

AFRICA RISK CONSULTING**Country briefing – Ethiopia****19 October 2014****1 Summary**

Ethiopia will launch a debut United States (US) dollar-denominated Eurobond in either late December 2014 or early January 2015. The International Monetary Fund (IMF) calls on Ethiopia to begin a structural reform programme to achieve a private investment led economic model. Ethiopia, Sudan and Egypt hold Tripartite Committee meetings on the Grand Ethiopian Renaissance Dam (GERD). President Mulatu Teshome (2013-present) says the GERD is 40% complete and on schedule to be completed in 2017. The US embassy warns of “potential imminent terrorist attack” by al Shabaab in Addis Ababa’s upscale Bole district.

1.1 Ethiopia to launch Eurobond in December or January

Ethiopia will fund large infrastructure projects through the launch of a debut **United States (US)** dollar-denominated **Eurobond** in either late December 2014 or early January 2015. With liquidity reduced following a series of bond launches by African governments in recent months,¹ January may be a more reasonable timeframe. The bond is likely to have a minimum 10-year tenure.² The government has contracted **BNP Paribas, Deutsche Bank** and **JP Morgan** to manage the Eurobond.³

The private sector will welcome Ethiopia’s first entry into the international capital markets as it will make the state less dependent on domestic capital and borrowing, which has typically squeezed out the private sector.⁴ In March 2011, the **National Bank of Ethiopia** issued a directive forcing commercial banks to buy bonds from the state-owned **Development Bank of Ethiopia** to channel national savings into financing state-owned long-term infrastructure projects.⁵ The Eurobond will help diversify the government’s sources of credit and traditional exports so as to increase the attractiveness of the Ethiopian economy to foreign investors. The government may seek to raise as

1 FT, 15 Oct 2014.

2 Reuters, 9 Oct 2014.

3 Addis Fortune, 19 Oct 2014.

4 Source, Ethiopian economist

5 Addis Fortune, 10 Nov 2013.

much as \$10 billion from private sources over the next five years.⁶ Much of this financing will come from **China** which has invested \$5.8 billion in Ethiopia since 1999,⁷ although the Ethiopian government is keen to diversify its foreign direct investment inflows and establish connections with investors from **Turkey, Brazil, South Korea, India and Pakistan**.⁸ Ethiopia's external debt currently stands at \$12.2 billion, with a debt to GDP ratio of 23%, up from 20.5% in 2012 – 2013.⁹ The **International Monetary Fund (IMF)** warned in October that this ratio is likely to increase further due to infrastructure investments (see below).

The announcement comes a year after Hailemariam said in an interview that Ethiopia would launch a Eurobond once it secured credit ratings.¹⁰ In May ratings agency **Fitch** assigned a long-term foreign and local currency issuer default debt rating of B with a stable outlook (see *ARC Ethiopia May 2014 Briefing*).¹¹ This compared to Fitch's B+ rating for **Kenya** which issued a heavily oversubscribed \$2 billion Eurobond in June. Hailemariam also said in October 2013 that the Eurobond would not be connected to the liberalisation of Ethiopia's closely guarded financial or telecommunications sectors or prize asset **Ethiopian Airlines**. There was nothing in the announcement of the bond launch to suggest that the government will recalibrate its state-led model as it develops a plan to replace the current **Growth and Transformation Plan 2010 – 2015 (GTP)** (see below).

The continuation of the state-led model runs counter to the counsel of international finance institutions. The IMF completed its **Article IV Consultation** with Ethiopia in October.¹² While acknowledging Ethiopia's robust economic growth and single digit inflation, the IMF called on it to embark on a structural reform programme to deliver a private investment led model to ensure sustainable growth. The IMF noted that external financing, declining prices for export commodities and weather related shocks all pose a risk to the current state-led growth strategy. The IMF additionally called on the government to increase domestic revenue by broadening the tax base, improving customs and tax revenue, and removing tax exemptions. The IMF welcomed the government's planned implementation of a new oversight mechanism to monitor the operations and finances of state-owned enterprises and contingent liabilities.

6 www.ifrasia.com

7 Source, journalist, Addis Ababa

8 Source, journalist, Addis Ababa

9 www.ifrasia.com

10 Reuters, 10 Oct 2013.

11 African Capital Markets, 9 Oct 2014.

12 IMF statement, 4 Oct 2014.

1.2 Tripartite Committee begins meetings on Grand Ethiopian Renaissance Dam

Ethiopia, **Egypt** and **Sudan** have moved closer to a final agreement on the **Grand Ethiopian Renaissance Dam (GERD)** following meetings of the Tripartite Committee.¹³ Egypt remains concerned that the construction of the GERD on the **Blue Nile**, a source of the **Nile River**, will negatively affect its water supply. However, Egypt and Ethiopia maintained a spirit of pragmatic cooperation when their respective water ministers met in **Addis Ababa** on 23 September. The ministers established guidelines for the appointment of international consultants to complete studies to assess the effect on water flow and the economic and social impacts of the GERD. They also reached consensus on the rules and procedures of the national experts committee that will resolve areas of dispute arising from the studies (see *ARC Ethiopia September 2014 Briefing*).¹⁴ The studies are expected to take six months. The committee of 12 national experts – four from each country – will appoint an international consultancy firm from a list of seven that the three governments have approved. This is likely to take place during a third round of talks scheduled for November.¹⁵ The committee will also settle on an international law firm to facilitate financial and administrative issues arising from the GERD roadmap. At the second round of tripartite talks in **Cairo**, which ended on 17 October, the delegations and national experts agreed on mechanisms for sharing technical information about the GERD.¹⁶

In October, regional water ministers met as the **Nile Council of Ministers (NCOM)**, part of the **Nile Basin Development Forum**, in **Nairobi**, Kenya.¹⁷ The NCOM called on Egypt to resume its membership of the **Nile Basin Initiative (NBI)**. Nine of the Nile's riparian states formed the NBI in 1999 to facilitate the codifying of a treaty covering equitable use of and benefit from the river.¹⁸ In May 2010, five upstream states¹⁹ signed a cooperative framework agreement to replace colonial era treaties that allocate Egypt a disproportionate amount of the Nile's waters and allow it to veto upstream projects that would impact on its "*historical and natural rights*".²⁰ Egypt responded by suspending its participation in the NBI. Ethiopia and **Rwanda** are the only two signatories to have ratified the cooperative framework agreement, although **Kenya** and **Tanzania** are both likely to do so before the end of the year. While Egypt is unlikely to agree to the 2010 framework agreement, it may

13 Sudan Tribune, 28 Sep 2014.

14 MENA, 28 Sep 2014.

15 MENA, 17 Oct 2014.

16 Al Ahram, 16 Oct 2014.

17 The Reporter, 11 Oct 2014.

18 NBI member states include Burundi, DRC, Egypt, Ethiopia, Kenya, Rwanda, the Sudan, Tanzania, and Uganda. South Sudan became a member state after gaining independence from Sudan in 2011.

19 Ethiopia, Kenya, Uganda, Rwanda and Tanzania (Burundi signed in February 2011)

20 1929 treaty with Great Britain

accept a process of renegotiation.²¹ There are a number of incentives for Egypt to resume its participation in the NBI, which would provide a forum to resolve future tensions around the GERD. The NBI is a key source of investment and has leveraged \$6.5 billion in financing.²² The future of the NBI is, however, uncertain. The **World Bank's** financial sponsorship of the NBI ends in December and it will then be entirely reliant on the contributions of its member states.

The broader political context should facilitate an agreement between Egypt and Ethiopia on the GERD. Bilateral relations with Ethiopia have improved steadily since Egypt's president **Abdel Fattah al-Sisi** (2014 – present) entered office in June. Prime minister **Hailemariam Desalegn** held a meeting on the sidelines of the **African Union** summit in **Equatorial Guinea** in June and Sisi is scheduled to visit Addis Ababa before the end of 2014.²³ It is possible that during the visit, the leaders will announce a package of agreements covering electricity exports and the energy sector.²⁴

Work continues on the GERD. Ethiopian president **Mulatu Teshome** (2013 – present) announced in an interview in October that the GERD was 40% complete and on schedule to be completed in 2017 with the country starting to benefit from related annual export revenue in 2021.²⁵ Despite the regional tensions that the GERD has caused, large hydroelectric projects will be central to the successor to Ethiopia's GTP expected in June 2015.²⁶ The water ministry has confirmed proposals for the **Gilgel Gibe IV** and **Gilgel Gibe V** dams on the **Omo River**.²⁷ These will have a combined generating capacity of 2,050MW.²⁸

1.3 *United States warns of al Shabaab attack in Addis Ababa*

The US embassy in Addis Ababa warned that it had received intelligence of “*potential imminent terrorist attack*” by **al Shabaab** in a reminder that Addis Ababa continues to be an attractive target for Islamist militants.²⁹ The embassy advisory to US citizens dated 14 October warned that al Shabaab may target the upscale **Bole** district in south-eastern Addis Ababa. It did not provide a specific location for the threat but warned US nationals to avoid public places including restaurants, hotels, bars, places of worship, supermarkets, and shopping malls as potential targets. Bole is popular with

²¹ Source, academic

²² Ethiopian foreign ministry statistics

²³ Al-Hayat, 18 Sep 2014.

²⁴ Al-Hayat, 18 Sep 2014.

²⁵ Sky News Arabia, 3 Oct 2014.

²⁶ Energy Monitor Worldwide, 18 Oct 2014.

²⁷ Energy Monitor Worldwide, 18 Oct 2014.

²⁸ Energy Monitor Worldwide, 18 Oct 2014.

²⁹ Embassy statement, 14 Oct 2014.

both Ethiopians and foreigners. Ethiopian security forces continue to be on heightened alert for an al Shabaab attack since two Somalis died while constructing a bomb in Addis Ababa in October 2013 (see *ARC Ethiopia October 2013 Briefing*). Their planned target was large crowds of Ethiopians gathering around giant screens in Bole to watch a qualifier match for the 2015 football World Cup. With Addis Ababa home to the headquarters of a number of international agencies including the **African Union**, it would be an attractive target for al Shabaab to retaliate against the presence of the **African Union Mission in Somalia** or avenge the death of al Shabaab leader **Sheikh Ahmed Godane (Abu Zubayr)** in September.

Several factors decrease the probability of a successful large-scale attack in Ethiopia. Ethiopian security forces are generally more competent than their Kenyan counterparts; there is a heavy security presence throughout Addis Ababa, with local and federal police, and the military guarding key installations. The **National Intelligence Security Service (NISS)** and **Federal Police Joint Anti-Terrorism Taskforce** have a long track record of infiltrating and disrupting plots in their early stages.³⁰ Roads connecting the centre with the border regions are marked by regular manned checkpoints. There is also an ingrained ‘neighbourhood watch’ culture of reporting suspicious activity to security officials.³¹

2 Implications

The Eurobond is likely to be oversubscribed due to Ethiopia’s strong economic growth rates, limited external debt and potential market size. Ethiopia’s state-led fiscal model is expected to remain unchanged in the medium term. For businesses, the result of Ethiopia’s tightly-controlled economy is a heavy bureaucratic workload and this will not ease soon. The only departure from its state-centred approach would be if Ethiopia needed to turn to the IMF for support whose policy prescriptions would focus on encouraging a more prudent level of public investment.

The regional benefits of the GERD’s power exports – especially to Egypt, which is facing an acute power shortage – will ensure that pragmatic cooperation continues until a final agreement is in place. This is likely to be connected to the riparian states renegotiating the 2010 cooperative framework agreement.

³⁰ Source, East Africa security expert

³¹ Source, diplomatic security officer, Addis Ababa

Despite the capacity of the Ethiopian security forces, the threat of an al Shabaab attack on key infrastructure or places frequented by westerners in Addis Ababa remains high. Businesses should continue to keep security protocols refreshed and local threat information up-to-date.