

Ethiopia Business Forecast Report Q2 2014

<https://marketpublishers.com/r/E864A5F48FBEN.html>

Date: March 2014

Pages: 32

Price: US\$ 1,195.00 (Single User License)

ID: E864A5F48FBEN

Abstracts

Core Views

Prime Minister Meles Zenawi's death did not have the politically destabilising effect many anticipated, and his successor Hailemariam Desalegn's adherence to the status quo should see policy continuity right until the elections in 2015. Even so, we expect ethno-religious divisions and social unrest to be a source of tension over the coming months.

Ethiopia will be among the fastest growing economies in Sub-Saharan Africa over the next few years and we are forecasting average growth of 6.0% annually between 2014 and 2018. Growth will be driven by heavy public investment into infrastructure and agriculture, and an increasingly buoyant consumer segment.

Inflation in Ethiopia has slowed markedly in recent years since reaching a peak of 40.6% year-on-year (y-o-y) in August 2011 and we expect inflation to remain relatively stable over the coming quarters, hovering broadly between 7.0 and 9.0% year-on-year. The view is based primarily on a relatively benign outlook for food prices due to favourable agricultural production prospects in the months ahead. Despite robust growth in current transfers, mainly in the form of remittance flows, Ethiopia will sustain a current account deficit in the region of 5.0-8.0% of GDP between 2014 and 2018, driven by a gaping trade deficit.

Major Forecast Changes

No major forecast changes

Key Risks To Outlook

Despite the relatively smooth handover of power following Meles Zenawi's death, political risks will remain heightened. Increasing social tensions raise the prospect of an uptick in domestic unrest, while a behind-closed-doors power struggle among the political elite could threaten policymaking.

As is the case for many African nations, Ethiopia is highly susceptible to volatility in global markets, particularly commodity prices (notably coffee and gold), which can in turn pose both upside and downside risks to export revenues and headline growth.

While inflation has slowed markedly from the high levels witnessed in 2011/12, inflation will continue to represent a key risk to macroeconomic stability. Food price inflation in particular will remain a concern, with unpredictable weather a constant threat.

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Prime Minister Meles Zenawi's death did not have the politically destabilising effect many anticipated, and his successor Hailemariam Desalegn's adherence to the status quo should see policy continuity right until the elections in 2015. Even so, we expect ethno-religious divisions and social unrest to be a source of tension over the coming months, while the country's controversial plans to construct the US\$4.3bn Grand Ethiopian Renaissance Dam (GERD) will see regional tensions continue to simmer.

Table: Political Overview

Long-Term Political Outlook

More Armed Conflict Likely This Decade

Ethiopia's much-vaunted democratisation programme - particularly a devolution of authority to the regions - is being used as a facade for ethnically-based 'divide and rule' policies designed to protect the interests of a small Tigrayan-run clique. This increasingly crude concentration of power ultimately risks exacerbating resentment to the point that largely fragmented groups could coalesce into a coherent armed threat to the regime.

CHAPTER 2: ECONOMIC OUTLOOK

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Fixed Investment, Consumer Segment To Drive Growth

Ethiopia's economy will witness strong growth over the next several years driven by heavy public investment into infrastructure and agriculture, and an increasingly buoyant consumer segment. While relatively high by regional standards, we believe that growth will remain below potential due to a weak business environment and project financing

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Despite robust growth in current transfers, mainly in the form of remittance flows, Ethiopia will sustain a current account deficit of 5.0-8.0% of GDP between 2014 and 2018, driven by a gaping trade deficit.

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We expect inflation in Ethiopia to remain relatively stable over the coming quarters, hovering broadly between 7.0 and 9.0% y-o-y. The view is based primarily on a relatively benign outlook for food prices due to favourable agricultural production prospects in the months ahead.

Fiscal Policy

Moderate Fiscal Deficits Ahead, But Challenges Await

We predict that Ethiopia will sustain a moderate, but stable fiscal shortfall over the medium term in the region of 2.0%-3.0% of GDP. Restrained recurrent spending will allow for continued emphasis on capital expenditure as the government drives ahead with its Growth and Transformation plan.

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