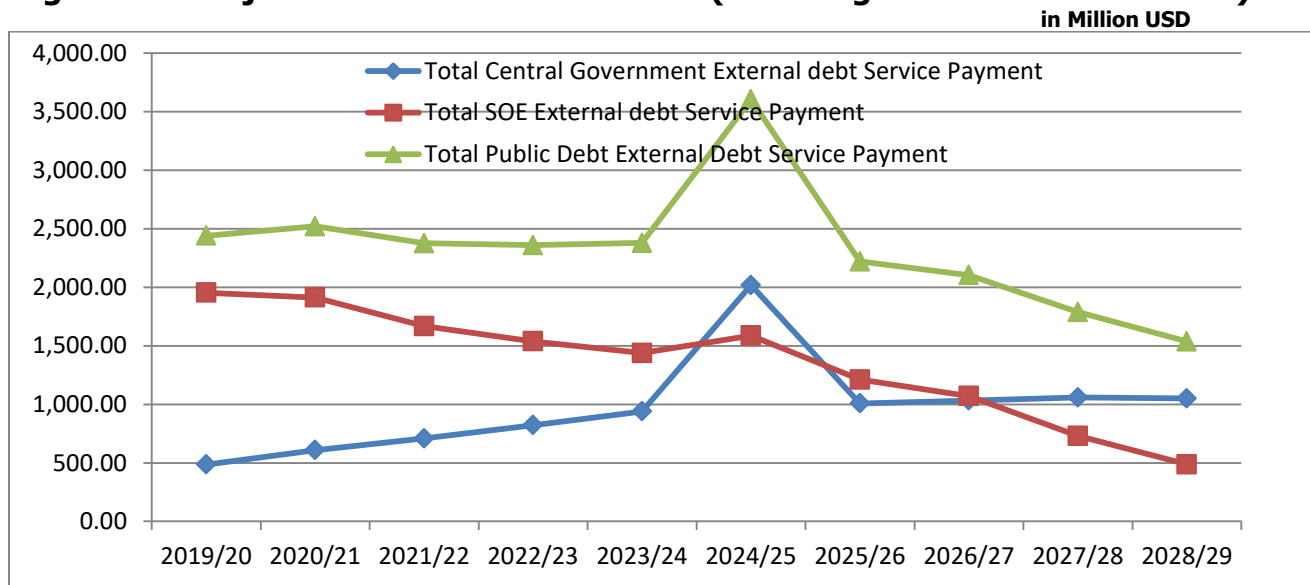
Projected external debt service, based on the June 30, 2019 debt outstanding (by not considering future disbursements) exhibits declining trend for the coming five years from about USD 2 billion in 2019/20 to USD 1.8 Billion in 2023/24, before it starts to move upward and reaches about USD 2.9 billion in 2024/25 because of maturing Sovereign Bond. The contribution of SOE's external debt service payment to the total external debt service is much higher than the central government external debt service but has shown a declining trend over the period, this can be explained by short term maturity structure of most of the SOE borrowing and almost no non-concessional borrowing except EAL in recent years. On the other hand the central government external debt service payments grow continuously throughout the observation period.

Figure .14 Projected External Debt Service (Based on Outstanding Debt Only)



Assuming that the committed and undisbursed amount will be disbursed over the coming years, total projected external debt service will decline from USD 2.4 billion in 2019/20 to USD 2.3billion in 2023/24. Then after, it increases to about 3.6 billion in 2024/25 because of maturing Sovereign Bond.

Figure-15. Projected External Debt Service (including Future Disbursements)



4.1.9 Net Resource Flows & Net Transfers

Gross disbursement less amortization (Disbursement minus Principal Payments) during the last five years net resource flows is declining, but it was positive with relatively higher magnitude in earlier years. It implies that the disbursement from external creditors, towards projects is much higher than matured principal payments to the creditors in the earlier years especially in 2014/15. In particular the central government net resource flows is much bigger than that of the other public sectors except in 2014/15, where there was a huge disbursement for SOEs from various creditors. The net resource flows on behalf of the SOEs shows a declining trend, as most of the ongoing projects are in final stages, thus the level of new disbursement is declining from time to time and some of the SOEs have also started to repay their principal payments. On the other hand, the net resource flows towards government especially from multilateral sources shows an increasing trend in the observation period. The net flow from private and Bilateral creditors in 2018/19 was negative this is due to a relatively lower new disbursement compared to the size of amortization to private creditors.

Table 6. Net Resource Flows on Public Sector External Debt **Million USD**

	2014/15	2015/16	2016/17	2017/18	2018/19
Total Central Government	2,123.92	1,633.15	1,420.63	1,650.66	1,340.58
Multilateral	856.83	1,330.33	1,300.94	1,355.20	1,373.88
<i>of which IDA (World Bank)</i>	714.27	1,084.67	1,024.47	1,104.62	1,220.91
Bilateral	267.09	302.81	119.69	295.46	-33.29
Private-Euro Bond Holders	1,000.00	0.00	0.00	0.00	0.00
Total Other Public Sector	3,067.02	1,092.29	654.69	677.31	77.71
Bilateral	1,119.60	1,096.80	529.85	86.74	-35.53
Private Creditors (Commercial Banks and suppliers)	1,004.80	369.98	353.68	575.08	-154.99
Grand Total	5,190.94	2,725.44	2,075.32	2,327.97	1,418.30

Net Resource Transfers (Disbursement minus Principal Payments minus Interest Payments). Net transfer is net flows less interest and commission payments (Disbursement minus Principal Payments minus Interest Payments). Similar to the net resources flows, net resource transfer also displayed similar declining trends, it was positive over the past five years.. In Table 6 and 7 items which exhibit negative amount in both the net flows and net transfers implies that the out flows is greater than the inflows for those creditors.

Table 7. Net Resource Transfers on External Debt

	Million USD				
	2014/15	2015/16	2016/17	2017/18	2018/19
Total Central Government	2,004.35	1,472.05	1,249.65	1,455.38	1,152.24
Multilateral	810.97	1,277.50	1,240.23	1,280.98	1,235.57
of which IDA (World Bank)	684.61	1,049.89	983.53	1,053.19	1,163.52
Bilateral	226.51	260.80	75.67	240.65	-17.08
Private-Euro Bond Holders	966.88	-66.25	-66.25	-66.25	-66.25
Total Other Public Sector	2,927.97	894.92	-392.8	-447.6	-368.47
Bilateral	1,084.81	1,083.46	469.23	- -27.41	- -249.2
Private Creditors (Commercial Banks and suppliers)	1,843.16	-188.54	-76.43	-420.19	- -119.27
Grand Total	4,932.4	2,366.95	1,642.46	1,907.86	-783.77

Table 8. Net Resource Flows on Public Sector External Debt**Million USD**

	2014/15	2015/16	2016/17	2017/18	2018/19
Total Central Government	2,123.92	1,633.15	1,420.63	1,650.66	1,340.58
Multilateral	856.83	1,330.33	1,300.94	1,355.20	1,373.88
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Private-Euro Bond Holders	1,000.00	0.00	0.00	0.00	0.00
Total Other Public Sector	3,067.02	1,092.29	654.69	677.31	77.71
Bilateral	1,119.60	1,096.80	529.85	86.74	-35.53
Private Creditors (Commercial Banks and suppliers)	1,004.80	369.98	353.68	575.08	-154.99
Grand Total	5,190.94	2,725.44	2,075.32	2,327.97	1,418.30

4.2 Domestic Debt

The total domestic debt comprises of five instruments namely; direct advance, treasury bills, government bonds for central government and corporate bonds, long term and short term loans for SOEs. Government uses direct advance and Treasury Bills to fill the budget gap. It is important to note that domestic debt market is not well developed and as a result Direct Advance (DA) which is the National Bank of Ethiopia overdraft facility that the government is used as a residual to fill the budget gap. The uses of direct advance become reasonable when government is not able to sell enough Treasury bill because of low demand, to fill the budget financing gap. Treasury Bills are sold through auctions, and do have four different maturities: 28 days, 91 days, 182 days and 364 days.

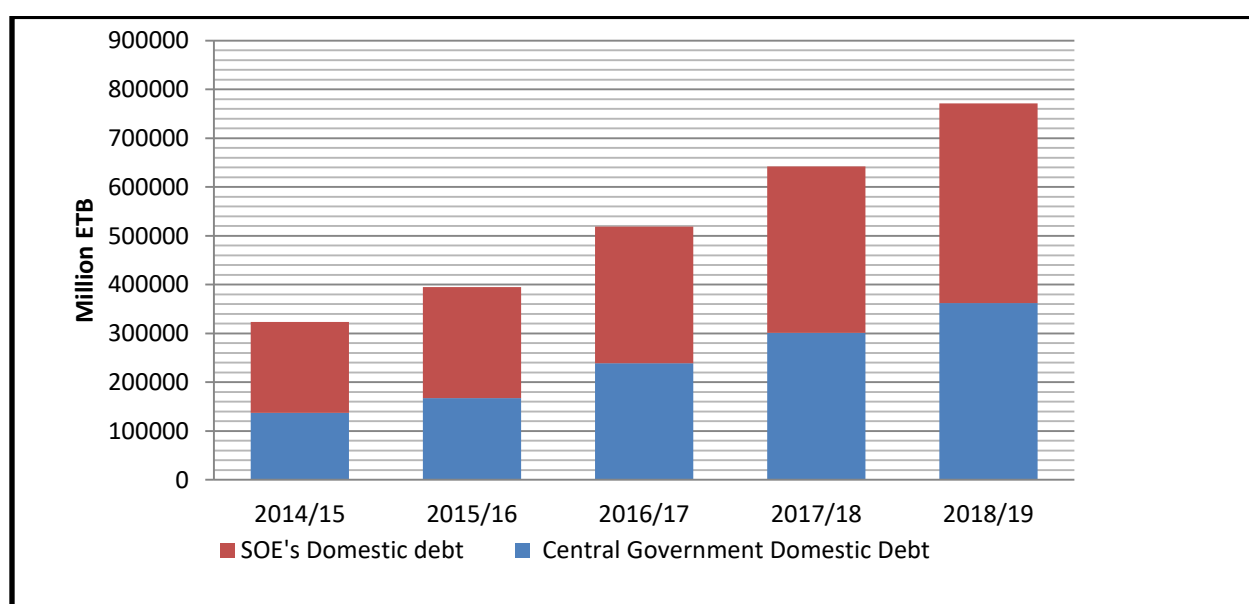
The government usually issues Government Bonds when there is a need to convert short-term borrowings of Central Government and bad debts owed by public enterprises into long-term instruments. Most of the Government Bonds are non-interest bearing.

SOEs issue corporate bonds mostly to CBE to finance mega projects and borrow also long term and short term loans contracted from CBE and DBE.

4.2.1 Total Domestic Debt Outstanding

Total domestic debt, comprising of the above three instruments of Central government and bonds and loans of SOE's, has shown an average increase of 24 percent per annum and has rose from its level of ETB 323,390 million in 2014/15 to ETB 771,379 million in 2018/19. The total stock of domestic debt increased more than 160 percent over the observation period.

Figure 16. Movement of Total Domestic Debt Outstanding



4.2.2 Total Domestic Debt Outstanding by Instruments

Over the observation period there were some changes in both the composition and structure of the domestic debt. The total domestic debt is dominated by borrowings of SOEs which currently constitute about 53.9 % of the total domestic debt. This tells that currently SOEs are contracting huge loans from domestic sources to finalize some of the mega projects.

In the last five years due to increase in the issuance of Treasury Bills, its relative share increased and reached to 17.9 percent of the total stock of domestic debt. Accordingly,

although direct advance was suspended for one fiscal year (July 8, 2011-July 7 2012) to arrest inflation, the percentage share of direct advance remains flat and declined to 24 percent in 2018/19. The stock of the corporate bonds of SOEs has the highest share of the total domestic debt stock followed by direct advance and treasury bills of central government.

Table 9. Domestic Debt Outstanding by Instrument Type

	2014/15	2015/16	2016/17	2017/18	2018/19
Grand Total	323,290.86	395,136.72	518,667.94	641,784.76	771,378.84
TOTAL Central Gov.	137,215.09	167,231.89	238,473.04	300,918.85	361,888.33
Government Bonds	10,345.34	9,214.39	37,436.53	37,140.35	36,589.03
Treasury Bills	43,604.80	57,252.56	73,271.56	111,513.56	138,034.36
Direct Advance	83,264.95	100,764.95	127,764.95	152,264.95	187,264.95
Total SOE	186,075.78	227,904.82	280,194.91	340,865.91	409,490.51
SOE CORPORATE BONDS	128,100.00	160,100.00	195,000.00	241,148.91	301,018.89
SOE Loans	57,975.78	67,804.82	85,194.91	94,666.69	106,451.61
SOE Short Term Loans				5,050.31	2,020.00

4.2.3 Central Government Domestic Debt Portfolio

The Government to fill its budget deficit uses three instruments to mobilize resources in the form of loans from domestic sources including Treasury Bills, Direct Advance and Government Bonds. The first two are short term instrument which are used for deficit financing while the government bond is usually issued for special purpose like that of converting short term instrument of central government into long term and acquisition of bad debt of SOEs during privatization of the enterprise..etc.

Direct Advance

Direct Advance is an overdraft facility from the National Bank of Ethiopia and is used to cover temporary liquidity problems or financial shortages on daily basis arising when government expenditures are greater than cash in the central government's treasury account.

Direct Advance in nominal terms has significantly increased over the observation period. It has risen from its level of ETB 83,264.95 million in 2014/15 to ETB 187,264.95 million in 2018/19 and it has more than doubled in absolute terms in last five years.

Treasury Bills

Treasury bills are basically means for the government to raise money from the public for a short period of time and are sold on the basis of weekly auctions. Currently there are treasury bills of four different maturities of 28, 91, 182 and 364 days. Most of the time the buyers of the bills are government banks, insurance companies, social Security securities agencies and other non-financial public enterprises.

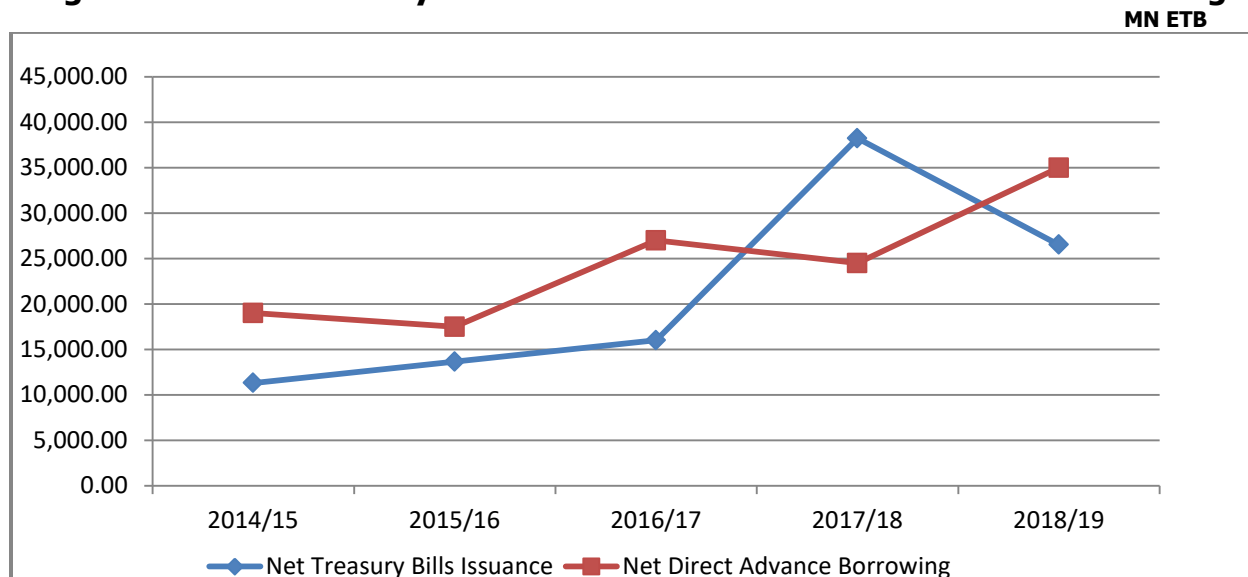
The outstanding balance for treasury bills, which was ETB 43,604.80 million in 2014/15 increased to 138,034.36 million in 2018/19. The share of 91 days treasury bills is increasing over the last five years and it is the highest in 2018/19; it accounted for 77 percent; while the 182, 28 and 364 days bills accounted for 1.0 percent, 0.5 percent and 22 percent respectively. Accordingly, the stock of Treasury Bills accounted 17.89 percent of the total government domestic debt as at the end of 2018/19.

The net issuance of treasury bills, as depicted Figure 17, at 2014/15 was ETB 11,319 million after a steady growth up to 2016/17 there was a sharp rise in 2017/18 to ETB 38,242.00 this specially a result of a higher net treasury bill issuance of 90 days and 364 days, to finance the budget gap during the period.

The net borrowing from central bank of Ethiopia in the form of direct advance in the last five years shows increasing trends until 2016/17 and declined on 2017/18 while for

the current year the net borrowing in the form of Direct Advance is much higher than the preceding year.

Figure 17. Net Treasury Bills Issuance and Net Direct Advance Borrowing



Government Bonds

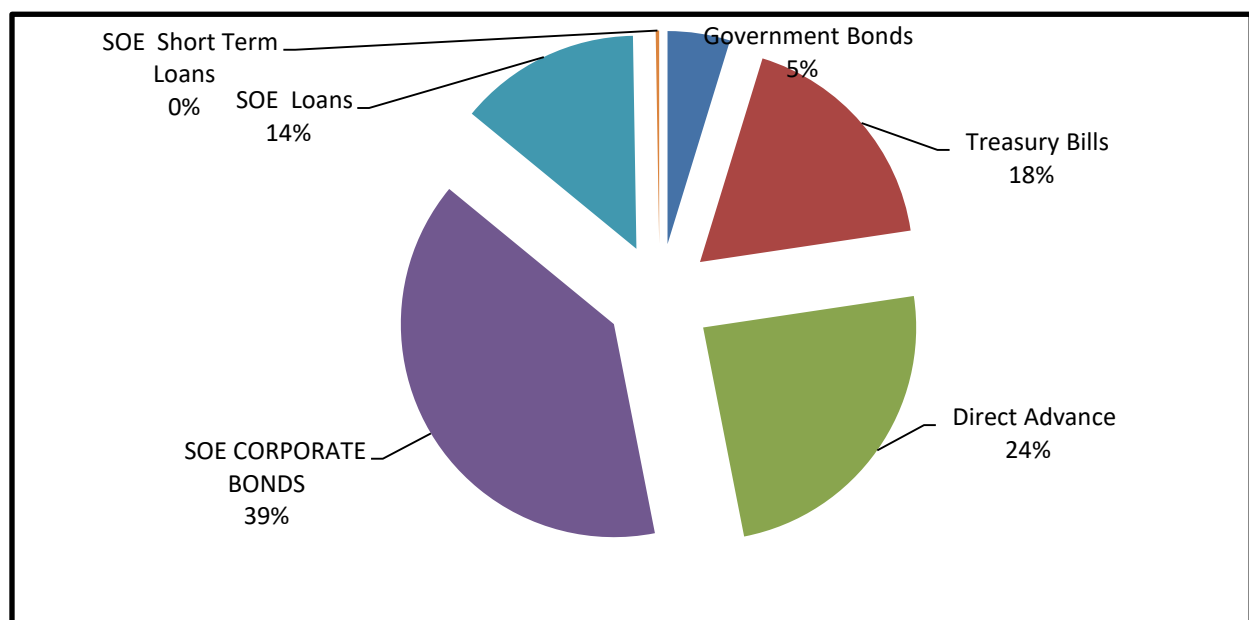
Government Bonds, represent instruments which have long term maturity (10 years and more), issued for special purposes rather than being used as a means for filling budget deficit. The holders of long term bonds among others include the National Bank of Ethiopia (NBE), the Commercial Bank of Ethiopia, the Development Bank of Ethiopia (DBE), Public Servants Social Security Agency and Private Organization Social Security Agency.

The outstanding balance of government bond was Birr 10,345.34 million in 2014/15 and declined in the following year and reaching ETB 9,214.39 million in 2015/16. As a result of the issuance of new government bond in 2016/17 for the purpose of increasing the capital of Commercial Bank of Ethiopia and Development Bank of Ethiopia, the stock of government bond increases to ETB 37,436.53 million and currently it stood about ETB 36,589 million.

4.2.4 State Owned Enterprises Domestic Debt Portfolio

State Owned Enterprises (SOE's) borrows from the domestic sources by issuing corporate bonds as well as long term and short term loans from CBE and DBE. Most of these borrowings are made with government guarantee. They issue corporate bonds and loans mostly to CBE to implement mega projects. The domestic debt outstanding balance of SOEs is ETB 186,0776 million in 2014/15 and has continuously increase since then to reach ETB 409,490 million in 2018/19.

Figure 18. Domestic Debt by Instrument (As at June 30,2019)



4.2.5 Domestic Debt By Holders

The major holders of government domestic securities and lenders to SOEs in Ethiopia are National Bank of Ethiopia, Social Security Agencies, Development Bank of Ethiopia, Commercial Bank of Ethiopia and other non-financial public enterprises.

The National Bank of Ethiopia: has been the major holder of government securities over the last 5 years. Its share from central government domestic debt was 64 percent in 2014/15, and 29 percent the total domestic debt. However, during subsequent years its relative share has continuously declined reaching 54 percent of the central

government domestic debt and 25 percent of the total domestic debt in 2018/19. Its holdings are mainly in the form of direct advance.

The Public Servants Social Security Agency (PSSSA) and Private Organizations Social Security Agency (POSSA): are the second major holder of government securities and their claims are long-term government bonds and short term treasury bills. The claim by PSSSA & POSSA has increased from ETB 26,371 million in 2014/15 to ETB 103,857 million in 2018/19 displaying an increment of 41 percent per annum on average. Its share out of the total government domestic debt portfolio has increased over the years and reached 13.5 percent in 2018/19.

The Development Bank of Ethiopia (DBE): is the third major holder of government securities and its claims are predominantly treasury bills and long-term government bonds. The claim by DBE has increased significantly from ETB 14,989 million in 2014/15 to ETB 32,795 million in 2018/19. This is mainly due to the surge in the stock of 364 days treasury bills held by DBE specifically in 2017/18.

The Commercial Bank of Ethiopia (CBE): holding of government securities by CBE was insignificant until 2016/17 where the government issued a special bond to raise the capital of the bank reached ETB 26,590 million in 2018/19.

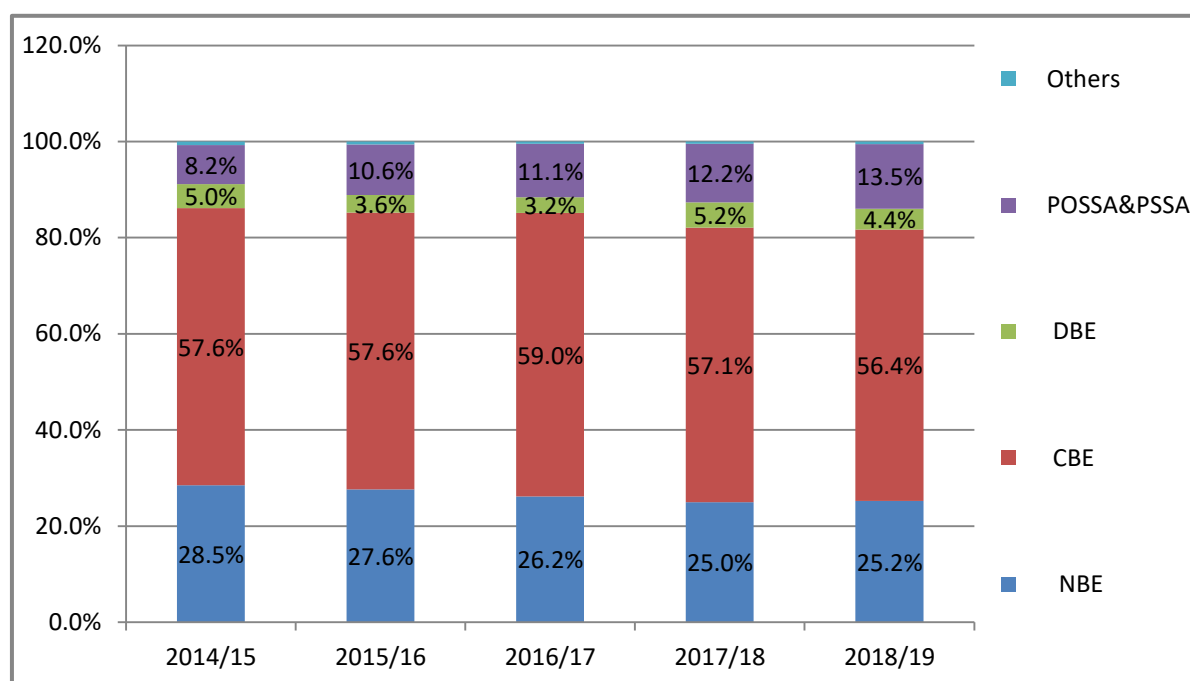
Others: the other holders of government securities are government insurances companies and other non- financial public enterprises. The holdings of insurances companies and other public enterprise are declining over the observation period and are insignificant.

Commercial Bank of Ethiopia for (State Owned Enterprises Bonds and Loans)

Commercial Bank of Ethiopia and Development Bank of Ethiopia are the holder of State Owned Enterprises Corporate Bonds and Loans mostly with the guarantee of the central government. Over the last five years the claim by CBE from State Owned Enterprises

has increased significantly from ETB 184,952.63 million in 2014/15 to ETB 408,687.16 million in 2018/19.

Figure 19. Share of Domestic debt Outstanding By holders



4.2.6 Government Domestic Debt Service

Total domestic debt service for government securities and SOE's bond and loans in 2018/19 amounted to ETB 30,677.61 million, of which ETB 3,879.82 million (13 %) was for principal repayments and ETB 26,797.79 million (87.%) for interest payments. The debt service payment for government securities amounted to ETB 7,864.64 million (26%), while the debt service payment by SOE's amounted to ETB 28,372.69 million (74%).

The principal repayments were made for different central government and SOEs bond holders, while the interest payments were made for direct advance, treasury bills, government and SOEs bonds. The interest payment for treasury bill and direct advance

has shown an increase per annum. The interest payment for the government bonds has decreased over the last five years.

Table 9. Total Public Sector Domestic Debt service Payment

Million ETB

	2014/15		2015/16		2016/17 ^R		2017/18 ^R		2018/19 ^P	
	ETB	%	ETB	%	ETB	%	ETB	%	ETB	%
TOTAL DEBT SERVICE	13,258.11	100.00	17,794.24	100.00	20,156.45	100.00	29,890.47	100.00	30,677.61	100.00
TOTAL PRINCIPAL	1,012.33	7.64	1,933.19	10.86	2,437.91	12.09	5,064.16	16.94	3,879.82	12.65
TOTAL INTEREST	12,245.77	92.36	15,861.05	89.14	17,718.54	87.91	24,826.31	83.06	26,797.79	87.35
CENTRAL GOV.	3,162.10	23.85	4,831.86	27.15	5,375.01	26.67	5,809.30	19.44	7,864.64	25.64
PRINCIPAL	326.84	2.47	1,130.95	6.36	845.63	4.20	296.18	0.99	551.32	1.80
Bonds	326.84	2.47	1,130.95	6.36	845.63	4.20	296.18	0.99	551.32	1.80
Treasury Bills	-	-	-	-	-	-	-	-	-	-
Direct Advance	-	-	-	-	-	-	-	-	-	-
INTEREST	2,835.26	21.39	3,700.91	20.80	4,529.38	22.47	5,513.12	18.44	7,313.32	23.84
Bonds	20.86	0.16	18.61	0.10	11.01	0.05	2.65	0.01	5.59	0.02
Treasury Bills	709.62	5.35	864.64	4.86	1,107.39	5.49	1,108.71	3.71	2,247.78	7.33
Direct Advance	2,104.78	15.88	2,817.66	15.83	3,410.98	16.92	4,401.76	14.73	5,059.95	16.49
SOE TOTAL	-	-	12,962.38	72.85	14,781.44	73.33	24,081.17	80.56	22,812.97	74.36
PRINCIPAL	685.49	5.17	802.24	4.51	1,592.28	7.90	4,767.98	15.95	3,328.50	10.85
INTEREST	9,410.51	70.98	12,160.14	68.34	13,189.16	65.43	19,313.19	64.61	19,484.47	63.51

5. On-Lending Loans, Guarantees and Contingent Liabilities

Contingent liabilities of the Government represent possible costs to Government arising from the possible occurrence of events in the future that are not within government's control. These include loan guarantees, warranties, indemnities, uncalled capital and letters of comfort, together with those contingencies considered remote.

Government has also supported SOEs by providing explicit guarantees to facilitate the process of securing credit on much softer terms. Government's policy on on-lending

and guarantees seeks to recover loans advanced to SOEs for commercially viable mega projects in order to support economic development of the country.

On Lending Loans

In accordance with the implementation of the Financial Administration Proclamation government sometimes initiated processes aimed at operationalizing all subsidiary on-lending agreements entered into between MoF and SOEs to enhance project cash flows towards debt service payment and reduce the debt burden on the taxpayer. In the past many years Ministry of Finance has been contracting loans from either external or domestic sources and in turn lent the proceeds to state-owned enterprises. On-lending to a SOEs is only applicable and eligible under the following conditions:

- The corporation plays a strategic role in economic development endeavor,
- Implementing infrastructure mega projects focusing on country's potentials,
- Has no access to multilateral credits and cannot attract competitive funding; and
- Is performing a social project that would be more efficiently executed on behalf of the government.

Accordingly, the government in the past several years has borrowed loans from both concessional and semi-concessional sources and transferred to selective SOEs to implement infrastructure projects. As a result, the outstanding debt stock for all on-lent loans to SOEs increased in the past years.

Providing Guarantees to SOEs

Some SOEs have been implementing various mega projects that enhance foreign currency earning as well as supporting the economic development endeavor of the country. In support of these objectives, the government has continued to support the SOEs to implement these projects among others by providing guarantee to secure finance from domestic as well as external sources. Nowadays, the volume of SOEs guaranteed debt outstanding has substantially increased thereby putting more risk on the government in the form contingent liability.

Measures undertaken to avoid any unforeseen contingent liability occurrences

Recently, to minimize exposure and risks associated with SOEs debt accumulation the Government has embraced new innovations in financing infrastructure development off balance sheet without impacting heavily on the debt portfolio. Towards this end Ethiopia has introduced the framework for raising private financing for public investments through the Public Private Partnership (PPP) initiatives.

Accordingly, the initiative will focus on two priority areas namely energy sector and Road sector. All guarantees and other security instruments provided under the PPP, together with all other contingent liabilities are integrated into the debt management process. To mitigate the contingent liabilities risks, a close follow up mechanism was established under the PPP Act to provide good governance framework to manage direct liabilities and contingent liabilities in all phases of the project cycle.

To achieve the better outcomes in fiscal risk management, the Ministry of Finance is also placing a lot of emphasis in project financial models, with the view to ensuring manageable project debt repayment mechanism to avoid any unforeseen contingent liabilities.

Similarly, the government has issued Public Debt Management and Guarantee Directive in order to enhance monitoring system and putting in place an organized coordination mechanism to avoid any risks associated with the borrowing by SOEs. In addition, various reforms of SOEs towards finance and corporate governance are underway to increase efficiency and effectiveness of the enterprises. All these concerted efforts by all stakeholders will reduce the occurrence of contingent liability.

6. Cost & Risk Analysis of Ethiopia's Public and Publicly Guaranteed Debt

Risk refers to the potential for the cost of debt to deviate from its expected outcome. This stems from unexpected variations of different economic variables such as interest rate and exchange rate. Market risk, operational risk and liquidity risk are the types of risks associated with public debt portfolio. In this regards it is important to assess the risks associated with the debt portfolio because such information enables decision makers to design forward looking strategies on the optimal debt structure in terms of maturity, interest rate and exchange rate. In this analysis, exposure of the debt portfolio risk is captured using the following risk indicators: refinancing risk, interest risk and exchange risk.

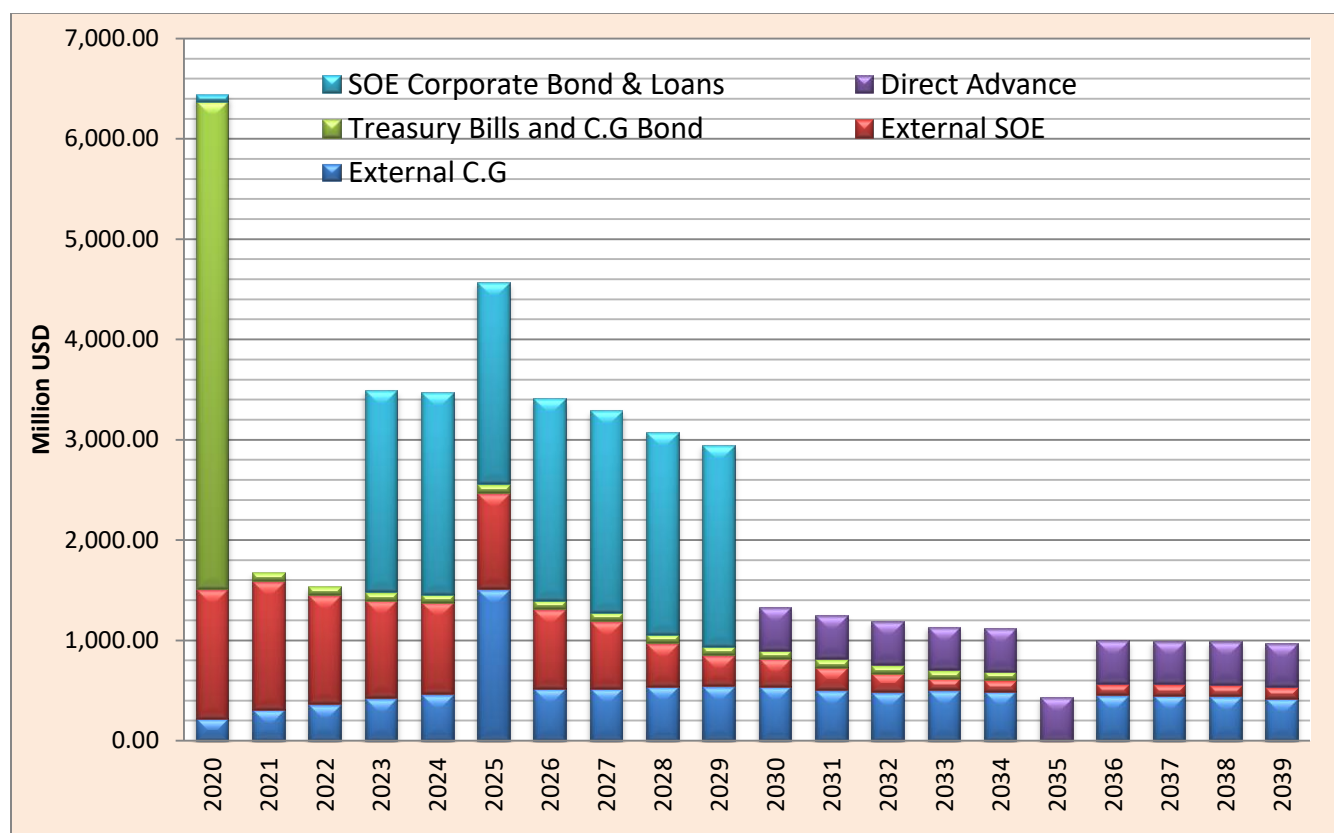
6.1. Refinancing Risk

Refinancing risk (rollover risk) is the possibility of having the debt to be rolled over at a higher interest rate. Three measures are used to assess the exposure of Ethiopia's public debt to refinancing risk, namely: the redemption (maturity) profile of debt, the Average Time to Maturity (ATM) and maturing in one year of the debt stock as discussed below.

- **Refinancing Risk Analysis Using Redemption Profile and debt maturing in one year**

The redemption profile refers to the outstanding debt stock or the amount of debt that is falling due in a given period of time. This indicator shows the specific time of a country's vulnerability which is manifested by high debt service payments in the debt repayment schedule. With new loans, it is feasible to choose repayment profile which does not coincide with humps in the redemption profile. When choosing the maturity of new borrowing, the redemption profile is useful in highlighting the specific points of a country's vulnerability, which is manifested by high debt service payments in the debt repayment schedule.

Figure 20. Public Sector Debt Redemption Profile by Instruments



Out of the total public debt about USD 7,178.22 million (14 percent) will fall in due in 2019/20 excluding direct advance and including the treasury bills that is going to be rolled over during the year. The total amount of external debt payment falling due at the same period accounts for USD 1,514 million (21 percent) of the total public debt service falling due during this year of which only 3 percent for central government and 18 percent for SOEs.

Out of the total public debt due in 2019/20 total domestic debt accounts for 79 percent (central government domestic debt service accounts for 68 percent and SOEs debt accounts for 11 percent). This show to what extent external debt of central government is characterized by very low exposure to rollover/refinancing risk while

domestic debt is characterized by high rollover risk as most of the domestic debt (excluding Direct advance) is in the form of short term maturity or treasury bills.

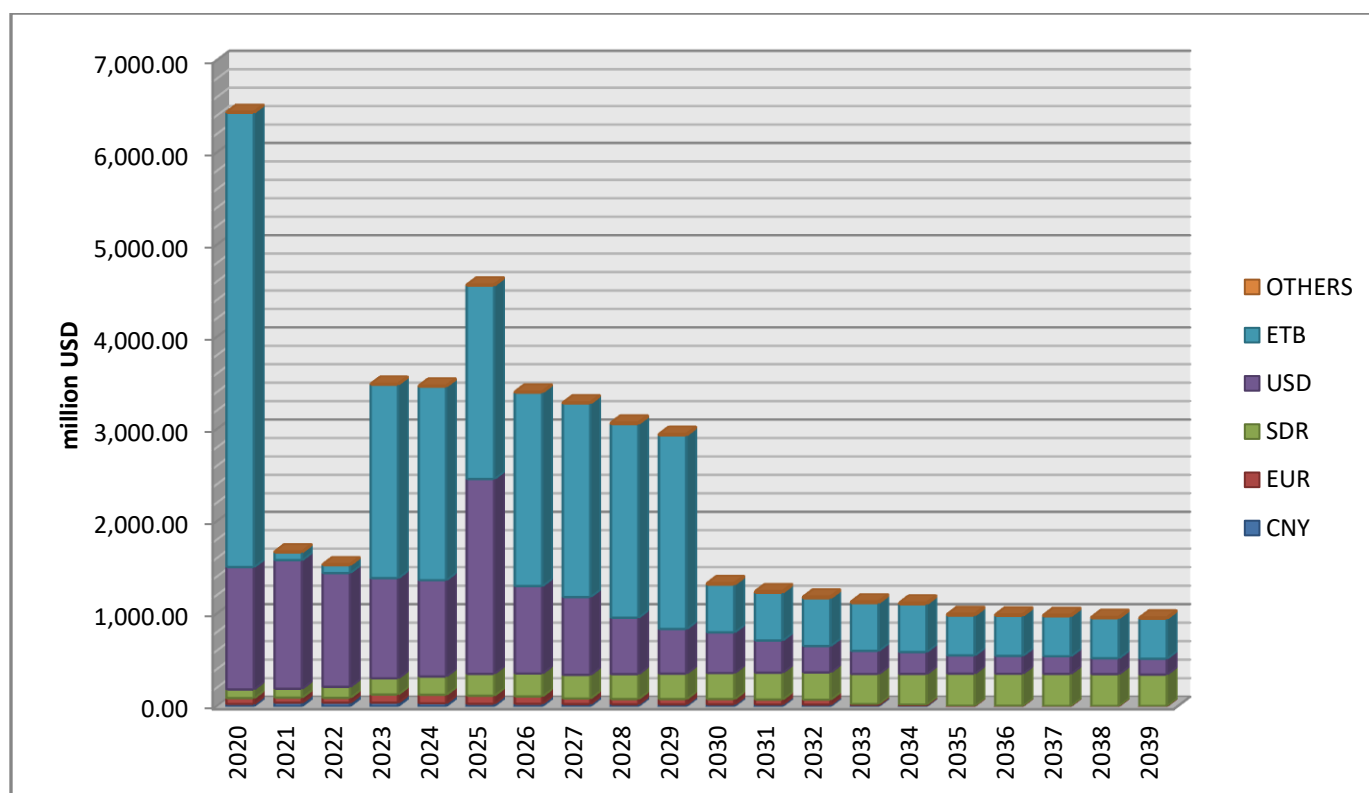
The central government domestic debt falling due in 2019/20 is about USD 4,858 which is 18.2 percent of the total domestic debt and 9.20 percent of the total public debt. This explain the short term nature of domestic debt of central government which is mostly in the form of treasury bills which mature in less than or equal to one year and is rolled over as it matures. Hence, the domestic debt portfolio, specially central government domestic is highly exposed to refinancing risk.

From the redemption profile (Figure 20) it is possible to observe that high debt service payment is manifested in 2020 and 2025. This accounts of the rollover of treasury bills in 2020 and by 2025 the sovereign bond bullet payment which are due during this period and most of the SOEs external borrowing will mature between this period. Ethiopia is, given the debt strategy of the country, expected to contract concessional loans for central government hence external debt obligations will be repaid over a long period of time as shown in above graph.

The measure of concessionality of a loan, calculated as the difference between the face value of the loan and the sum of the discounted future debt service payments expressed as percentage of the face value of the loan. The higher the grant element the higher the concessionality of the loan and the lower will be the cost. As most of the central government external debt is from official creditors it has high concessionality.

The public debt redemption profile in the borrowing currency (Figure 21) indicates that, most of the total debt repayment will be made in ETB, USD and SDR, as all domestic debt are denominated in ETB and the majority of external debt is denominated in USD and SDR. The largest payment in ETB will occur in 2020 and the majority of this payment in ETB will be realized as a rollover of Treasury Bills and in 2025 there will be big repayment in USD as a result of the redemption of the sovereign bond bullet payment.

Figure 21. Public Sector Debt Redemption Profile in Currency



Costs of Public Debt as measured on weighted average interest rate

The current weighted average interest rate as shown on Table 9 of the total external debt is 2.58 percent, the weighted average interest rate of central government external borrowing is about 1.6 percent while the borrowing by SOE's from external source is relatively more expensive as they have borrowed at the rate of 3.6 percent for fixed interest borrowing, and 4.4 percent on variable rates at the current labor rate plus the fixed margin. The substantial share of the central government external borrowing is from IDA and AfDB thus its weighted average interest rate is lower than others.

The weighted interest rate for SOEs external debt is higher specially borrowing made on variable interest rate are much higher. As the worldwide financial situation is volatile the current situation may not hold for long time, specially the borrowing on variable interest on the basis of LIBOR and EURIBOR, the rate is expected to rise and the cost of borrowing by the SOE's will rise too.

Hence, to avoid refinancing risks and any unforeseen negative impacts on debt portfolio of the country there is a need to closely monitor the cost and additional conditionality's of borrowing by SOEs. The weighted average interest for total domestic debt is 5.5 percent and 2.6 percent for Central government and it is 8.3 percent for SOEs domestic debt.

- **Refinancing Risk Analysis Using Average Time to Maturity**

The Average Time to Maturity (ATM) of the debt portfolio also known as Average Residual Life provides information on how long it takes on average to rollover or refinances the debt portfolio. Long ATM in the external debt portfolio indicates that the predominance of concessional loan is relatively higher and has less refinancing risk than domestic debt.

Low value of ATM indicates that a high share of the debt will be due for payment or roll-over in the near future, implying a substantial exposure to refinancing risk if resources are not available to meet or roll-over the maturing debt. Higher value of ATM indicates that a low proportion of the debt will be maturing in the near future, implying a low exposure to refinancing risk. In this case, Ethiopia's public external debt portfolio has a minimal exposure to refinancing risk.

Accordingly, the average time to maturity of the total public debt portfolio is about 10 years with the external and domestic debt portfolio displaying 11.87 years and 8.13 years respectively. Central government external debt ATM has the highest which is 15.83 years as most of the central government external borrowing is obtained from official multilateral and bilateral sources, where the country secures credits with a long term maturity and on highly concessional terms.

Table 10. Cost and Risk Indicators as at June 30, 2019

		EXTERNAL DEBT TOTAL	EXTRNAL DEBT CENTRAL GOV.	EXTRNAL DEBT SOEs	DOMESTI C DEBT TOTAL	DOMESTIC DEBT CENTRAL GOV.	DOMESTI C DEBT SOEs	TOTAL DEBT
Amount (in millions of USD)		27,029.38	15,931.41	11,097.97	26,676.45	12,515.12	14,161.33	53,705.83
Nominal debt as % GDP		28.1	16.6	11.5	27.7	13.0	14.7	55.9
PV of debt as % of GDP		21.2	9.9	11.3	27.7	13.0	14.7	49
Interest Payment in % of GDP		0.7	0.2	0.5	1.2	0.3	0.9	1.9
Cost of debt	Weighted Av. IR (%) for Fixed	1.6						
			1.37	3.6	5.5	2.6	8.3	4.0
	Weighted Av. IR (%) for Variable	4.38						
		2.58	4.03	4.40				
Refinancing risk	ATM (years)	11.87	15.83	6.31	8.13	10	6.47	10
	Debt maturing in 1yr (% of total)	5.77	1.43	12.0	18.47	38.82	0.49	24.24
Interest rate risk	ATR (years)	9.68	15.77	1.16	8.1	10	6.47	8.91
	Debt refixing in 1yr (% of total)	37.02	1.72	86.4	18.47	38.82	0.49	27.7
	Floating rate debt (% of total)	35.41	0.28	84.0	18.2	38.1	.49	26.7
FX risk	FX debt (% of total debt)	50.34						

The ATM for bond, treasury bills and borrowing by SOE's from domestic and external sources shows somewhat shorter maturity period and may create risk to refinance the debt portfolio.

Applying the above analysis the external debt will take a long period of time before the debt due for repayment. Comparing the ATM for the total public debt at 10 years with

the external debt portfolio has a lower exposure of refinancing risk. This is explained by the structure of the external debt profile which is comprised of concessional loans. All in all, the average time to maturity for central government external debt is 15.83 years while that of State Owned Enterprises (SOEs) is about 6.31 years.

Average Time to Maturity of total domestic debt is 8.13 years, for central government assuming direct advance will be converted to 15 years bond with 10 years grace period and , this means that on average it takes 8.9 years for Central Government Domestic debt and 5.5 years for SOEs domestic debt before the debt is due for repayment or roll over. The domestic debt is associated with a substantial degree of refinancing risk due to the short term nature of Treasury Bills.

6.2. Interest Rate Risk

Interest rate risk refers to the exposure of the portfolio to changes in the market interest rates. Three measures are used to assess the exposure of the debt portfolio to interest rate risks, as follows:

- i. The ratio of debt that has fixed or floating interest rates in the total portfolio.
- ii. Debt that is exposed to interest rate re-fixing within a specific time period. In other words, this refers to maturing debt or variable debt whose interest rate is subject to change within a given period. Maturing debt may be exposed to interest risk if resources are not available to redeem it and thus it has to be rolled over.
- iii. Average Time to Re-fixing (ATR), which indicates the average time required to reset the interest rate for the debt portfolio.
- iv. The Average Time to Re-fixing (ATR) indicates the exposure of the debt portfolio to changes in interest rates. High ATR will indicate low risk, because this will imply that a relatively low share of the debt will have its interest rates re-set in a short period of time. Conversely, a low value of ATR indicates that a high share of the debt will be re-fixed in the near future, i.e. exposure to risk

- **Assessment of Interest Rate Risk of Ethiopia's Public Debt**

- i. ***Analysis of Interest Rate Risk of Public Debt Based on Fixed and Floating Rates Mix***

The central government external and domestic debt portfolio is made up of instruments which were contracted on fixed and relatively on a low interest rate terms. This means that the central government debt is less susceptible to interest rate risk except treasury bills. Adverse interest rate movements on the world market would not significantly affect the interest payment obligations of the central government.

On the other hand the majority of borrowing by SOEs' is on variable interest rate 86 % and this implies that there will be an interest rate risk associated with the external borrowing by SOE's. Overall, a significant proportion of the external loans are highly concessional, with contractual interest rates for these loans set at significantly below the market rates.

- ii. ***Analysis of Interest Rate Risk of Public Debt Based on Exposure to Re-fixing***

Interest rate risk of the public debt is well captured by proportion of debt that is subject to interest rate re-fixing within a specified period. For both external and domestic debt, changes in interest rates affect debt servicing costs. Hence, assessing the proportion of debt to be re-fixed shows the extent to which the portfolio is vulnerable to higher funding costs as a result of higher market interest rates.

Analysis of Ethiopia's external public debt shows that the portfolio is subject to high interest rate risk because relatively a larger portion of the total public debt (37 percent total external debt) is contracted in floating interest rate. On the other hand analysis of domestic debt particularly treasury bills shows that the portfolio is subject to high interest rate risk. This is as a result of the short-duration nature of the Treasury bill. By the end of June 2019 Treasury bill amounting to USD 4.7 billion is expected to be rolled over. This implies that 18 percent of the central government domestic debt portfolio is subject to changes in domestic interest rates. A higher proportion of debt that is

subjected to re-fixing within one year indicates high risk to adverse interest rate movements. Excluding domestic debt, interest risk associated with Ethiopia's external debt is relatively lower since 63 percent of the existing debt is not subject to interest rate changes due to fixed interest rates.

iii. ***Analysis of Interest Rate Risk of Public Debt Based on Average Time to Re-fixing***

As of June 2019 the Average Time to Re-fixing (ATR) of Ethiopia's public debt was 8.9 years. Thus, it will take an average of 8.9 years to re-fix the interest rates of the portfolio. The ATR of the external debt stands at 9.7 years which imply that it will take, on average, 9.7 years to reset the interest rate of the external debt portfolio.

The ATR for central government is 15.8 years while that of SOEs external debt ATR is 1.2 years. This high value of central governments external debt ATR indicates lower interest risk associated with the central government external debt portfolio whereas SOEs external debt is with high exposure to interest risk as its ATR is the lowest.

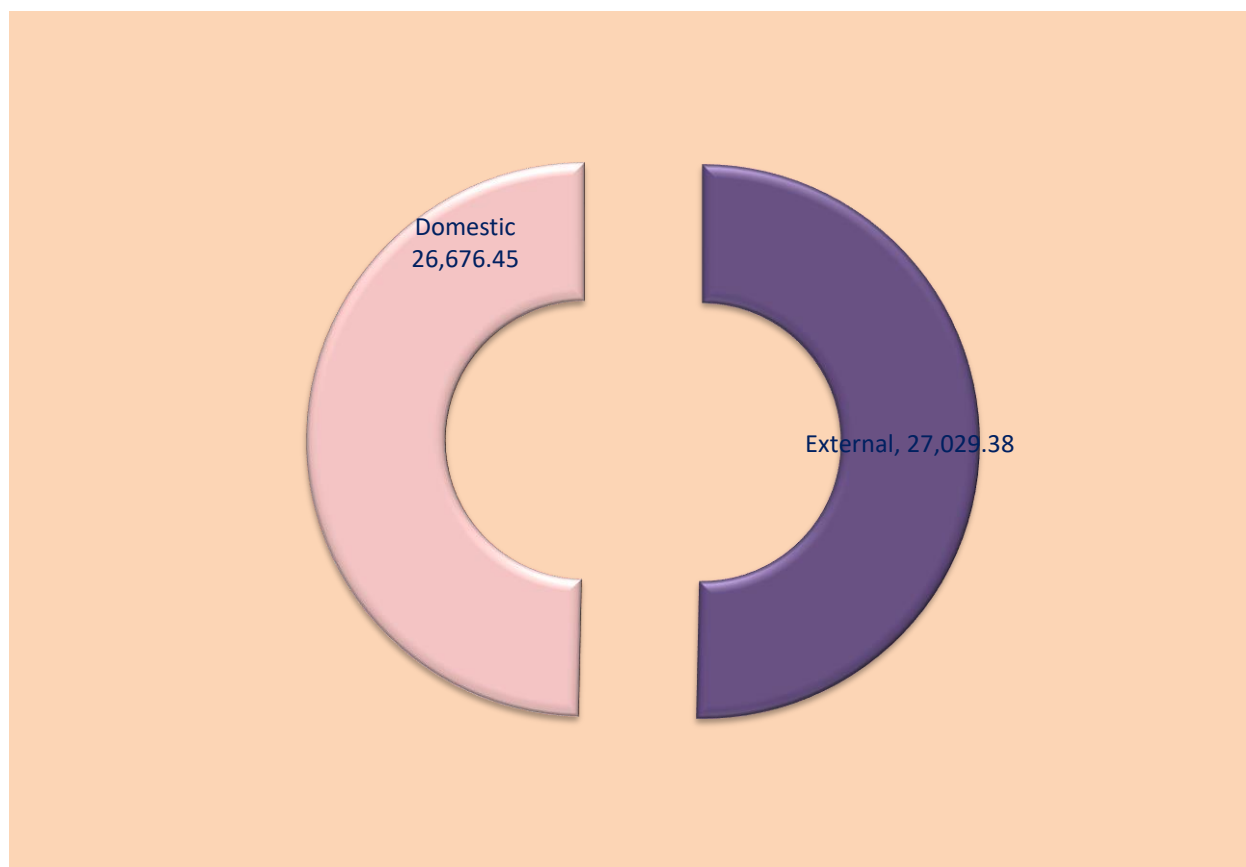
The total domestic debt is also highly exposed to interest risk. This is confirmed by a lower value of ATR which stands at 8.9 years. This ATR implies that it will take only 8.9 years to re-fix the interest on domestic debt hence domestic debt has a relatively high exposure to interest rate risk. The reason for this lowest ATR for domestic debt is the treasury bills which constitute more than one third of the total domestic debt.

6.3. Exchange Rate Risks

Exchange rate risk refers to the exposure of the debt portfolio to changes in exchange rate or the mismatch between the repayment obligations and the sources of foreign exchange rate risk. There are three methods of quantifying exchange rate risk of the debt portfolio, namely: the share of external debt in total debt; the currency composition of the debt portfolio; and degree of currency mismatch between the debt service obligations and the composition of foreign exchange for a given country.

Figure 22. Composition of External and Domestic Public Debt (June 30, 2019)

MN USD

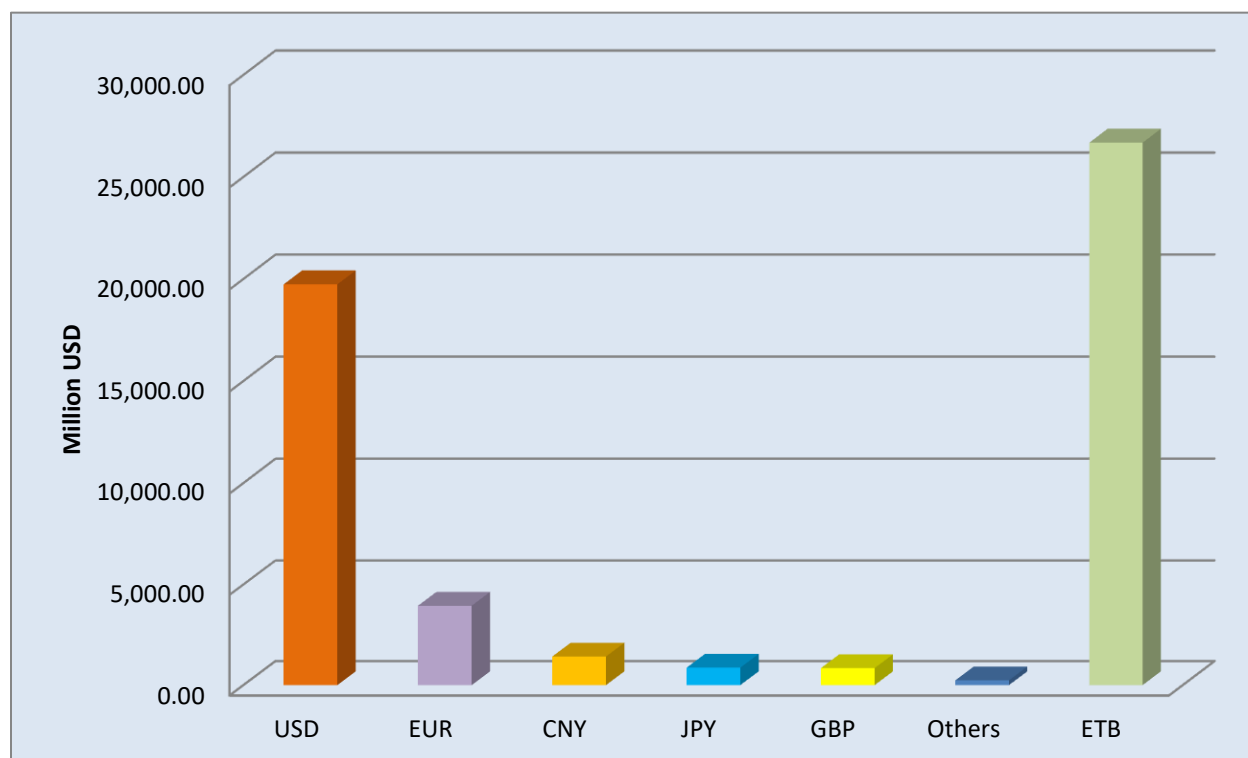


The share of external and domestic debt on total public debt is 50.3 percent and 49.7 percent respectively. This ratio measures the dependency on external borrowings for development. The external debt portfolio is exposed to exchange rate risks owing to adoption of free floating exchange rate. Hence any significant depreciation of the Ethiopian Birr against the foreign currencies can substantially contribute to higher debt service payments in local currency terms. As a result, there could be higher debt service payments in the budget than forecasted.

The currency composition of total public debt exhibits minimal exchange rate risk emanating from currency mismatch since most of the external debt service obligations are in United States Dollars whereas all domestic debt service obligations are in Ethiopian Birr. The currency composition of Ethiopia's external debt does not constitute

a significant source of external vulnerability since the currency structure closely matches with foreign reserves/ earnings.

Figure 23. Currency Composition of Total Public Debt (June 30, 2019)



Debt Service Restructuring

The Government in collaboration with SOEs has exerted the maximum effort to renegotiate with some of the policy financial institutions as part of debt restructuring strategy so as to reduce the immediate foreign currency demand at the short term. Accordingly, the debt restructuring of the eight sovereign guaranteed loan facilities that were successfully amended enabled to extend substantial amount of debt service payment per year including reduction of margins, extending of grace and maturity period.

As per the debt restructuring agreement with the respective creditors a combined amount of about USD \$376 million annual saving from foreign currency payment obligation has been secured.

This has a direct impact on the foreign currency demand for SOE projects with a view of alleviating the immediate need and allocation of foreign currency resource to other obligations. In addition, MoF will also design a new system to monitor debt obligation of SOEs to proactively address any distress and engage relevant creditors.

7. Conclusion

The current debt portfolio analysis exhibits that the stock of total public debt increases at the rate of 12 percent per annum. Both public sector external debt and domestic debt stock increased over the analysis time horizon, which can be partly explained by huge disbursement towards the development and upgrading of infrastructures. Not only has the magnitude of the public sector debt changed but also the beneficiaries and the composition of the public debt shows a significant change. During the observation period the relative share of central government debt is increasing at a declining rate while that of the SOE's is increasing at an increasing rate.

Over the last years the main composition of the debt portfolio continued to be concessional for loans denominated in foreign currency, and direct advances, treasury bills and corporate bonds denominated in Ethiopian Birr.

Currently external debt is dominated by central government borrowing whereas domestic debt is dominated by SOEs borrowings. It is evident that the share of concessional loans as a total of external debt has increased from 49 percent at end June 2015 to 55 percent as of end June 2019. This is due to higher borrowing by central government to implements its projects and the reduction of SOEs borrowing in the last three years as the government commitment to improve the debt distress level of the country and as per the non-concessional borrowing limit of the World Bank. The main areas where the resources were used are energy, sugar, transport, roads and others projects that support the endeavor of economic development of the country.

The debt structure of the public debt has also changed towards concessional sources, as all of the borrowing by SOEs from external non-concessional source is from commercial banks and suppliers and its stock is declining in the last three years. The accumulation non-concessional debt might have a negative impact on the debt sustainability of the country.

As most of the SOEs borrowing is with the guarantee of the government, it is a contingent liability for the government and if any of the SOEs are unable to repay their debt service the guarantee might be called and may have a negative impact on the government budget.

The share of external debt with variable interest rate is also increasing from time to time and this will have an interest rate risk. Following the 2008 international financial crisis the variable interest like LIBOR and EURIBOR reference rate was low and the interest payment of the SOE's to their respective creditors was relatively low but currently the interest rate is increasing, their future interest payment may show significant upward change as a result of upward movement of LIBOR rate, but this year since January 2019 it also starts to decline.

The borrowings of the government from domestic source is mainly in the form of direct advance and treasury bills which has high rollover risk, that is the government need to rollover the existing treasury bills whenever they mature. The borrowing of the SOEs from CBE with the guarantee of the government has also significantly increased.

Debt is sustainable when a borrower is expected to be able to continue servicing its debts without an unrealistically large correction to its income and expenditure balance. Debt sustainability, thus, reflects a country's solvency, liquidity, and adjustment capacity.

The public debt dynamics over the last few years appear to have worsened, due to external sector poor performance indicating some risk on debt sustainability. As the current debt volume is increasing at increasing rate, it is appropriate to evaluate and manage the risk involved in different debt compositions, facilitating coordination with fiscal and monetary management, and enhancing transparency. Accordingly, to improve the existing situation, the government has taken subsequent measures including:

- Maintaining in a sustainable manner the decision of the Government the SOEs not to borrow from non-concessional sources so that it is possible to improve the

debt risk situation of the country including adhering to the decision of the World Bank and IMF,

- Focused central government borrowing exclusively from concessional sources,
- Diversified sources of concessional borrowing including focusing on non-traditional sources,
- Taken the necessary measures that enhance foreign currency earnings by investing in the development of industrial zones, attract FDI inflow and boost government revenue etc.,
- Use the new Public Private Partnership framework to implement strategically important mega infrastructure projects,
- Enhancing domestic debt market and secondary market, with the objective to introducing bonds with various maturities to replace part of the treasury bills so that the rollover risk of the domestic debt will be minimized,
- Undertake debt management capacity building activities in a sustainable manner so that it is possible to enhance analytical capacity to undertake useful analysis, assessments and studies for policy makers decisions.

Finally, it is the expectation of the Ministry of Finance that this report will enhance transparency and accountability of public debt management in Ethiopia.

8. GLOSSARY

DEFINITIONS

It is hoped that the following definitions could help the reader to understand the concepts and correctly interpret the figures provided in the various tables. The definitions are taken from:

- 'External Debt Management: An Introduction', by Thomas M. Klein, World Bank Technical Paper No. 245
- 'External Debt Statistics: Guide for Compilers and Users, BIS, ComSec, Eurostat, IMF, OECD, Paris Club Secretariat, UNCTAD, World Bank, 2003'.
- Debt and DMFAS Glossary, UNCTAD, 2008

A

Allocation of a Tranche: All or part of a loan/grant tranche assigned to finance projects or programs.

Amortization: The repayment of principal of a loan spread out over a period of time.

Amortization Schedule: The schedule for the repayment of principal and payment of interest on an ongoing basis.

Arrears: The total of scheduled debt service payments that have fallen due but remain unpaid.

B

Bilateral Creditor: In DMFAS, it refers to a type of creditor in the context of external debt. Official bilateral creditors include governments and their agencies (including Central Bank), autonomous public bodies or official export credit agencies.

Bilateral Debt: Loans extended by a bilateral creditor.

Borrower (debtor): The organization or the entity defined as such in the loan contract which usually is responsible for servicing the debt.

C

Cancellation: An agreed reduction in the undisbursed balance of a loan commitment.

Commercial Credit: In the context of the Paris Club, loans originally extended on terms that do not qualify as official development assistance (ODA) credits.

Commercial Interest Reference Rates (CIRR): A set of currency-specific interest rates for major OECD countries.

Commitment: An obligation to furnish resource of a given amount under specified financial terms and conditions.

Commitment Charge (fee): Charge or fee made for holding available the undisbursed balance of a loan commitment.

Commitment Date: The date on which the commitment occurs.

Concessional Loans: Loans that are extended on terms substantially more generous than market loans.

Concessional Level: See grant element.

Credit: An amount for which there is a specific obligation of repayment.

Creditor: The organization or entity that provides money or resources and to whom payment is owed under the terms of a loan agreement.

Creditor Country: The country in which the creditor resides.

Currency of denomination or Currency of a Loan: The unit of account in which amounts of indebtedness are expressed in the general/loan agreement.

Currency of Repayment: The unit of account in which a loan is to be repaid.

Currency of Reporting: The unit of account in which amounts are reported to the compiling agency and/or to an international agency compiling debt statistics.

Currency of Transaction: The medium of exchange in which an individual transfer occurs.

Current Maturities: Maturities falling due during the consolidation period of a rescheduling.

D

Debt Relief: Any form of debt reorganization that relieves the overall

Debt Reorganization/Restructuring: Debt reorganization arises from bilateral arrangements involving both the creditor and the debtor that alters the terms established for the servicing of a debt.

Debt Rescheduling: Debt rescheduling refers to the formal deferment of debt service payments and the application of new and extended maturities to the deferred amount.

Debt Service: Refers to payments in respect of both principal and interest.

Debt-Service to Export Ratio: The ratio of debt service (interest and principal payments due) during a year, expressed as percentage of exports (typically of goods and services) for that year.

Debt Sustainability Analysis: A study of a country's medium- to long term debt situation.

Debtor Country: The country in which the debtor resides.

Direct Advance: Government over draft from the Central Bank.

Disbursed Loans: The amount that has been disbursed from a loan but has not yet been repaid or forgiven.

Disbursed and Outstanding Debt (DOD): The amount that has been disbursed from a loan commitment but has not yet been repaid or forgiven.

Disbursement: The transactions of providing financial resources.

Domestic Currency: It is a legal tender in the economy and issued by the monetary authority for that economy, or for the common currency area to which the economy belongs.

Domestic Debt: Gross domestic debt, at any given time, is the outstanding contractual, and not contingent, liabilities that residents of a country owe to other residents of the country that require payment(s) of interest and/or principal by the debtor at some point(s) in the future.

E

External Debt: Gross external debt, at any given time, is the outstanding amount of those actual current, and not contingent, liabilities that require payment(s) of interest and/or principal by the debtor at some point(s) in the future and that are owed to nonresidents by residents of an economy.

Euro Inter Bank Offered Rate (EURIBOR): is the rate at which euro inter bank term deposits are being offered by one prime bank to another within the European Monetary Union (EMU) zone. Such as Euribor 6 months

F

Face Value: The amount of principal to be repaid (for example, the redemption amount of a bond).

Fixed Interest Rate: A rate of interest that is defined in absolute terms at the time of the loan agreement.

Foreign Currency: A currency other than the domestic currency.

G

Government Bonds: Negotiable securities issued by the government. They are long term obligations issued with maturity of more than 5 years.

Grace Period: The period between the commitment date of the loan and the date of the first principal repayment.

Grant Element: The measure of concessionality of a loan, calculated as the difference between the face value of the loan and the sum of the discounted future debt service payments to be made by the borrower expressed as percentage of the face value of the loan.

Guarantee of a loan: An undertaking usually by a bank or a government agency to pay part or all of the amount due on a debt instrument extended by a lender in the event of nonpayment by the borrower.

H

Heavily Indebted Poor Countries (HIPCs): Group of 41 developing countries classified as being heavily indebted poor countries.

HIPC Initiative: Framework for action to resolve the external debt problems of the heavily indebted poor countries that was developed jointly by the IMF and the World Bank and was adopted in 1996.

I

Interest Payments: Payments made in accordance with the contractual terms of a loan that specify the rate of interest that are to be applied, and the way in which the interest is to be computed. The loan may have fixed or variable interest rates.

International Development Association (IDA): IDA, established in 1960, is the concessional lending arm of the World Bank Group.

International Monetary Fund (IMF): Following the Bretton Woods Accords and established in 1945, the IMF is a cooperative intergovernmental monetary and financial institution with 184 member countries.

L

Late Interest Charges: This is the additional interest that may be levied on obligations overdue beyond a specified time.

Line of Credit: An agreement that creates a facility under which one unit can borrow credit from another up to a specified ceiling usually over a specified period of time.

Loan: An agreement in which a lender undertakes to make specified resources available to a borrower. The amount of funds disbursed is to be repaid (with or without interest and late fees) in accordance with the terms of a promissory note or repayment schedule.

Loan Agreement: The legal evidence and terms of a loan.

Loan Guarantee: A legally binding agreement under which the guarantor agrees to pay any or all of the amount due on a loan instrument in the event of nonpayment by the borrower.

London Interbank Offered Rate (LIBOR): The London Interbank Offered Rate for deposits, such as the six-month dollar LIBOR. LIBOR is a reference rate for the international banking markets and is commonly the basis on which lending margins are fixed.

Long-term External Debt: External debt that has a maturity of more than one year.

M

Maturity: The debt service amounts to be paid on a particular date.

Maturity Date (Final): The date on which a debt obligation is contracted to be extinguished.

Maturity Structure: A time profile of the maturities of claims or liabilities.

Medium-Term Debt Management Strategy (MTDS): is a plan that the Government intends to implement over the medium term in order to achieve a desired composition of the Government debt portfolio, which captures the Government's preferences with regard to the cost-risk trade off.

Multilateral Creditors: These creditors are multilateral institutions such as the IMF and the World Bank, as well as other multilateral development banks.

Multilateral Development Banks (MDBs): Another term for international financial institutions, such as the World Bank Group and the regional development banks.

N

Net Flows: From the view point of a loan, the net flow is gross disbursements less principal repayments.

Net Present Value (NPV) of Debt: The nominal amount outstanding minus the sum of all future debt service obligations (interest and principal) on existing debt discounted at an interest rate different from the contracted rate.

Net Resource Transfers: Loan disbursements minus repayments of principal minus service payments during some period.

Nominal Value: The nominal value of a loan instrument is the amount that at any moment in time the debtor owes to the creditor at that moment.

O

Official Creditors: Official creditors are international organizations, governments and government agencies including official monetary institutions.

Official Development Assistance (ODA): Flows of official financing administered with the promotion of the economic development and welfare of developing countries as the main objective, and which are concessional in character with a grant element of at least 25 percent (using a fixed 10 percent rate of discount).

Official Development Assistance Loans: Loans with a maturity of over one year meeting criteria set out in the definition of ODA, provided by governments or official agencies and for which repayment is required in convertible currencies or in kind.

P

Paris Club: An informal group of creditor governments that has met regularly in Paris since 1956 to reschedule bilateral debts; the French treasury provides the secretariat.

Present Value: The discounted sum of all future debt service at a given rate of interest.

Present Value of Debt-to Exports Ratio (PV/X): Present value (PV) of debt as a percentage of exports (usually of goods and services) (X).

Principal: The provision of economic value by the creditor, or the creation of debt liabilities through other means, establishes a principal liability for the debtor, which, until extinguished, may change in value over time.

Principal Outstanding: The amount of principal disbursed and not repaid.

Principal Repayment Schedule: The repayment schedule of principal by due date and installment amount.

Principal Repayments: The payments which are made against the drawn and outstanding amount of the loan.

Private Creditors: Creditors that are neither government nor public sector agencies. These include private bondholders, private banks, other private financial institutions, and manufacturers' exporters, and other suppliers of goods that have a financial claim.

Program Allocation: A type of direct allocation for which there is a programme to account for it.

Project: A specific set of activities aimed at the development of an economic sector.

Project Allocation: Allocation of a certain amount of a loan which is going to a specific project.

Public Debt: The debt obligation of the public sector.

Public External Debt: The external debt obligation of the public sector.

Publicly Guaranteed Debt: The external obligation of a private debtor that is guaranteed for repayment by a public entity.

Public Sector: The public sector includes the general government, monetary authorities, and those entities in the banking and other sectors that are public corporations.

R

Repayment Period: The period during which the debt obligation is to be repaid.

Rescheduling: See Debt Rescheduling

Rescheduling Agreement: An agreement between a creditor, or a group of creditors, and a debtor to reschedule debt.

S

Service Charges: All charges that must be paid as a price for the loan, such as: interest, commitment fees, management fees.

Service Payments: Amounts actually remitted by the borrower to repay a debt.

Short-term Debt: Debt that has maturity of one year or less.

Spread (Margin): A percentage to be added to some defined base interest rate, such as LIBOR, to determine the rate of interest to be used for a loan.

Stock of Debt: The amount outstanding as of a moment of time.

Supplier Credit: A loan extended by an exporter to finance the purchase of that exporter's goods or contractual services.

T

Tranche: A particular portion of a financial claim or liability with its own specific terms as opposed to the general terms governing the whole claim or liability.

Treasury Bills: Negotiable securities issued by the government. In general these are short term obligations issued with maturity of one year or less. They are traded on a discount bases.

U

Undisbursed Balance: Funds committed by the creditor but not yet utilized by the borrower.

W

Write-off: A financial claim that a creditor regards as unrecoverable and so no longer carries on its books.