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TITLE: THE IMPACT OF ECONOMIC REFORM ON THE ETHIOPIAN FOREIGN TRADE

***SUBMITTED TO*: DEPARTMENT OF MANAGEMENT**

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ABSTRACT

Ethiopia has been perusing a passive exchange rate policy having the "Birr" pegged to US dollar which is believed to have imposed an adverse impact on economic efficiency and growth, especially which makes production for export unprofitable while imports become artificially cheaper resulting in increased smuggling of exportable goods. So, an over valued exchange rate would lead to persistent trade deficit since it makes earnings from export to decline. In addition, as the country was following command economic system, the micro economic management of Ethiopia was poor. In general policy problems, markets structural constraints, and natural factors have been the major problems to Ethiopian foreign trade. Due to these, the current account of the balance of payment has been widening form time to time.

However, after the fall of the derg military regime, a package of policy measures have been undertaken with the objective of encouraging exports, while discouraging imports and there by improve the external performance of the country. Among these, trade liberalization, currency devaluation and reduction in export duty can be mentioned.

This study is aimed at the assessment of the progress in external performance of the country as attributed to the reform program. The data needed (secondary data) was collected from ministry of trade and industry, central statistics bureau, Customs Authority and National Bank of Ethiopia all located in Addis Ababa. The data was analyzed quantitatively and descriptively; and interpreted on comparative basis and the report includes multiples of tables and chart showing yearly improvement in external performance of the country. Comparison is also made between average terms of trade (ratio of export to import) over a decade, before and after the reform. Emphasis has been also given to the degree of improvement in export and import ratio to GDP of the country.

The major recommendation is that the country should diversify its product and market and seek ways to improve quality of the existing products.

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Part One

1. INTRODUCTION

Like many other sub Saharan African countries Ethiopian has faced serious economic crises through out the mid 1970's and the entire decade of 1980's. This economic crises brought low growth rate of gross domestic product (GDP), negative growth rate of per capita income and increased balance of payment deficit, huge debt services followed by accumulation of arrears.

Among the various sectors, Agriculture was hard hit, Agricultural output in general and food production in particular grew at a rate lower than population growth forcing the country to either import basic necessities or to depend on external donation.

The cause of these poor economic situations is many and varied. Some people put the blame on the deteriorating terms of trade, Even though this contribute to the worsening of economic situation and (crises) by far the most important causes of poor economic situation and or performance can be attributed to the over all macro economic management. This is again manifested in the way it promotes efficiency in the utilization of resources. In general the macro economic polices of Ethiopia have led to the distortions in all sectors of economy. The end of civil war in 1991 and, subsequent establishment of the Transitional Government, have ushered in a new era of radical transformation in both political and economic spheres. The comprehensive economic reforms introduced in 1992 envisaged to eliminate distortion in the economy and regain internal balances thereby promote sustainable growth development in all sectors.

Since 1992, a package of policy measures has been undertaken with the objective of encouraging exports, while discouraging imports. Among these were realignment of currency by devaluating it, which is likely to improve the external trade deficit through its effect on both export and imports; removal of takes and duties on exports, streamlining of export licensing procedure and export credit guarantee shemes.

This study is aimed at the assessment of the impact of the reform (primarily devaluation of national currency) on the trade balance of Ethiopia. Basically, devaluation is expected to improve the international competitiveness of devaluing county and devaluation is also expected to improve the current account and balance of payment position by changing the relative price of home as well as foreign goods. Other wise stated, the aim of devaluation is to reduce the demand for foreign exchange reducing the demand for imports and to increase the supply of foreign exchange by exporting more goods and services. Other things remaining constant or the same, devaluation raises the domestic currency price of imports and reduces currency price of exports by changing relative price of home and foreign goods and services of the devaluing country.

2.LITRATURE REVIEW

The Ethiopian currency (Birr) was pegged to the U.S dollar at the rate 2.07 per dollar during the period between 1973 to October 1992. Despite changes in the domestic & foreign prices indices as well as floating exchange rates of the country's trading partners, the exchange rate of Birr remained fixed during the above stated period.

Hence the country had been perusing a passive exchange rate policy having the "Birr" pegged to the U.S. dollar. The basic problem of an overvalued exchange rate is an adverse impact on economic efficiency and growth. Especially it makes production for exports unprofitable while imports become artificially cheaper resulting in increased smuggling of exportable goods. So an over valued exchange rate would lead to persistent trade deficit. This is because over valued exchange rate makes earnings from export to decline. Therefore, devaluation helps to stabilize export price distortions.

In theory and under the most common conditions, nominal devaluation will affect an economy in three main ways. First devaluation will usually have an expenditure reducing effects. Second it will tend to have an expenditure switching effect. This involves shifts in the pattern of domestic demand from tradable to non tradable, and the patterns of domestic production from non tradable to tradable. The combined effects of expenditure reducing and expenditure switching will of course improve the external situation of the country.

Third, devaluation will increase the domestic price of imported intermediate inputs and imported capital goods. This will increase the cost of production and results in a contraction of real out put or aggregated supply.

The immediate objective of a nominal devaluation is to reduce or eliminate the misalignment of the real exchange rate by generating a real devaluation, which would improve the international competitiveness of the country with ultimate goal of improving the external position. The accomplishment of this will depend on the conditions prevailing before devaluation and accompanying policies implemented with devaluation.

Generally the whole idea of devaluing a national currency is mainly to provide incentive to export products and traders by increasing their export income in local currency.

However some analyses argue that devaluation may not insomes have the expected effects of increasing earnings and encouraging imports substituting firms. As a single or few agricultural commodities dominate the trade structure of developing countries' export, there would be considerable time lag before devaluation results in a positive response. There may also be unfavorable world price for those commodities, further the prospects of diversifying the export structure is even very difficult with in a short period of time.

It was argued that devaluation could be inflationary. Therefore, it fraught with adverse social consequences, especially for the poor imported consumer goods would become more expensive and production of manufactured goods & cost of agricultural inputs would rise aggravating the inflationary aspects of devaluation. Since the impact of inflation is much greater than low-income groups, the opponents of devaluation argue that it is bound to have undesirable social impacts.

The inflationary consequences of nominal devaluation will also increase the budget deficit because inflation affects the public expenditure price. Therefore, the pap between expenditure and revenue widens when fiscal revenue lag behind expenditure. However proponents of devaluation argued these inflationary consequences of devaluation can be minimized by taking other appropriate polices along with the devaluation. The effects of devaluation can also be sustained if supporting polices particularly measures to control growth of money are adopted. In general appropriate polices (such as restrictive monitory policy) are needed so that the rise in exchange rate of Birr is not neutralized by an increase in domestic prices.

Devaluation also have domestic political advantages since it is one way to reduce a current account deficit with out implementing austere economic polices such as reducing government spending, raising taxes or cutting subsidies.

Government sometimes coordinate devaluation with other fiscal and monetary polices for instance if a country increased government spending and lowered interest rates to stimulate economic growth, the resulting inflationary pressures and lower rate of return on investment might mean that at present exchange rate of foreign demand for the countries currency would decrease. The government might devaluate in order to reverse the decline and stimulate the demand for its currency to make its investments (exports) more attractive.

Under a floating exchange rate system the decline or rise of currencies foreign exchange value is not refereed to as devaluation or revaluation, instead, an increase or decrease is refereed to as appreciation or depreciation respectively. Depreciation is a process that occurs overtime due to market forces, possibly influenced by government action that may be prompted by changes in economic conditions.

2.1. OBJECTIVE OF THE STUDY

❖ **General Objective**

To get in sight in to the impact that changes in economic policy has imposed on the deficit in the current account of the balance of payment. In other words, it is aimed at assessing the improvement in the external performance of the country as attributed to the reform and suggests some appropriate measures to be taken.

❖ **Specific Objectives**

- Assessing major problems to the foreign trade sector and improvement in volume and value of export after the reform comparing it with pre reform.
- Assessing the improvement in export value as a percentage of GDP and imports payment.
- Assessing the improvement in imports as measured by its ratio to GDP.

2.2. STATEMENT OF THE PROBLEM

In the 1970's and 1980's the foreign trade sector of the country has generally revealed a sluggish performance. This can particularly be observed if we look at the ratio of exports to GDP and imports as well as the growth rate in export earnings which showed a general stagnation and declining trend in the 1980's. The importation of basic investment goods had been hampered by the poor export performance.

In other words, there has been deficit balance of payments which makes the country to look either for external or domestic financing. External financing (borrowing) in turn would divert the government's attention from public expenditure.

2.3. SIGNIFICANCE OF THE STUDY

The government to help remedy the current account deficit, which occurs when the country is buying more from its trading partners than it is selling to them, has under taken a package of policy measures; devaluation of national currency, and trade liberalization, among others can be mentioned.

In spite of these efforts, currently the country's major export commodity (coffee) price has shown a sharp decline, on the one hand, high cost of agricultural product due to sky rocketing of the price of fertilizer, on the other hand. This has become chronic head ache for the nation. The severity of this problem necessitated the study in which assessment in external performance would be made and subsequently some appropriate measures that need to be taken to over come the problem is recommended. That is the essence of this study.

3. METHODOLOGY

Ethiopia is one of the countries that face a secular decline in their terms of trade and the benefit they gain from external trade is minimal. This is attributable to low elasticity to its products and reduction in the amount of raw materials need for industrial production in developed countries through technical innovations. (World Bank, 1987).

In addition, policy constraints like high burden of tax on export commodities, strict control on coffee trade and absence of export promotion programs can be mentioned. After the fall of the derg regime, however, Ethiopia has undergone dramatic changes and a range of reforms have been implemented including the complete liberalization of trade, the devaluation of national currency and adoption of export promoting program. This was aimed at boosting the external performance of the country.

The researcher aims in this study at the general assessment of the impact that those policy measures have imposed on the deficit of the current account of the balance of payment.

The data has been collected from central Statistics Authority, National Bank of Ethiopia, Ethiopian Customers Authority and Ministry of Trade and Industry, all located in Addis Ababa.

The scope of the time covered in this study is the years 1970'$_s$, 1980$_s$, and 1990$_s$.the study was conducted from December up to May

1994EC. It was found easy to divide the whole study time into pre and post reform time for comparison of the performance.

The data was analyzed quantitatively and descriptively. Descriptive analysis involves the computation of the value of import and export growth rate and trade balance over decades of two periods (pre and Vs post reform time). Emphasis is also given the comparative improvement in the ratio of export to import and GDP during the time mentioned.

Quantitative analysis focuses on the computation of the value of export and import & visible trade balance of the country.

The report encompasses multiple tables and charts (at the appendix) showing the value and volume of export and import and balance of payment over the study period.

Limitation

Though the study had revealed quite important implications on external performance of the country, it would be a must to mention few words about several limitation of it.

- The time and financial budget allotted for the study was not enough.
- Absence of enough proximity to adequate source of information.

Part Two

RESULTS AND DISCUSSION

1. Overview of the Ethiopian foreign trade

Ethiopian foreign trade, which has been characterized by commodity concentration (high dependence on agricultural exports, coffee, in particular) to Europe, North America and Japan, indicates the system of unequal exchange in international trade.

Constraints to this sector can be classified in to broad categories, namely demand and supply side problems or internal and external, and other constraints.

The world demand for agricultural products (Ethiopia's major export items) is limited due to slow growth of population, low income elasticity of demand for these goods, the development of agricultural substitutes and synthetic materials in industrial countries. Beside these the world price of primary products are characterized by price fluctuation and deteriorating term of trade.

On the other hand, policy problems, structural constraints and natural factors (draught, disease etc..) are major factors which constraint Ethiopian's foreign trade, Demand and supply side problems together have led to ever-growing trade deficit which directly affects the size and signs of the current account balance. As a result, the deficit in the current account of the balance of Ethiopia has been widening from time to time. This deficit is covered mainly through external finance and this would lead to ever-increasing debt burden.

The relative unattractiveness of legal exports and strict control on coffee and other trade by the derg regime has provided incentive to illegal exports of coffee, gold, live animals, fruit vegetables and chat, " it is estimated that about 225 thousands heads of cattle, 759, thousand heads of goat and sheep, and 100 thousand camels are illegally exported annually by traders and pasturalists to Djibouti, Somalia, Kenya and Sudan" (GASHAW; 1992). Although there are no reliable estimates of smuggled exports according to same sources (GASHAW),

Coffee and live stock alone amount to 185,000,000 per annum in the years before economic reform. This is about 46% official exports in 1990/91. There fore, in addition to unfavorable external factors, which brought about a deterioration of terms of trade, smuggling of export able goods mainly due to over valuation of the exchange rate has severely affected the export sector. It is also interesting to note that the total value of exports substantially increased after the reform, despite the fact that the structure of exports has remained the same (Agricultural product dominated).

2) *The impact of the reform on external trade deficit.*

Since 1992, a package of policy measures has been undertaken or implemented with the objectives of encouraging exports, while discouraging imports. Among these were: devaluation of national currency, which is likely to improve the external trade deficit through its effect on both exports & imports, removal of taxes and duties on exports, streamlining of export licensing procedure and export credit guarantee schemes.

To see the impact of reform on external trade position of Ethiopia, it is better to see its effect on export sector and imports separately.

2.1 Exports

Devaluation would enable exporters to offer competitive prices there by bring about switch from an unofficial to official export market. More over, it channels exportable products from domestic consumption to exports by increasing the domestic currency price of such commodities. More importantly, it encourages production of exportable goods even though it needs a long period of time for its response to a policy measure. Further more, it encourages non-traditional exports to come into the international market, that is it enhance diversification of exports.

2.1.1. The export structure of Ethiopia

As stated earlier, the fact that exports sector of Ethiopia is concentrated on a few primary commodities is one of the major problems of Ethiopia's foreign trade. This structure has not significantly changed over time. Coffee has still remained being the dominant export commodity. It accounted for an average of 60% export between Ethiopian fiscal year 1970/71 and 1999/00(Tables 1).

Table 1:- Average share of major export items in total export value.

Period	Coffee	Oil seeds	Hides skins	Pulses	Chat	Total	Industrial products *
1970/71-1980/81	55.6	7.1	10.5	8.1	0.7	82.0	3.3
1981/82-1991/92	61.3	1.7	14.4	2.8	2.2	82.4	8.8
1992.93-1999/00	64.1	3.9	11.6	2.4	8.1	90.2	2.8
1970/71-1999/00	60.3	4.3	12.2	4.5	3.7	84.8	5.0

* Includes sugar, oil lakes and petroleum products

Source: - National Bank of Ethiopia Quarterly Bulletin, various issues.

Oil seeds, hides and skins, pulses and chats constituted 4.3%, 12.2%,4.6% and 3.7% during the same period respectively. The share of coffee together with the latter four items averaged 84.8%. This confirms the limited diversification of export sector.

The shift towards the export of manufactured goods is not so much impressive. The export of processed goods contributed, on average, only 5% to the total export earning during the period mentioned.

Apparently, the absence of diversification & high dependence on specific commodities have exposed the export to external shocks. Specially, heavy reliance on a single commodity, coffee, has negative impact on the export receipts and the growth of the economy in general.

1. The Coffee- Sector

As already noted, the coffee sector is the principal foreign exchange earner for the country. It also provides direct and indirect employment opportunities for more than 25 percent of the population.

Arabica coffee that contributes more than 75 percent of the world's coffee production is believed to be indigenous to Ethiopia. Because of this, the country is African's leading exporter of Arabica coffee. Which is the best quality (ECEA, 1998)

It is also plausible to say that, the country is unique in Africa in the sense that there exists high domestic consumption of coffee.

Nevertheless, the country's supply of coffee in the world market is extremely low. Its share of the world coffee does not exceed 2.7 percent. The smallest share of 0.9% was registered in 1991/92 due to the negative effect of war on the economy. The largest share was 2.7% recorded in 1997/98.

Some problems to the sector

i) *Policy constraints. (INTERNAL CONSTRAINTS)*

The coffee sector though crucial for the economy has not been developed yet. During the imperial regime, there had been some commercial farms until they were nationalized by the derg regime. There had also been market based marketing structure during the period. Coffee had been shipped to the central markers at Addis Ababa and Diredawa where auctions were conducted

When the economy was under the whim of the socialist ideology small producers were forced to sell coffee to service co-operatives and to the Ethiopian coffee-marketing corporation (ECMC). Export of coffee was conducted almost entirely through ECMC. Taxes levied on coffee were also substantial. According to the World Bank (1987), the taxes on coffee at the time, i.e. coffee surtax transaction taxes an export duty and coffee cess took up 37-50 percent of the coffee export (F.O.B) price. As a result producers prices were too low discouraging small farmers to produce coffee. Due to all these problems, there were several cases where farmers had to up root their coffee trees to replace with or plant cereal crops on the land. "(Itana 1999)"

Currently, however, the government has adopted various measures to remove the policy bottlenecks that the sector had faced. Taxes have been reduced and the previous three types of taxes. (Coffee duties, Surtax and coffee cess) have been consolidated into a flat rate of 6.5 percent of F.O.B price (see proclamation No 99/1998).

ii) External factors

Among the external factors that impede the export of coffee includes the variability of international prices and the existence of competing coffee exporters from other countries with better quality than that of Ethiopia. When there is improvement in the coffee price, there would be subsequent rice in its supply particularly since Brazil is the major competitor of coffee Arabica. Price fluctuation depends on the production and supply of coffee from that county. Whenever the coffee production is boosted in Brazil, the world price for coffee falls.

If we look at the world price for coffee, price gradually declined in the 1960's, but increased until early 1970's. After showing marginal decline in mid 1970's prices again surged up, as the Brazil coffee was hard hit by frost in 1974/75. Latter, a significant rise in prices was registered in 1985/86 and 1994/95.

iii) Other constraints

The other problem associated with the marketing of Ethiopian coffee, in general, is the remoteness of most coffee growing regions from the centers which, leads to substantial costs of transporting coffee to the auction centers to port and to importing countries.

These transport costs may not change no matter what the prices of the coffee in the world market are. As already mentioned, all types of coffee are auctioned either at Addis Ababa or Diredawa, which are at far distant from the coffee growing regions. Further more, weather, conditions affect both the quality of coffee export.

2. Non - Coffee Export

The major non - coffee export commodities of the country include among others, oilseeds, pulses, hide and skins, chat, sugar, oil cakes, live animals, meat and meat products and bees wax. The volume of non-coffee exports was on the average 340 thousand metric tons between 1972/73 and 1974/75 but declined to 157 thousand metric tons during 1990/91-1992/93 (Table 2). After showing a recovery to 235 thousand metric tons between 1993/94-1995/96, it again went down to 169 thousand metric tons during 1996/97-1998/99.

Table 2:- Annual average volume of major None- coffee exports (in thousands of metric tons.

Period	Oil seeds	Hides & skins	Gold	Pulses	Meat & Meat Prod.	Fruits & Veg.	Sugar & Mollies	Oil cakes	Live animals	Chat	Petrol. prod.	Bees wax	Total
1972/73-1974/75	100.2	12.1	-	122.4	9.1	28.1	18.1	38.7	8.7	2.2	0.0	0.6	340
1975/76-1977/78	30.8	9.4	-	75.7	2.0	15.9	16.0	32.0	8.1	2.0	0.0	0.6	192
1978/79-1980/81	10.3	19.3	-	28.1	1.8	7.1	25.7	25.6	2.4	1.8	0.0	0.5	122
1981/82-1983/84	18.3	9.7	-	56.0	2.5	7.9	37.1	29.8	4.1	2.7	0.0	0.4	168
1984/85-1986/87	10.1	10.7	1.8	10.4	1.2	11.3	43.8	6.6	6.3	1.7	125.1	0.3	229
1987/88-1989/90	10.0	9.0	2.4	16.2	0.8	9.9	32.4	5.5	10.6	1.9	189.0	0.2	287
1990/91-1992/93	1.0	5.0	9.1	5.9	0.1	8.7	15.4	1.0	0.9	1.2	109.3	0.1	159
1993/94-1995/96	10.0	8.4	5.1	21.6	0.5	18.1	5.1	0.0	1.1	3.5	161.8	0.3	235
1996/97-1998/99	44.0	7.4	5.1	30.4	1.9	19.4	6.6	0.0	1.2	6.9	46.8	0.6	169

Source:- NBE, Quarterly Bulletin and annual report,
Various issues

The down ward trend in the volume of none- coffee exports was entirely attributed to the decline in the export of almost all components. Export of oil seeds and pulses, which contributed larger share of non-coffee exports in the early 1970's showed a significant decline at the eve of the 1992 reform programme. These two items experienced a substantial decline from earlier respective position 100.2 and 122.4 thousand metric tons between 1972/73 and 1974/75 to 1.0 and 5.9 thousand metric tons through 1990/91-1992/93, but revived to 44.0 and 30.4 thousands metric tons during 1996/97 - 1998/99. The main reason for such decline is that the peasants shifted towards growing cereals for their food requirements as well as the profitability of cereals was more than that of oil seeds and pulses (World Bank 1987). The export volume of hides and skins meat and meat products, fruit and vegetables, sugar and molasses, live animals and Beeswax, also followed the same lines of development. On the other hand, the export of oil cakes went down to nil in the most recent years. The export of chat. However, has been increasing.

When we consider the export value of these items, it also followed the same trend, as was the case in volume.

The volume declined from USD 131 million during 1972/73-1974/75 to USD 127 million between 1984/85 and 1986/87. Nevertheless a reasonable foreign exchange earnings were obtained and reached to the peak of USD 1,893 million during 1996/97 - 1988/99. This was mainly obtained from the export of Gold, Chat. hides and skins and oil seeds that registered USD 850.3, USD 305.6 million, USD 300.3 million and 220.1 million respectively.

Table3:- Annual average value of major non coffee exports
(in million of USD)

Period	Oil seeds	Hides & skins	Gold	Pulses	Meat & Meat Prod.	Fruits & Veg.	Sugar & Mollies	Oil cakes	Live animals	Chat	Petrol. prod.	Bees wax	Total
1972/73-1974/75	38.3	26.2	-	37.5	7.1	4.6	5.1	3.6	5.6	2.2	0.0	1.1	131
1975/76-1977/78	11.9	24.7	-	21.2	2.1	3.3	2.1	4.0	5.9	2.5	0.0	1.6	81
1978/79-1980/81	8.3	54.6	-	10.7	2.2	2.4	3.9	3.8	3.2	7.9	0.0	2.0	99
1981/82-1983/84	10.5	42.6	-	12.8	3.4	2.9	4.4	4.7	6.3	14	0.0	1.4	103
1984/85-1986/87	5.0	45.4	33.8	4.6	1.8	4.0	5.2	0.7	7.6	9.8	8.5	0.8	127
1987/88-1989/90	6.7	62.8	64.4	8.8	1.4	6.2	10.0	0.4	10.3	8.4	13.1	0.6	192
1990/91-1992/93	0.7	33.2	261.6	2.9	0.2	3.1	3.3	0.0	1.0	8.5	9.4	0.3	324
1993/94-1995/96	45.4	295.6	351.7	69.4	6.3	15.2	9.3	0.0	6.4	151	76.5	6.7	1034

Source:- NBE, Quarterly Bulletin and annual report,
Various issues

The export volume of processed goods such as oil cakes, sugar and molasses and petroleum products declined after the reform programme despite the removal of the policy constraints including the over valuation of the national currency and export taxes. The problem, therefore, lies not only on the policy constraints but also on other structural constraints as can be observed from the following quotation.

" This puts the crux of the problem not on these broad policy issues related to liberalizing foreign trade., but on the capabilities of foreign firms to go through the necessary process of technological change to a sufficient leve of productivity increment in order to be competitive in the international market, on the one hand , and a concerted country wide strategy to encourage the development of such firms peared towards the promotion of manufactured exports on the other hand. The absence of clear strategy towards the manufacturing sector and the orientation of the existing manufacturing sector towards meeting the consumption requirement of the domestic has meant that little attention has been paid to improve the efficiency of firms and the quality of their products to enable them to export at desired level" (Befikadu and Berhanu, 1999/2000:225)

*2.1.2 **Direction of Ethiopia's Export***

Ethiopia's foreign trade, which has been characterized by commodity concentration (high dependence on agricultural products), also, shows a limited market concentration. The flow of exports has remind to be to the same destination as had been for a long period to

Europe, North America, Asia (mainly Japan) and few countries from Africa.

The share of African nations had been the lowest especially before 1990s. Djibouti imports the largest share of Ethiopia's export to Africa.

Trade with African nations is very much limited despite strong efforts made by African leaders to promote regional trade and integration.

Lack of economic diversification, heavy debt burden and impacts of globalization, among others can be mentioned as the factors that have been inhibiting African's economic integration. How ever the idea of transforming OAU into African union if effective can be a turning point in integrating African's nations so that promoting the trade between Ethiopia and other African countries.

The most important European markets are Germany, Italy, France, and the United-Kingdom (UK). Germany is the leading importer of Ethiopia's goods in Europe. The United States from America and Japan and Saudi- Arabia from Asia are the major destination for Ethiopian's exports.

In the 1970's and 1980's the export sector of the county has generally revealed a sluggish performance. This can particularly be observed of we look at the ratio of exports to GOP and to imports as a well as the growth rate in export earnings. Accordingly, exports as a percentage of GDP that registered 8.1 percent in the 1970's declined to

6.1 percent during 1980's (table 4). In particular, export earning have showed a general stagnation and declining trend in 1980's as its growth rate averaged 1.4 percent during the period.

Due to such unsatisfactory performance of the export sector, receipts obtained there from were insufficient to finance imports. The share of exports in imports financing had declined from 80.3 percent in the 1970's to 42.4 percent in the 1980's. This implies that the importation of basic investment goods had been hampered by the poor export performance.

The poor performance of the export sector during 1980's was attributed to different factors, including, bad weather condition, problem in production & marketing, pervasive impact of international commodity market for exports and low elasticity of demand and supply for exports (GHIORGIS, 1992. Alemayehu. 1999). The significant over-valuation of exchange rate together with high export tax rat also contributes to the reduction of the profitability of exports interms of local currency (WORLD BANK, 1982).

During the early 1990_s, there was even more declines in total exports, Export earning was only 1.5% of GDP and covered 7.6% of imports in 1991/92 (Table 4). This was the lowest figure ever registered during 1970/71 - 1999/00 and this can be traced back to the heightened civil war. There was, however, a recovery observed in the late 1990_s that is since the introduction of the economic reform. Regarding the diversification of exports, there has been no change in Ethiopia's export so far. It is still marked by luck of stead- fastness.

Table 4 :- Ratio of exports (EXP) to GDP and to imports (IMP), and imports (IMP) to GDP (%) and growth rate of IMP & EXP.

Year	EXP/GDP	EXP/IMP	IMP/GDP	EXP Growth rate	IMP Growth rate
1970/71	5.9	69.1	8.6		
1971/72	5.8	69.2	8.4	3.0	
1972/73	8.1	103.9	7.8	40.0	
1973/74	10.1	114.5	8.8	32.1	
1974/75	7.3	71.0	10.2	-20.1	
1975/76	8.2	79.3	10.4	12.7	
1976/77	9.1	86.4	10.5	19.2	
1977/78	8.3	84.1	9.9	4.3	
1978/79	8.7	61.1	14.3	11.1	
1979/80	10.0	64.7	15.4	27.6	
Average	8.1	80.3	10.4	13.0	
1980/81	8.4	61.5	13.7	-10.4	
1981/82	7.3	47.4	15.4	-8.6	
1982/83	4.3	29.1	14.9	4.0	
1983/84	7.1	45.0	18.8	14.8	
1984/85	5.7	42.1	13.6	-19.9	
1985/86	6.9	42.6	16.3	24.1	24.3
1986/87	5.6	36.2	15.5	-13.9	1.6
1987/88	5.3	34.6	15.2	-2.7	1.7
1988/89	5.8	43.5	13.4	16.7	-7.2
1989/90	4.5	41.5	10.5	-18.4	-13.6
Average	6.1	42.4	14.8	-1.4	1.4
1990/91	3.0	26.9	11.1	-26.4	16.8
1991/92	1.5	17.6	8.7	-48.6	-15
1992/93	3.5	26.2	13.5	18.6	99.8
1993/94	5.0	29.9	16.7	24.2	31.0
1994/95	8.4	43.3	19.3	120.3	38
1995/96	6.9	33.8	20.3	-8.1	17.8
1996/97	9.4	45.8	20.5	12.3	17.1
1997/98	9.2	44.3	20.7	12.3	17.1
1998/99	7.1	30.0	23.8	-22.3	16.8
1999/00	7.1	104.1	23.6	4.2	3.9
Average	6.1	40.2	16.2	10.8	22.2

2.2 *Imports*

Devaluation discourages imports by making imports relatively more expensive and provides a spur to greater import substitution. Import substitution creates domestic industries to produce for local use some of the goods, which were previously imported (saving of foreign exchange).

The main advantage of import substitution is that these will be a reduction in the relative importance of foreign trade to the economy; thus reducing the vulnerability of the economy to externally induced fluctuation (Equar Desta: 1999). In general devaluation by discouraging imports, help a devaluing country to save its foreign exchange so that to use it in priority sectors.

What does the import sector of Ethiopia tell us during the last two decades?

2.2.1. *The structure and performance of the import sector*

The structure of import has basically remained the same in 1980_s as well as early 1990_s though noticeable changes were made in the relative size of individual commodity categories. Capital and consumer foods and fuel have been the most important items. Capital and consumer goods accounted for 30 percent of total import.

The share of consumer goods increased from 26 percent of total import in 1987/88 to 35 percent in 1993/94. It later reduced to 23 percent of the total import value in 1996/97, but increased to 30 percent in 1999/00.

The importation of non-durable goods had shown a trend of increment but later, declined during the time period considered. The value of semi finished goods has also shown a decline during early 1990_s, but it has increased in late 1990_s.

In general as can be seen from the (Table 5) one can under stand that Ethiopia imports industrial products mainly capital goods, consumer goods, durable and non-durable goods.

Table 5:- Imports by end use as the percentage of total imports

	YEARS												
	1987/ 88	1988/ 89	1989/ 90	1990/ 91	1991/ 92	1992/ 93	1993/ 94	1994/ 95	1995/ 96	1996/ 97	1997/ 98	1998/ 99	1999/ 00
Raw materials	2.4	2.6	3.2	2.7	1.57	5.96	1.82	2.0	2.3	2.2	2.4	1.8	1.6
Semi-finished goods	17.6	20.6	17.6	12.0	8.79	9.02	16.29	17.0	16.4	19.2	18.6	18.5	19.1
Fuel	9.5	10.1	12.3	9.9	13.77	22.68	15.3	15.2	12.1	16.5	17.6	11.7	18.0
Capital goods	47.1	39.00	38.6	45.3	25.84	34.97	29.23	31.9	33.7	36.7	32.2	35.9	33.4
Consumers goods	26.3	30.8	28.1	30.2	29.75	31.3	35.12	32.5	31.6	23.0	27.1	30.2	29.6
Durable	8.6	9.5	12.0	10.0	7.59	7.25	9.76	8.7	9.3	8.5	8.2	11.1	10.2
Non- Durable	17.8	21.3	15.7	20.2	22.15	24.1	25.4	23.8	22.3	14.5	18.8	19.1	18.5
Miscellaneous	8.0	0.1			20.29	0.1	2.20	1.5	1.9	1.1	0.3	1.9	2.8

Source:- National Bank of Ethiopia

Imports rose steadily from 1991/92 to 1999/00 except in 1996/97 from 1,810.9 million birr to 10,495 million in 1999/00.

After 1985 onwards up to the Ethiopian fiscal year 1991/92. The import of the country was showing an increase on average value 1.4 percent. Nevertheless, after the economic reform has been introduced. i.e Form Ethiopian fiscal 1992/93 up to 1999/00 22.2 percent growth rate on average value has been noticed (Table4).

Under the pervious regime, imports as a share of GDP claimed 15 percent, but then declined to less than 10 percent in 1991/92. During the past 1992/93 period; however, the value of imports as a percentage share of GDP increased to more than 20 percent (Table 4).

Generally speaking, devaluation and other economic reform has not so much discouraged imports though there has been an improvement in export receipts. The percentage of import payments, exports covered in 1990_s (40.2) was lower than that of 1980_s (42.4 percent) mainly because of a rise in import to GDP ratio during 1990_s (Table 4). Consequently, in absolute terms, trade balance deficit further deteriorated following reform.

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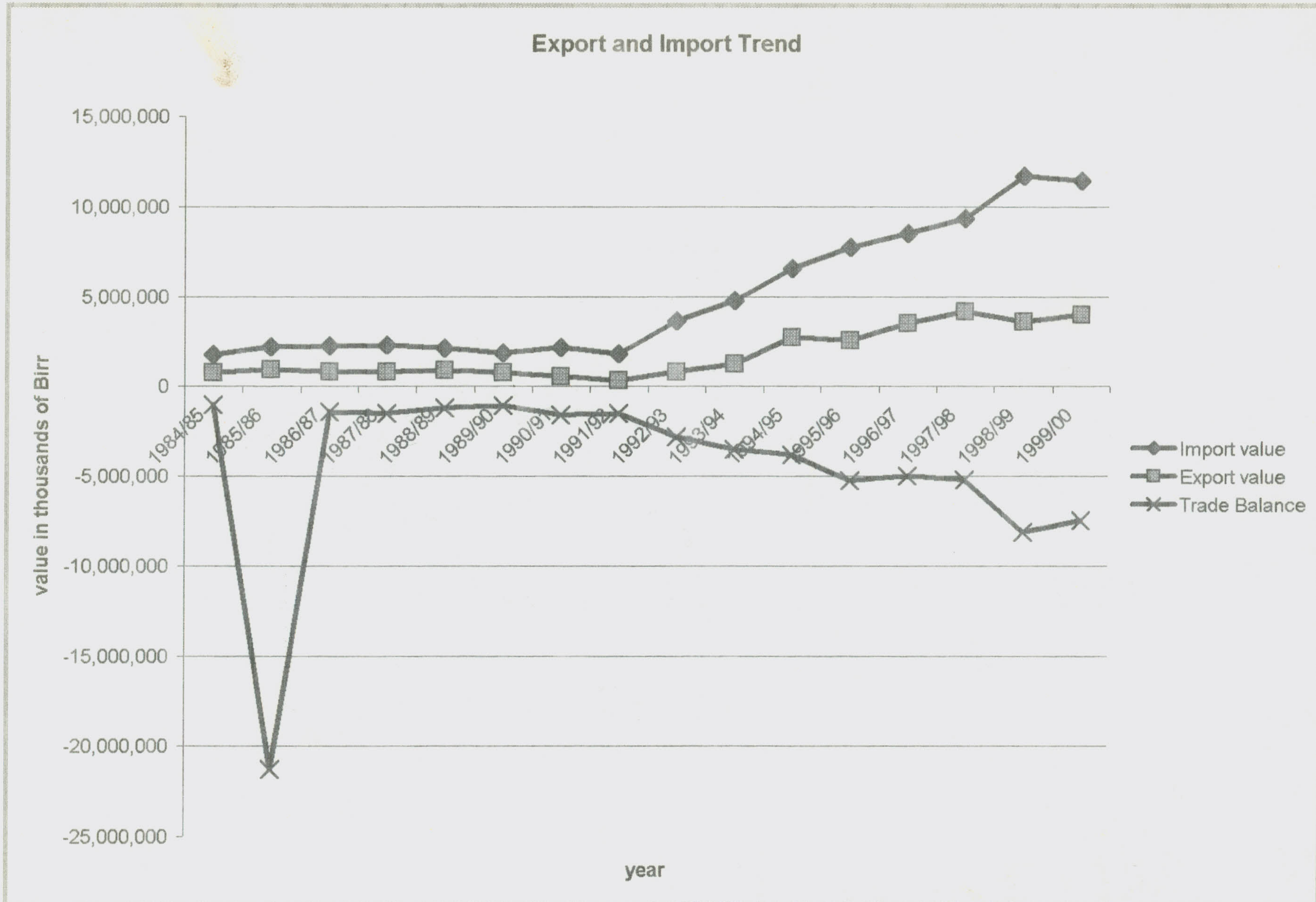

Export and Import Trend
15,000,000
10,000,000
5,000,000
0
-5,000,000
-10,000,000
-15,000,000
-20,000,000
-25,000,000
value in thousands of Birr
1984/85
1985/86
1986/87
1987/88
1988/89
1989/90
1990/91
1991/92
1992/93
1993/94
1994/95
1995/96
1996/97
1997/98
1998/99
1999/00
year
Import value
Export value
Trade Balance

Part Three

CONCLUSION AND RECOMMENDATION

In the first part of this paper, some policy measures that has been undertaken by the current Ethiopia's government to boost the country's international competitiveness and thereby improve the trade deficit; arguments for and against devaluation of national currency on the literatures; objectives and significance of the study, and finally the methodology used, has been discussed. In the second part, overview of the Ethiopian foreign trade and post reform external performance of the country as compared to the pre reform performance has been discussed.

According to this study it is observed that Ethiopia's foreign trade structure is characterized by lack of product and market diversification with heavy reliance on agricultural products (accounting for about 90 percent of the total export during the post reform years). Coffee has been the single most important foreign exchange earner (accounting for 60 percent of the total export.).

The demand for agricultural products is characterized by low income elasticity. Further more high volatility of world price for these products has increased the country's vulnerability to external shock.

Market concentration also puts a negative impact on export sector of the country. America, Europe, Asia and few countries from Africa have been the main focus for Ethiopian's export.

The export sector has shown a bit improvement both in its volume and value growth rate and percentage to gross domestic product (GDP) after the reform as viewed comparatively with figures during 1970$_s$ and 1980$_s$.

Regarding the sector industrial goods mainly, capital goods, consumers' goods, durable and non-durable are the major components. These goods have high-income elastic demand.

Under the previous regime imports as a percentage of GDP claimed 15 percent, but increased to 20 percent after the reform.

The percent of import payments, an export covered in 1990s (40.2) was lower than before 1990$_s$ (42.5). Though there has been improvement in export receipts payments for import increased significantly outstripping the export recovery. In sum, trade balance deficit further deteriorated following the introduction of the reform.

RECOMMENDATION

Ethiopia needs to diversify its export product by developing sectors like textiles and leather products and pave the way to shift towards the export of semi processed and industrial goods in order to become less dependent on the volatile coffee market.

There is also a need to diversity the market for exports. The contribution of the private sector in seeking market and advertising our coffee in international market has been insignificant. So, the government in close cooperation with private sector should undertake studies that enable to identify potential market for the different varieties of coffee, which the country is endowed with, and other export items of the country. Thus, much commitment is needed from the government and private sector as well.

There has been little attention paid to improve the efficiency of firms and quality of their products to enable their export at desired level. To enhance market and price competitiveness of the existing products, a huge investment should be made in quality improving technology.

The government should set clear strategies, which would build domestic firms' calpability and competitiveness in international market. In this regard the export trade duty incentive schemes, voucher system, duty draw back and bonded manufacturing ware house schemes, which has been under taken recently are to be welcomed and encouraged.

ANNEX

Appreciation :- An increase in the value of the domestic currency against other currencies on the foreign exchange market which is caused by a change in market forces.

Balance of payment:- A record of earnings from abroad from the sell of good and services as well as capital inflows and expenditures on goods and services brought from abroad and capital outflows.

Budget deficit:- A situation where government expenditure exceeds government revenue.

Current account:- A record of all transactions which involves the purchase or sell of goods and services abroad as well as international transfer payments.

Depreciation:- A decrease in the value of a domestic currency against other currency on the foreign exchange market which is caused by a change in free market forces.

Devaluation:- A movement of the domestic currency against foreign currency from one fixed parity to a lower fixed parity; such a movement is the result of an official act of policy rather than the result of free market forces.

Exchange rate:- The rate at which the domestic currency can be exchanged for foreign currency.

Fixed exchange rate:- A system of exchange rates where currencies have a fixed value against other currencies.

Floating exchange rates:- A system of exchange rates where the value of a currency against any other currency changes in response to changes in free market forces.

Gross domestic product (GDP):- is the total value in current market prices of all goods and services by residents of the country.

Inflation:- A continuous rise in the price level.

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