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CDRC Digest Team:

Abdeta Dribssa Beyene, Ph.D (Executive Director)
Amb. Kasahun Dender (Deputy Executive Director)
Wegene Mengistu (Senior Researcher)
Yidnekachew Mitiku Ph.D (Senior Researcher)

Centre for Dialogue, Research and Cooperation
Ethio-China Friendship Avenue
Medina Tower 5th floor
Tel: +251 11 470 0370/73
Fax: +251 11 470 0359
Email: cdrc@cdrcethiopia.com
<http://www.cdrcethiopia.org>

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Auditing Ethiopia's Macroeconomic Reform Trajectory in a Shifting Global Context: Progress, Fragilities, and Governance Considerations

Background and Context

The trajectory of Ethiopia's macroeconomic reforms reflects the complex interplay between structural fragility and the political economy of controlled liberalization. Positioned at the intersection of ambitious economic transformation and systemic vulnerability, these reforms signal a measured opening of the economy while remaining deeply embedded in political priorities, state dominance, and cautious policy sequencing. Although the reform agenda has introduced bold measures aimed at addressing long-standing macroeconomic and structural imbalances, implementation continues to unfold in a context marked by contested state legitimacy, recurrent conflicts, and a rapidly evolving, difficult, and complex regional and global environment. Persistent challenges—including high public debt relative to export capacity, entrenched inflationary pressures, rising youth unemployment, and stagnant export performance—underscore that the reform process is being pursued not from a position of macroeconomic stability, but from within a landscape characterized by structural strain and institutional constraints.

The government's Homegrown Economic Reform Program (HERP), launched in 2019, represented a significant policy shift designed to liberalize key sectors, restructure fiscal policy, and modernize Ethiopia's monetary framework. The reform package introduced steps to open strategic sectors such as telecommunications, logistics, and finance to private and foreign investment, while fiscal restructuring efforts sought to address unsustainable debt dynamics and strengthen domestic revenue mobilization. Collectively, these measures signaled a departure from Ethiopia's

historically state-led development model, which had previously underpinned rapid growth but had begun to exhibit structural limitations. At its core, the reform agenda reflected an acknowledgment that the earlier model—centered on state dominance, public investment, and tightly managed markets—had reached the limits of its sustainability. Nonetheless, even as the government lays the institutional groundwork for private-sector-led growth, the state continues to retain a commanding presence in the economy, reflecting a deliberate strategy of gradual and controlled liberalization rather than wholesale market transformation.

A critical turning point in this trajectory came with the launch of Ethiopia's International Monetary Fund (IMF)-supported Structural Adjustment Program in July 2024. Implemented under the Extended Credit Facility (ECF) arrangement, the program committed the government to a series of policy reforms, including fiscal consolidation, exchange rate reform, further sectoral liberalization, and improved public financial management. In return, the IMF pledged approximately \$3.4 billion in financial support intended to ease balance-of-payments pressures, stabilize foreign exchange markets, support critical imports, and provide a financial cushion for politically sensitive reforms. The program effectively reinforced earlier liberalization efforts by accelerating foreign exchange reforms, tightening fiscal discipline, and strengthening monetary policy instruments. These measures were designed to address chronic macroeconomic imbalances, curb inflation, restore investor confidence, and create a more predictable macroeconomic environment capable of supporting sustainable growth.

The Ethiopian government has framed its reform package as a necessary response to deep-rooted structural weaknesses in the national economy, including rising debt burdens, persistent inflation, widespread unemployment, currency misalignment, and chronically low productivity. Official policy narratives emphasize the need to transition away from what is described as a fiscally unsustainable state-led development model toward a more competitive and efficiency-driven system anchored in private-sector dynamism. In pursuit of this shift, the reform agenda encompasses a wide array of structural measures: liberalizing sectors such as telecommunications, banking, wholesale and retail trade (which needs a careful navigation, and is delayed), and logistics; revising tax, investment, labor, and foreign exchange frameworks; improving the accounting and management of state-owned productive assets; establishing the country's first public stock exchange; and opening selected areas of property ownership to foreign investors. Taken together, these initiatives represent a deliberate pivot toward a more market-oriented economic framework intended to reshape Ethiopia's long-term development trajectory and signal a new phase of economic liberalization.

While these reforms have produced notable transformations in some sectors and strengthened certain aspects of state capacity, they remain closely intertwined with structural fragilities and governance challenges. The tension between ambitious reform objectives and complex socio-political realities renders Ethiopia's economic trajectory both promising and uncertain. Emerging fault lines between established domestic institutions and new market entrants illustrate these tensions. Competition between Ethio-Telecom and Safaricom Ethiopia over access to lucrative digital financial services markets, for example, reflects broader regulatory and institutional challenges associated with market opening. At the same time, persistent premiums in the parallel foreign-exchange market and the continued struggles of domestic private-sector actors underscore the depth of market distortions that remain unresolved. These developments reveal not only inefficiencies within the evolving

market structure but also the political and institutional constraints embedded within the reform process.

Comparative experiences elsewhere highlight the importance of carefully sequencing liberalization. The rise of Safaricom in Kenya occurred within a policy environment that strongly supported private-sector participation and facilitated the rapid expansion of private telecom operators as public sector dominance receded. Although this transformation accelerated technological innovation and financial inclusion, it also illustrates how liberalization can significantly reshape sectoral power structures when regulatory safeguards are weak or uneven. For Ethiopia, the policy challenge lies in ensuring that increased competition enhances efficiency and innovation while preserving domestic institutional capacity and maintaining a level playing field for local actors. These dynamics raise important questions regarding the distribution of reform costs and benefits. Market opening often imposes transitional costs on domestic firms and consumers through regulatory adjustments, price shifts, or market restructuring designed to accommodate new entrants. While such costs may be justified when they generate long-term efficiency gains, policymakers must ensure that citizens do not bear the burdens of reform disproportionately in ways that primarily facilitate the success of foreign market participants. Sustainable liberalization requires regulatory frameworks that protect consumers, ensure fair competition, and safeguard national economic interests while still encouraging foreign investment and technological transfer.

This consideration is particularly important for a country such as Ethiopia, where foreign exchange earnings remain limited and are critically needed for the import of strategic capital goods, industrial inputs, and essential commodities. Allowing foreign companies to operate in revenue-generating domestic sectors can introduce valuable capital, expertise, and technology. However, it can also lead to significant profit repatriation in hard currency, placing additional pressure on an already constrained balance of payments. This challenge is especially pronounced

in sectors such as telecommunications, digital finance, and logistics, where services are delivered locally but profits may ultimately be transferred abroad.

In such circumstances, policymakers must carefully balance the benefits of foreign participation with the macroeconomic implications of sustained foreign-currency outflows. Where domestic firms possess the capacity to provide comparable services, strengthening their competitiveness can help retain financial resources within the national economy, support local capital formation, and foster indigenous technological development. The policy question, therefore, is not whether to allow foreign participation, but how to design regulatory and investment frameworks that ensure such participation complements rather than displaces domestic enterprise.

Ultimately, the success of Ethiopia's reform agenda will depend on the strength of regulatory oversight and institutional capacity during this period of economic transition. Market liberalization alone does not guarantee efficient or equitable outcomes; its effectiveness depends on transparent governance, credible enforcement of competition rules, and safeguards against the emergence of dominant market positions that could distort economic outcomes. The government's continued involvement in strategic sectors suggests that liberalization is being cautiously managed rather than fully delegated to market forces. While this calibrated approach may help mitigate social and political disruptions, weak regulatory institutions raise concerns about potential elite capture during privatization and about the inflationary consequences of currency adjustments, which disproportionately affect vulnerable populations.

On the other hand, allowing foreign competition in sectors that traditionally generate substantial public revenues also carries important fiscal implications. Even when governments continue to collect taxes and regulatory fees, the entry of foreign firms into highly profitable sectors can reduce direct income streams that previously accrued to the state through public enterprises. In

countries such as Ethiopia, where government-owned enterprises have historically served not only as engines of growth but also as major sources of public revenue, this shift can significantly affect the fiscal resources available for social spending.

This issue is particularly relevant in relation to programs that support the most vulnerable segments of society. Social protection initiatives designed to assist low-income households—many of which initially benefited from financial and technical support from the World Bank—have gradually become an increasing fiscal responsibility for the Ethiopian government itself. As external support declines and domestic financing takes on a larger role, the availability of stable public revenue streams becomes critical for sustaining subsidies, social transfers, and targeted assistance programs for the poorest populations.

At the same time, ongoing reforms encourage the government to gradually withdraw from productive sectors and instead focus on expanding the tax base as the primary source of public revenue. While this approach aligns with conventional liberalization models that emphasize private-sector-led growth, it also has broader implications for state capacity and fiscal autonomy. A reduced role in revenue-generating sectors may limit the government's flexibility in making strategic economic decisions and weaken its ability to directly mobilize resources during periods of economic stress.

Beyond fiscal considerations, these shifts also affect the nature of state–society relations. When governments rely more heavily on taxation rather than direct income from state-owned enterprises, questions of accountability, representation, and public expectations tend to become more pronounced. Citizens who contribute more directly to state revenues often demand greater transparency, efficiency, and responsiveness from public institutions. At the same time, the government must confront persistent challenges that can undermine the effectiveness of a tax-based revenue system, including tax evasion, contraband trade, and the illegal export of high-

value commodities such as gold. Addressing these practices will require stronger regulatory enforcement, improved customs and tax administration, and more effective monitoring of illicit financial flows.

The government's efforts to digitalize public administration have the potential to significantly reduce opportunities for rent-seeking, informal payments, and corruption associated with direct human interaction in service delivery. By shifting tax administration and other regulatory processes to digital platforms, authorities can enhance transparency, improve compliance, and minimize avoidable costs often borne by businesses and citizens. Initiatives such as the "Mesob" integrated service platform—which aims to provide all-round government services through a one-stop engagement model—represent an important step in this direction. If effectively implemented and expanded, such systems could streamline administrative procedures, strengthen public accountability, and improve the efficiency of government service delivery. In this context, the restructuring of Ethiopia's economic model represents not merely a technical economic adjustment but a broader political transformation that reshapes the relationship between the state, markets, and society.

These economic challenges are further complicated by the broader political and geopolitical environment in which the reforms are unfolding. Ethiopia's macroeconomic transition is taking place amid ongoing conflict, political uncertainty, and significant humanitarian pressures. Debates over land ownership, regional autonomy, and governance reform intersect with economic restructuring, adding layers of complexity to policy implementation. At the same time, volatile regional and global dynamics—from tensions in the Horn of Africa, including strained relations with Eritrea, to broader geopolitical confrontations involving major powers in the Middle East—introduce additional uncertainties that may affect investment flows, trade routes, and economic stability. The war underway now between the U.S and Israel against Iran might likely make the situation even more uncertain.

Within this complex environment, the present analysis undertakes a systematic audit of Ethiopia's macroeconomic reform process. It assesses both the progress achieved and the structural obstacles that continue to constrain reform outcomes. By examining liberalization measures, fiscal restructuring, and monetary policy adjustments—particularly in the context of the July 2024 Structural Adjustment Program—the paper evaluates whether Ethiopia's reform agenda has advanced its stated objectives while navigating the country's evolving political and geopolitical realities.

Ethiopia's Macroeconomic Reform Trajectory: Continuities and Breaks with the Past

Ethiopia's macroeconomic reform program represents a significant departure from decades of a predominantly state-led development model. Anchored in the 2019 Homegrown Economic Reform Agenda and subsequently accelerated through successive policy initiatives, the reform trajectory illustrates the challenges of pursuing economic transformation amid structural fragility.. The program has been driven by pressing domestic challenges—including chronic foreign exchange shortages, persistent inflation, and widening fiscal imbalances—while also shaped by external pressures from international financial institutions and global investors seeking greater policy predictability and market openness. At its core, the reform framework rests on several interrelated pillars: fiscal consolidation, monetary modernization, exchange rate liberalization, and the restructuring of state-owned enterprises. Together, these measures signal a calibrated shift toward structural adjustment principles, albeit implemented through a controlled and gradual approach intended to balance economic stabilization with political and social considerations.

A number of policy decisions illustrate the extent to which the reform agenda diverges from earlier policy frameworks. Measures such as the gradual withdrawal of fuel subsidies, incremental increases

in electricity tariffs, the removal of preferential foreign exchange allocations for selected imports, and the introduction of targeted social protection programs collectively represent a break from the extensive subsidy regimes that previously characterized Ethiopia's developmental state model, and will have significant implications on perceptions of the government and state-society relations. Fiscal reform has also focused on expanding the domestic revenue base. The Income Tax Amendment Proclamation No. 1395/2025 introduced significant changes designed to broaden tax coverage and improve compliance. Among its key provisions are the establishment of a Minimum Alternative Tax to ensure that businesses contribute even when reporting minimal taxable income, the inclusion of digital economy activities—such as online platforms, digital creators, and consultants—within the formal tax system, and revised thresholds that expand taxation among middle- and high-income groups. These reforms are complemented by efforts to strengthen value-added tax enforcement and expand taxpayer registration. While these initiatives are intended to enhance fiscal sustainability, they also raise important questions regarding the distributive effects of subsidy removal and the political economy of taxation within Ethiopia's federal governance structure.

Monetary reform has also constituted a central component of the broader macroeconomic adjustment process. In January 2025, the National Bank of Ethiopia issued Directive No. NBE/INT/13/2026, which effectively liberalized interest rates by removing the long-standing seven percent minimum savings rate and allowing commercial banks to determine lending and deposit rates according to market conditions. This directive marked an important step toward transitioning from administratively determined financial pricing to a more market-based monetary framework. Complementing this shift was the adoption of Proclamation No. 1359/2025, which aims to strengthen the institutional independence of the national bank and insulate monetary policymaking from short-term political pressures. The law is intended to support Ethiopia's transition toward an interest-rate-based monetary policy

regime while facilitating broader financial sector liberalization. Nevertheless, the pace and depth of institutional transformation remain uneven, reflecting persistent tensions between technocratic reform objectives and the political realities that shape policymaking in a fragile governance environment.

Another critical element of Ethiopia's macroeconomic reform agenda has been the decision to end direct monetary financing of fiscal deficits. For many years, the government relied heavily on national bank financing, including mechanisms that compelled commercial banks to purchase long-term government bonds in order to finance budget shortfalls. This practice contributed to inflationary pressures and weakened the credibility of monetary policy. In June 2025, however, the National Bank of Ethiopia announced the termination of the treasury bond directive (MFAD/TRBO/001/2022), which had previously required commercial banks to allocate a portion of their lending portfolios to government securities. Ending direct monetary financing is closely linked to Ethiopia's ongoing debt restructuring negotiations and its broader reform commitments under the IMF-supported program. By curtailing national bank financing of fiscal deficits, the government seeks to enhance macroeconomic discipline, strengthen its negotiating position with international creditors, and signal a commitment to fiscal transparency and stability. Yet sustaining this reform under conditions of fiscal pressure remains a major challenge, particularly in an environment marked by high public spending demands and limited domestic revenue mobilization.

Foreign exchange reform has emerged as one of the most consequential and politically sensitive components of the reform program. Ethiopia's longstanding fixed and tightly managed exchange rate regime generated significant distortions in the economy, including the proliferation of parallel markets and persistent shortages of hard currency. In response, policymakers introduced foreign exchange auctions and initiated a gradual process of exchange rate liberalization aimed at restoring external balance and improving export

competitiveness. By decentralizing foreign exchange allocation and granting commercial banks greater autonomy in managing foreign currency transactions, the National Bank of Ethiopia has sought to reduce rent-seeking behavior and improve the efficiency of currency markets. However, this transition has also produced economic and social challenges. Exchange rate adjustments have contributed to inflationary pressures, increasing the cost of imports and intensifying public concern over the rising cost of living. The recently introduced Directive No. FXD/04/2026, which further relaxes foreign exchange regulations, represents a significant milestone in the liberalization of Ethiopia's foreign exchange regime. The directive aims to develop a more functional foreign exchange market, reduce distortions associated with restrictive currency controls, and facilitate international trade and investment. Nevertheless, the effectiveness of this reform will ultimately depend on consistent implementation, market confidence, and the broader stability of the macroeconomic environment.

A central objective of the reform agenda is to expand the role of the private sector within Ethiopia's economy. For more than a decade, the country's growth strategy was heavily dependent on large state-owned enterprises such as Ethiopian Airlines, Ethio-Telecom, and Ethiopian Electric Utility and Ethiopian Electric Power, which played a pivotal role in infrastructure development and economic expansion. While these enterprises, especially Ethiopian Airlines and Ethio-Telecom, contributed significantly to rapid GDP growth, the others generated inefficiencies, created fiscal pressures, and contributed to rising public debt levels. In response, the reform program has prioritized the restructuring of state-owned enterprises, particularly in sectors such as telecommunications, logistics, and energy. Plans to restart privatization efforts in the sugar sector following a new valuation of assets further underscore the government's intention to attract private investment and reduce fiscal burdens. Partial privatization and sectoral liberalization are expected to stimulate competition and enhance efficiency. However, the reform of state-owned

enterprises also highlights the inherent political economy risks associated with opening strategic sectors, including concerns about market concentration, regulatory capacity, and the transparency of privatization processes.

Financial sector liberalization has also gained momentum through the adoption of the Banking Business Proclamation No. 1360/2025, which marks a significant shift by opening Ethiopia's banking sector to foreign participation and introducing modern regulatory frameworks. This represents a major break from the historically closed and state-dominated financial system. Parallel reforms are underway in commodity markets. The National Bank of Ethiopia has announced plans to withdraw from its longstanding role as the sole purchaser and exporter of gold by the end of 2026. For decades, the national bank acquired gold—particularly from artisanal miners—at premiums significantly above international prices, a practice that critics argue distorted domestic markets and placed financial burdens on the bank's balance sheet. Under the new reform framework, private banks will be authorized to purchase gold directly and participate in export markets. This policy shift forms part of the broader liberalization strategy and has been highlighted by the International Monetary Fund as an important step in strengthening market-based economic governance. Nonetheless, whether private financial institutions possess the operational capacity and regulatory oversight to effectively assume this role remains uncertain.

Taken together, Ethiopia's macroeconomic reform trajectory is closely intertwined with broader transformations in the country's legal, institutional, and technological landscape. A series of recent initiatives—including the decision to allow foreign ownership of residential property, the establishment of a capital market through the Ethiopian Securities Exchange, the upgrading of several industrial parks into special economic zones, and the expansion of digital payment systems and fintech innovation—are intended to reinforce the reform agenda by modernizing the country's economic infrastructure. Complementary

initiatives such as the rollout of a national digital identification program and increased investment in emerging technologies, including artificial intelligence, further signal an effort to align economic governance with global technological trends. The introduction of the Disaster Risk Response Fund adds an additional institutional mechanism designed to strengthen fiscal resilience in the face of environmental shocks and conflict-related disruptions. Ultimately, however, the success of Ethiopia's reform program will depend not on the adoption of individual policy measures but on the coherence and durability of the overall reform framework. Sustained progress will require a careful balance between fiscal discipline, monetary stability, structural transformation, and the strengthening of institutional capacity capable of managing the complexities of economic liberalization.

Auditing Ethiopia's Macroeconomic Reform Trajectory: Assessing Progress

Audits of Ethiopia's macroeconomic reform trajectory point to measurable areas of progress. Fiscal imbalances have begun to stabilize, budget deficits have narrowed, and foreign exchange earnings have expanded alongside rising remittance inflows. At the same time, high-growth sectors—particularly mining—have gained renewed policy attention as potential drivers of export diversification and foreign currency generation. A combination of institutional strengthening and selective liberalization across strategic sectors of the economy supported these gains. While the reform agenda remains incomplete and uneven in its implementation, these developments suggest that the macroeconomic adjustment program has begun to yield tangible outcomes in stabilizing key economic indicators.

Fiscal consolidation and improved domestic revenue mobilization remain central pillars of Ethiopia's reform strategy. Efforts to stabilize inflation have been supported by the modernization of the monetary policy framework, the gradual withdrawal of direct national bank

financing of government deficits, and initiatives aimed at reducing financial repression in the banking sector. According to assessments by the International Monetary Fund, these policy shifts have contributed to a gradual moderation in inflation, although pressures associated with currency depreciation and reform-related price adjustments continue to keep inflation relatively elevated. While official statistics in Ethiopia indicated that year-on-year inflation fell below double digits by late 2025, the IMF has taken a more cautious position, projecting inflation levels closer to 18–20 percent. This divergence between official reporting and external assessment highlights a broader challenge within the reform process: the question of whether macroeconomic indicators accurately reflect the everyday economic realities experienced by households. For many families whose spending is concentrated on basic necessities, rising living costs remain a central concern. Without anchoring macroeconomic progress in improvements in household welfare, statistical achievements risk appearing detached from lived experience.

The IMF's most recent review also notes progress in narrowing Ethiopia's fiscal deficit, with projections indicating further reductions in the 2025/26 fiscal year. The government has attempted to limit reliance on deficit financing by curbing quasi-fiscal activities undertaken by state-owned enterprises, rationalizing subsidies, and expanding the tax base. Revenue mobilization has strengthened through reforms aimed at improving tax administration and compliance. These measures include revisions to value-added tax and excise regulations, the introduction of new levies, and amendments extending the standard 15 percent VAT rate to utilities such as electricity, water, and animal feed. Non-tax revenues have also increased, driven by higher public service fees and tariff adjustments. Notably, electricity tariffs have been raised substantially by the Ethiopian Electric Utility, reflecting broader efforts to align pricing with cost recovery and reduce fiscal pressures on the state.

Despite these improvements, Ethiopia's tax-to-GDP ratio remains relatively low—estimated at

approximately 9 to 10 percent—well below the 15 percent benchmark recommended by the African Union for sustainable domestic resource mobilization. At the same time, intensified revenue collection efforts have imposed considerable burdens on households. Higher VAT rates, expanded property taxation, increased service fees, and tariff adjustments have collectively raised the cost of living. In a context where consumer purchasing power has already been eroded by sustained currency depreciation, the expansion of taxation measures risks disproportionately affecting lower-income households and individuals on fixed salaries. As a result, fiscal consolidation—while strengthening the state’s financial position—has unfolded alongside declining real incomes for many citizens, raising important questions about the equity and long-term social sustainability of the reform agenda.

Sectoral liberalization has constituted another key pillar of Ethiopia’s reform process. The gradual opening of telecommunications, financial services, logistics, and energy markets is intended to attract foreign investment, facilitate technology transfer, and introduce new managerial expertise into previously state-dominated sectors. The entry of Safaricom Ethiopia into the country’s telecommunications market represents a symbolic milestone in this regard. Increased competition in the sector has the potential to expand consumer choice, improve service delivery, and stimulate broader economic dynamism. Banking sector reforms have also cautiously begun to permit foreign participation. A directive issued by the National Bank of Ethiopia—Directive No. SBB/94/2025—requires majority Ethiopian ownership while capping foreign equity participation at 49 percent. This framework reflects an attempt to balance financial sector modernization and capital inflows against concerns about domestic financial stability and regulatory oversight. Additionally, Directive No. SBB/99/2026 establishes specific regulatory conditions for the licensing of bank branches within Special Economic Zones, clarifying the operational framework under which foreign financial institutions may function in designated areas. Yet the experience of Safaricom’s market entry illustrates that reform

outcomes are shaped by a complex interplay of regulatory, commercial, and political factors, underscoring that Ethiopia’s reform trajectory cannot be fully captured through headline policy announcements alone.

Foreign exchange reform has also contributed to improved external sector performance. The gradual adoption of a more flexible exchange rate regime and measures aimed at easing foreign currency shortages have increased foreign exchange inflows and boosted remittance transfers from the Ethiopian diaspora. Remittance inflows have grown significantly in recent years, rising from approximately \$4.4 billion in the 2023/24 fiscal year to more than \$6 billion in 2024/25—an increase approaching 50 percent. Export revenues have also surged, driven largely by coffee and gold exports benefiting from favorable global commodity prices as well as increased production volumes. Analysts attribute the surge in global gold prices partly to heightened investor demand for safe-haven assets amid geopolitical tensions and trade policy uncertainties in major economies. As a result, Ethiopia’s total foreign exchange earnings reached approximately \$32 billion in the 2024/25 fiscal year, representing a 33 percent increase from the previous year’s \$24 billion. This improvement occurred despite Ethiopia’s suspension from the African Growth and Opportunity Act since 2022, highlighting the extent to which the country has sought to diversify foreign exchange sources beyond preferential trade arrangements. At the same time, investments in hydropower, natural gas, and renewable energy are intended to leverage Ethiopia’s abundant natural resources to meet domestic demand while generating new export streams. In addition, a major fertilizer manufacturing project launched in partnership with the Dangote Group aims to strengthen food security, reduce reliance on fertilizer imports, and protect foreign currency reserves. These sectoral initiatives indicate a broader strategy that seeks to combine macroeconomic stabilization with longer-term structural transformation.

Institutional reforms have complemented these macroeconomic and sectoral changes. The

establishment of new regulatory bodies in telecommunications and capital markets—most notably the Ethiopian Communications Authority (ECA) and the Ethiopian Capital Market Authority (ECMA)—signals a shift toward more rule-based economic governance. These institutions are intended to provide regulatory oversight capable of supporting liberalized markets while minimizing the risk of monopolistic behavior or regulatory capture. The Ethiopian Communications Authority's intervention during the dispute between Ethio Telecom and Safaricom Ethiopia over tower rental fees and infrastructure payment arrangements demonstrated the emerging role of regulatory institutions as arbiters within increasingly competitive markets. At the same time, transparency initiatives—such as the publication of public debt data, improvements in budget reporting, and strengthened audit mechanisms—have contributed to greater accountability and improved investor confidence. Nonetheless, these institutional reforms remain fragile. Weak enforcement capacity, political fragmentation, and administrative constraints continue to limit the extent to which regulatory frameworks can consistently translate into effective governance.

Overall, Ethiopia's Homegrown Economic Reform program—supported by engagement with the International Monetary Fund and the World Bank—marks a significant turning point in the country's macroeconomic trajectory. The IMF's Extended Credit Facility has supported fiscal consolidation and monetary modernization, while World Bank financing has helped advance sectoral reforms and institutional capacity building. Rising foreign exchange inflows from exports and remittances, combined with a gradual narrowing of parallel-market currency activity, have strengthened the country's external position and modestly increased foreign currency reserves. However, reserve levels remain below internationally recommended adequacy thresholds, highlighting the need for deeper structural reforms, expanded export diversification, and sustained inflows of foreign investment. The IMF's upward revision of Ethiopia's GDP growth forecast to approximately 9.3 percent for the 2025/26 fiscal year reflects growing confidence in the reform trajectory. Yet

strong headline growth figures obscure enduring structural vulnerabilities. Ethiopia continues to face high debt distress, and the benefits of macroeconomic expansion have yet to translate into broad improvements in living standards. Real wages remain under pressure, while household costs continue to rise—an imbalance that underscores the central challenge of ensuring that macroeconomic reform ultimately delivers inclusive and socially sustainable economic progress. How much all this might be affected even more by the war now underway is yet to be seen.

Fragilities Confronting Ethiopia's Macroeconomic Reform—The Case of Safaricom and Beyond

Despite notable progress, Ethiopia's macroeconomic reform trajectory continues to face deep structural fragilities that complicate the sustainability of the adjustment process. One of the central pillars of the reform agenda has been the transition toward a more market-based exchange rate regime. This shift was intended to align the official exchange rate with market realities, particularly in a context where the premium between official and parallel markets had previously exceeded 100 percent. The sharp depreciation of the Ethiopian birr that followed the reform significantly narrowed this gap, yet a parallel market premium of roughly 15 percent persists. In most reforming economies, economists consider premiums above 10 percent to be indicative of continuing distortions and structural weaknesses in foreign exchange markets. The persistence of this gap suggests that Ethiopia's reforms have only partially corrected the underlying imbalances. Structural constraints—including weak export capacity, high dependence on imports, shallow financial markets, and limited institutional capacity—continue to hinder the emergence of a fully functioning foreign exchange market capable of supporting credible price discovery.

The magnitude of the birr's depreciation itself has become a major vulnerability within the reform

process. While currency adjustments are a common feature of transitions toward more flexible exchange rate regimes, Ethiopia's experience has been unusually severe compared with many of its regional peers. In 2024, the depreciation of the birr ranked among the most pronounced in Sub-Saharan Africa, surpassed only by the extreme currency instability experienced in South Sudan. Although the pace of depreciation slowed somewhat in 2025, the birr remained among the region's weakest currencies. The currency's decline has become a powerful transmission channel for inflation, amplifying global commodity price movements and eroding domestic purchasing power. Rising import costs—particularly for essential goods such as fuel, pharmaceuticals, food inputs, and industrial machinery—have intensified cost-push inflation across multiple sectors of the economy.

Ethiopia's structural dependence on imported fuel, fertilizer, intermediate inputs, and capital equipment magnifies the inflationary impact of currency depreciation. As the exchange rate weakens, the local currency cost of these imports rises sharply, directly increasing consumer prices, at all levels—transport and activities that rely on this, while also raising production costs for domestic industries. These pressures cascade throughout the economy, as higher input costs translate into more expensive final goods and services. In an economy characterized by high import dependence and limited domestic substitution capacity, exchange rate depreciation transmits inflation through both direct channels—such as higher prices for imported consumer goods—and indirect channels through supply chains and production networks. For low-income households, the effects are particularly acute because food and transportation expenditures account for a large share of household budgets. The resulting erosion of real incomes highlights the fragile balance between macroeconomic stabilization and social welfare within Ethiopia's reform trajectory.

The liberalization of long-standing state monopolies has revealed a deeper tension between reform ambitions and political caution.

Ethiopia's reform strategy seeks to attract foreign capital, technology, and managerial expertise while at the same time preserving strategic state influence over key sectors of the economy. This approach reflects a broader paradox within the reform framework: encouraging private-sector participation while cautiously managing the pace and scope of open market competition.

The telecommunications sector illustrates this tension most clearly. The entry of Safaricom Ethiopia into the Ethiopian market was widely viewed as a landmark step toward sectoral liberalization. Yet the transition toward competition continues to be closely managed by the government, partly to ensure that the market remains viable for new entrants. In this context, the state-owned incumbent Ethio Telecom still retains significant market strength and operational advantages that could potentially overwhelm competitors in a fully unconstrained market environment.

Consequently, policymakers appear to be calibrating the competitive landscape in ways that balance the continued presence of the incumbent with the sustainability of new entrants. Measures affecting pricing structures and market conditions, at the society's cost, may be intended to prevent excessive market dominance and allow new investors time to recover substantial initial investments. While such managed competition can help stabilize the sector during the transition to liberalization, it also raises important questions about regulatory neutrality, market fairness, and the long-term trajectory of competition within Ethiopia's evolving telecommunications industry.

In practice, Safaricom's entry has catalyzed important market changes, although the competitive dynamic began even before the company formally launched operations. The mere announcement that a second telecom license would be issued prompted Ethio Telecom to lower prices, expand network coverage, and improve service quality in anticipation of competition. However, Safaricom's expansion has proven costly. The company reportedly incurred losses exceeding \$325 million in 2024, reflecting the high

operational costs associated with entering a new market, combined with structural disadvantages in competing with the incumbent. Analysts frequently attribute these challenges to the absence of a level playing field. Ethio Telecom continues to benefit from extensive legacy infrastructure, strong political backing, and preferential regulatory treatment that allows it to maintain a structural advantage over new entrants.

The asymmetry between the two operators has manifested itself in multiple areas of competition. Ethio Telecom retains control over critical infrastructure and has leveraged this advantage in negotiations over tower leasing and network access. Safaricom, by contrast, faces persistent obstacles including coverage gaps, licensing complexities, and limited access to foreign exchange for equipment imports. Regulatory frameworks governing competition remain relatively underdeveloped, exposing new entrants to policy uncertainty and inconsistent enforcement. Moreover, several market practices have raised concerns among analysts and industry observers. These include the absence of wallet interoperability between competing mobile money platforms, pricing differences between on-network and off-network transactions, bundled service packages that reinforce customer lock-in, aggressive price competition, and elevated infrastructure leasing fees.

These tensions are particularly visible in the contest over mobile money services. Ethio Telecom's Telebirr platform entered the market earlier and quickly established a strong user base, benefiting from the company's nationwide network coverage and government support. Safaricom's M Pesa platform entered later and has encountered interoperability barriers that limit its ability to compete on equal terms. Public statements from Safaricom alleging that its M-Pesa Lehulum service—designed to enable broader interoperability—was inaccessible through Ethio Telecom's network intensified the perception of a "turf war" within Ethiopia's digital finance ecosystem. Critics argue that the incumbent operator's control over infrastructure has allowed it to constrain competition and shape the trajectory of mobile money adoption in the country.

The competitive tensions within Ethiopia's telecommunications sector also carry an ironic historical dimension. Analysts often note that Safaricom's own dominance in Kenya's mobile money ecosystem was built under similar competitive dynamics. In Kenya, M-Pesa achieved rapid market dominance through exclusive agent networks, differential pricing strategies, and prolonged resistance to interoperability requirements. For more than a decade, Kenya's mobile money market remained largely non-interoperable. By the time regulatory authorities enforced interoperability in 2018, M-Pesa had already established an overwhelming market presence. As of early 2025, M-Pesa controlled approximately 90 percent of Kenya's mobile money market, illustrating how early market advantages can translate into long-term structural dominance.

These asymmetries underscore a broader reality: the outcomes of Ethiopia's reform process are shaped as much by political decisions as by market dynamics. The country's model of controlled liberalization—carefully sequenced and closely managed by the state—reflects enduring concerns related to sovereignty, fiscal stability, and developmental priorities. Decisions regarding licensing frameworks, sectoral sequencing, and regulatory oversight illustrate that economic reforms are deeply embedded within political considerations rather than being purely technocratic exercises. While this cautious approach may reduce the risks associated with rapid liberalization, it also creates uncertainty for investors. The experience of Safaricom Ethiopia has therefore become a critical test case for the credibility of Ethiopia's broader liberalization agenda. If protection of incumbent state enterprises persists for too long, it may undermine investor confidence and slow the pace of innovation that liberalization was intended to stimulate in the sector.

Another persistent fault line in Ethiopia's macroeconomic trajectory lies in the tension between state-led development initiatives and the standardized prescriptions of international financial institutions (IFIs). The Ethiopian

government has pursued an assertive model of state-driven development, channeling substantial resources into capital-intensive urban corridor projects, agricultural ventures such as wheat cultivation, and other strategic sectors. Domestically, these initiatives are presented as cornerstones of efficiency, self-reliance, sovereignty, and economic resilience. They are framed as deliberate investments in long-term modernization, designed to strengthen domestic capacities and reduce structural vulnerabilities. From the perspective of international financial institutions, however, these same interventions often conflict with conventional prescriptions for fiscal restraint, minimal state interference, and market-driven efficiency. Programs such as urban corridor development and large-scale wheat production are frequently viewed by IFIs as distortive, generating elevated public expenditures and potentially undermining market signals, even as they create tangible domestic capacities and economic opportunities.

Parallel efforts at the regional and local level further illustrate this divergence. Initiatives such as Oromia's Busa Gonofa program and the recently introduced transaction tax on telecommunications and financial services exemplify Ethiopia's pursuit of socially embedded and sovereignty-enhancing policy tools. Busa Gonofa, which draws on traditional mechanisms of communal solidarity and resource redistribution, not only mobilizes significant local resources but also fosters the potential for sustainable investment ventures that complement broader development objectives. Similarly, the transaction tax is designed to generate domestic revenue streams to support humanitarian interventions and critical social programs, reducing dependence on external aid and enhancing fiscal autonomy. While these measures align with Ethiopia's vision of socially grounded and resilient development, IFIs often interpret them as deviations from structural adjustment orthodoxy, which prioritizes broadly based consumption taxes, progressive income taxation, and narrowly targeted safety nets as instruments for fiscal discipline and efficiency.

The contrast between Ethiopia's domestic priorities and IFI expectations highlights a deeper

contest over the principles guiding economic transformation. Ethiopia's state-led initiatives seek to embed economic growth within social and political realities, leveraging public investment to generate employment, build infrastructure, and strengthen domestic industrial capacity. By contrast, IFI frameworks emphasize uniform approaches designed to ensure macroeconomic stability, minimize fiscal risks, and maximize market efficiency. The resulting friction underscores the complex trade-offs faced by Ethiopia as it attempts to reconcile domestic imperatives—sovereignty, resilience, and social inclusion—with externally mandated reform frameworks.

Taken together, these dynamics illustrate that Ethiopia's macroeconomic reforms cannot be understood solely through the lens of technical adjustment measures. They are simultaneously expressions of developmental sovereignty, instruments of social cohesion, and mechanisms for fostering domestic economic capacity. The tension between state-led interventions and IFI orthodoxy reflects the broader challenge confronting many emerging economies: how to pursue modernization, social solidarity, and self-reliance within global systems that often privilege standardization and efficiency over context-specific realities. Successfully navigating this tension will require careful policy calibration, institutional strengthening, and a pragmatic engagement with both domestic stakeholders and international partners to ensure that Ethiopia's developmental objectives are advanced without compromising macroeconomic stability.

Debt sustainability represents another major source of fragility within Ethiopia's macroeconomic landscape. Ongoing restructuring negotiations under the G20 Common Framework for Debt Treatments have highlighted the scale and complexity of the country's external liabilities. Although Ethiopia reached an agreement in principle to restructure approximately \$8.4 billion in external loans—including about \$3.5 billion in

debt relief—the process has encountered significant delays. The Official Creditor Committee

determined that the restructuring terms agreed with private bondholders failed to satisfy the principle of comparability of treatment, preventing final implementation. As a result, private holders of Ethiopia's \$1 billion Eurobond have indicated that they may pursue legal action after bilateral creditors—led by China and France—rejected the preliminary agreement and demanded equivalent concessions from private lenders. These developments illustrate the fragile balance between macroeconomic stabilization efforts and the realities of sovereign debt negotiations within a complex global financial environment.

Beyond financial vulnerabilities, Ethiopia's reform trajectory continues to be constrained by deep structural weaknesses in the productive sector. Export diversification remains limited, with the export basket heavily concentrated in a small number of commodities. In the 2024/25 fiscal year, coffee and gold together accounted for approximately 77 percent of total export earnings. This concentration exposes the economy to fluctuations in global commodity prices and external demand conditions. Although export revenues reached record highs during this period, the increase was driven largely by favorable international prices and exchange rate depreciation rather than by structural diversification into higher-value industries. Manufacturing exports remain limited, raising concerns that Ethiopia may remain locked in a low-value commodity export cycle rather than transitioning toward a more diversified industrial economy. Consequently, the country continues to experience a substantial trade deficit driven by high import demand.

Efforts to expand manufacturing through industrial parks have encountered persistent structural bottlenecks. Logistics inefficiencies, unreliable energy supply, and continued shortages of foreign exchange have constrained production and limited export competitiveness. Security instability in several regions—including Amhara and Oromia—has further disrupted supply chains and discouraged new investment. At the same time, Ethiopia's suspension from the African Growth and Opportunity Act has reduced preferential access to

the United States market, weakening the competitiveness of export-oriented industries. Regulatory complexity, unpredictable tax enforcement, retroactive tax claims, and inconsistent customs procedures have also constrained domestic private sector growth.

The fragility of the business environment is reflected in recent labor market data. According to the Ministry of Labor and Skills' Fifth Labor Market Intelligence Report, more than 80 percent of federal business licenses were inactive in 2025. This striking statistic illustrates the pressures that many firms face in adapting to Ethiopia's evolving macroeconomic environment. While reforms have been designed to stabilize the economy and attract new investment, they have also exposed underlying structural weaknesses in domestic enterprises. Many firms have struggled to cope with rising costs, tighter financial conditions, and regulatory uncertainty. This dynamic raises broader concerns about the inclusiveness and sustainability of the reform process.

Socio-economic disparities remain another persistent challenge. Unemployment—particularly among young people—remains high, reflecting both rapid demographic growth and the limited capacity of the formal economy to absorb new entrants into the labor market. The contraction in active business licenses illustrates the extent to which employment-generating enterprises have been weakened during the reform transition. Meanwhile, foreign investment has yet to significantly expand the reach of the formal economy. Persistent protectionism in strategic sectors, ongoing security instability, and institutional fragility have dampened investor confidence and slowed deeper integration into global value chains. Recent assessments by the U.S. Department of State highlight these concerns, noting that Ethiopia's investment climate remains characterized by significant risks. Issues such as displacement linked to large corridor development projects, uneven infrastructure investment, and limited access to financial services outside major urban centers continue to reinforce the country's rural-urban divide. These socio-economic gaps not only exclude large segments of the population

from the benefits of reform but also undermine the political legitimacy of the liberalization agenda. The central challenge facing policymakers is therefore not only to stabilize the macroeconomy but also to ensure that economic transformation translates into inclusive growth capable of bridging the gap between macroeconomic reform and social equity.

Governance Considerations in Ethiopia's Macroeconomic Reform Agenda

Ethiopia's ambitious macroeconomic reform program has introduced significant changes in fiscal, monetary, and exchange-rate management, reflecting a strong commitment to stabilizing the economy and creating conditions for sustainable growth. At the same time, the success and durability of these reforms are closely linked to broader governance considerations. Strengthening transparency, oversight, and accountability within public financial management systems remains an important component of ensuring that reform measures achieve their intended outcomes and maintain public confidence. While Ethiopia has recorded modest improvements in its standing on the Corruption Perceptions Index published by Transparency International, continuing efforts to reinforce institutional integrity and governance practices will be essential to support the credibility of the reform agenda. Such improvements are particularly relevant for reforms such as exchange-rate liberalization, which depend on transparent market operations, competitive financial institutions, and effective regulatory oversight to function efficiently.

The persistence of a parallel foreign-exchange market illustrates the complex interaction between macroeconomic reforms and institutional capacity. Exchange-rate liberalization is intended to promote more accurate price discovery and reduce distortions by allowing market mechanisms to play a greater role in determining the value of the currency. However, achieving these objectives requires strong institutional frameworks that ensure fair and transparent access to foreign exchange. In contexts where access to foreign

currency is limited, and demand remains high, disparities between official and parallel market rates can emerge. Addressing these dynamics requires continued efforts to improve foreign exchange management, broaden export capacity, and strengthen regulatory mechanisms that ensure equitable access to foreign currency while discouraging informal market activity.

Governance considerations also extend beyond monetary policy into the broader domain of public investment and fiscal management. Large-scale infrastructure development has been central to Ethiopia's development strategy over the past two decades, contributing to significant improvements in connectivity, energy supply, and industrial capacity. As with many rapidly developing economies, managing complex infrastructure programs presents challenges related to project implementation, procurement processes, and cost management. Continued improvements in monitoring and evaluation systems, procurement transparency, and parliamentary oversight can further enhance the efficiency and accountability of public investments. Strengthening these frameworks is particularly important given Ethiopia's efforts to manage external debt levels while ensuring that infrastructure investments contribute effectively to long-term economic productivity and export growth.

Institutional coordination represents another area where ongoing reforms can further strengthen policy effectiveness. Ethiopia's reform agenda aims to gradually transition the economy toward a more private-sector-led growth model supported by modern regulatory frameworks. In practice, the implementation of such reforms involves multiple government institutions, regulatory bodies, and state-owned enterprises. Ensuring clear mandates, effective coordination, and consistent policy communication among these actors is essential for maintaining investor confidence and providing a predictable policy environment. Continued alignment between fiscal authorities and the National Bank of Ethiopia, particularly in areas such as liquidity management, foreign exchange allocation, and macroeconomic stabilization, will be important for reinforcing the effectiveness of monetary and fiscal policy measures.

The creation of new regulatory institutions has been a positive step toward strengthening Ethiopia's economic governance architecture. Bodies such as the Ethiopian Communications Authority (ECA) and the Ethiopian Capital Market Authority (ECMA) were established to support liberalization by introducing rule-based regulatory oversight in sectors that were previously dominated by state monopolies. As relatively new institutions, they are continuing to develop their operational capacity, technical expertise, and regulatory frameworks. Sustained investment in institutional capacity-building, professional training, and operational independence will help ensure that these bodies are well equipped to oversee rapidly evolving sectors such as telecommunications, financial services, and digital payments. Strong and credible regulatory institutions are essential to ensure that market liberalization produces healthy competition, protects consumers, and avoids the emergence of market concentration.

Additional governance considerations relate to property rights, legal predictability, and financial inclusion—factors that are critical for encouraging private investment and expanding economic participation. Reliable contract enforcement and clear investment rules provide the confidence needed for domestic and foreign investors to undertake long-term commitments. In Ethiopia, questions surrounding land tenure arrangements, particularly within the context of the federal system and state ownership of land, continue to shape investment decisions. At the same time, expanding access to formal financial services remains an important priority. Large segments of the population, particularly in rural areas, remain outside the formal banking system. Strengthening financial inclusion—through digital finance, expanded banking services, and improved financial literacy—would help broaden the reach of economic reforms and enhance the effectiveness of monetary policy transmission.

Beyond institutional and technical considerations, the broader political economy context also shapes the implementation of macroeconomic reforms. Economic policy adjustments inevitably interact with political dynamics, governance structures,

and regional realities. In Ethiopia's case, the federal system and diverse regional contexts require careful coordination between federal and regional authorities to ensure that national economic policies are implemented consistently across the country. Maintaining political stability and constructive dialogue among stakeholders remains an important element in sustaining reform momentum and ensuring that economic policies deliver inclusive benefits.

Macroeconomic reforms also tend to redistribute economic opportunities and adjustment costs across different segments of society. For instance, exchange-rate liberalization may benefit export-oriented sectors and investors with access to foreign currency while increasing costs for import-dependent businesses and urban consumers. Similarly, fiscal adjustments, including subsidy reforms or tax changes, can create short-term pressures for some households even when designed to support long-term economic stability. Recognizing these dynamics and designing appropriate social protection measures can help mitigate the transitional impacts of reform and maintain public support for the broader policy agenda.

A further consideration concerns the inclusiveness of the reform process itself. Ensuring that economic reforms are widely understood and broadly supported can strengthen their long-term sustainability. While national reform initiatives are often driven by central government institutions in collaboration with international partners, expanding opportunities for consultation with domestic stakeholders—including small and medium-sized enterprises, civil society organizations, regional administrations, and local communities—can enhance policy design and implementation. In particular, addressing youth unemployment and expanding economic opportunities for younger generations remains central to translating macroeconomic reforms into tangible improvements in livelihoods.

Taken together, these governance considerations highlight the importance of aligning macroeconomic stabilization with broader institutional strengthening. Economic liberalization

is most effective when supported by transparent governance systems, capable regulatory institutions, and inclusive policy processes. For Ethiopia, the long-term success of the reform agenda will depend not only on technical policy adjustments but also on continued efforts to deepen institutional capacity, strengthen regulatory credibility, and ensure that the benefits of reform are widely shared across society.

Ethiopia's Macroeconomic Reforms Vis-à-Vis Regional and Global Dynamics

Ethiopia's macroeconomic reform trajectory cannot be understood in isolation from the broader geopolitical environment in which it unfolds. The country sits within one of the world's most strategically contested regions—the Horn of Africa—whose geographic proximity to critical maritime corridors connecting Europe, Asia, and the Middle East magnifies its geopolitical significance. The Red Sea corridor and the Bab el Mandeb Strait represent essential chokepoints for global trade, energy shipments, and military deployments. A significant portion of global maritime commerce, including oil and container traffic, transits through these waters before entering the Suez Canal and the Mediterranean. As a result, political and security developments in the Horn reverberate well beyond the region, shaping global supply chains and economic stability. Ethiopia's reform agenda, therefore, unfolds within a geopolitical setting marked by persistent instability, shifting alliances, and strategic competition among regional and global powers.

Regional political volatility continues to influence Ethiopia's economic prospects and the sustainability of its reform program. Persistent insecurity in Somalia and ongoing conflict in Sudan have created a fragile security environment across the Horn of Africa. At the same time, periodic tensions between Ethiopia and Eritrea underscore the enduring geopolitical fault lines within the region. These dynamics intersect with the expanding strategic engagement of Middle Powers such as Turkey, Saudi Arabia, the United Arab Emirates, and Qatar, as well as an active Egypt,

whose economic investments, security partnerships, and political interests increasingly shape the political economy of the Red Sea basin. The resulting web of alliances and rivalries produces a fluid strategic environment that directly affects Ethiopia's external vulnerabilities. For a country pursuing ambitious fiscal consolidation and structural reform, such geopolitical uncertainty heightens exposure to external shocks that can disrupt trade flows, investment inflows, and regional economic integration.

These regional pressures are further compounded by intensifying global geopolitical tensions. The widening confrontation involving the United States, Israel, and Iran has evolved into a broader regional crisis with implications extending across the Middle East and the Red Sea corridor. Iranian retaliation and proxy confrontations have expanded the geographic scope of the conflict, raising concerns about potential disruptions to global energy supplies and maritime security. The escalation in strategic waterways—particularly the Strait of Hormuz and the Red Sea shipping lanes—has heightened global risk. Energy markets, which are highly sensitive to geopolitical uncertainty, have already responded to these tensions. Global crude oil prices have surged significantly in response to the conflict, reflecting fears that shipping disruptions or military escalation could constrain supply or increase transportation costs. Even the perception of heightened geopolitical risk can trigger speculative price movements, further amplifying volatility in global energy markets.

For Ethiopia, such developments carry direct macroeconomic consequences. As a net importer of strategic commodities—especially petroleum products—the country is highly exposed to fluctuations in global energy prices. Even moderate increases in oil prices translate into substantial increases in Ethiopia's import bill, placing additional pressure on scarce foreign exchange reserves. Rising fuel costs also propagate throughout the domestic economy, affecting transportation, food distribution, manufacturing, and electricity generation. These cost increases inevitably feed into inflation, complicating the efforts of the National Bank of

Ethiopia to stabilize prices while maintaining monetary discipline. A sustained period of elevated energy prices could therefore undermine macroeconomic stabilization by intensifying currency pressures, widening the trade deficit, and reducing the government's fiscal space.

The inflationary transmission of global energy shocks tends to be particularly pronounced in low-income, import-dependent economies such as Ethiopia. While the International Monetary Fund estimates that a 10 percent increase in global oil prices typically raises headline inflation by roughly 0.3–0.4 percentage points worldwide within a year, the impact is often significantly larger in economies with limited financial buffers and high import dependency. In Ethiopia's case, where transportation and food prices are closely linked to fuel costs, the pass-through effect of energy price increases is likely to be far stronger. This dynamic places policymakers in a difficult position. Tightening monetary policy to curb inflation may stabilize prices but risks slowing economic growth and investment. Conversely, loosening monetary conditions to support growth could further weaken the currency and intensify inflationary pressures.

The implications of geopolitical tensions extend beyond petroleum markets to other strategic imports that underpin Ethiopia's productive sectors. Fertilizer supplies, agricultural machinery, pharmaceuticals, and industrial equipment are all vulnerable to disruptions in global supply chains. Ethiopia's agricultural sector, which remains the backbone of the national economy and a primary source of livelihoods for much of the population, is particularly sensitive to fluctuations in fertilizer availability and pricing. The Gulf region plays an important role in the global fertilizer market, and fertilizer production itself is closely tied to natural gas prices. When energy costs rise, fertilizer prices tend to increase as well, placing additional burdens on agricultural producers. Although Ethiopia sources significant quantities of fertilizer from countries such as Morocco, global price movements inevitably affect procurement costs. Rising fertilizer prices can reduce agricultural productivity by discouraging usage among farmers, which in turn threatens food security and export revenues from agricultural commodities.

These cascading economic pressures can have profound social implications. Higher input costs raise food prices and reduce household purchasing power, particularly among low-income populations that already spend a large proportion of their income on basic necessities. Small businesses, which often operate with limited financial reserves and restricted access to credit, are especially vulnerable to such shocks. As costs rise and demand weakens, many enterprises may be forced to scale back operations or close entirely, exacerbating unemployment and economic inequality. In this way, global geopolitical tensions can indirectly affect Ethiopia's domestic socio-economic stability, reinforcing the fragility of the broader reform agenda.

At the same time, Ethiopia's external partnerships play an important role in shaping the trajectory of its economic reforms. Beyond the concessional financing provided by the International Monetary Fund, the country maintains deep economic ties with China, which has been a major financier of Ethiopia's infrastructure expansion over the past two decades. Chinese financing supported the development of railways, industrial parks, and energy infrastructure that formed the backbone of Ethiopia's earlier state-led growth model. Recently, however, China has begun recalibrating its engagement strategy across Africa. Initiatives emphasizing smaller-scale, commercially viable projects—sometimes described as “small and beautiful” development initiatives—reflect a broader shift away from large debt-financed infrastructure programs. This transition has mixed implications for Ethiopia. On one hand, reduced reliance on large-scale external borrowing may ease long-term debt pressures. On the other hand, it may limit access to the transformative infrastructure investments that previously underpinned rapid economic expansion.

China's evolving trade policies also present new opportunities. Beijing's decision to extend zero-tariff treatment to imports from many developing countries opens the possibility for Ethiopian exporters to gain improved access to one of the world's largest consumer markets. If effectively leveraged, such preferential access could support

diversification of Ethiopia's export base and strengthen foreign exchange earnings. Nevertheless, expanding exports into global markets requires improvements in industrial competitiveness, logistics infrastructure, and product standards—areas where Ethiopia still faces structural challenges.

In addition to China, a growing number of middle powers—including Gulf states, European partners, and emerging Asian economies—are increasingly active in the Horn of Africa. These actors provide alternative sources of investment, trade partnerships, and diplomatic support that can help diversify Ethiopia's external economic relationships. However, their competing geopolitical interests also introduce additional complexity into the regional landscape. Infrastructure investments, port access agreements, and security partnerships often intersect with broader strategic rivalries, creating an environment in which economic cooperation is frequently entangled with geopolitical competition.

Ultimately, Ethiopia's macroeconomic reform agenda is deeply intertwined with both regional security dynamics and the shifting architecture of global economic relations. The country's geographic position within the Horn of Africa places it at the crossroads of major trade routes and geopolitical rivalries. In an era where global supply chains function as the lifelines of international commerce, the stability of maritime corridors and regional political systems becomes a crucial determinant of economic resilience. For Ethiopia, sustaining macroeconomic reform will require strategic flexibility—adapting domestic policy frameworks to external shocks while strengthening diplomatic engagement with regional and global partners. The success of the reform agenda will therefore depend not only on sound economic policymaking but also on Ethiopia's ability to navigate the complex and evolving geopolitics that shape the broader Red Sea and Horn of Africa region.

Conclusion

Ethiopia's macroeconomic reform trajectory reflects both bold ambition and underlying fragility, embodying the tensions inherent in economic transformation in developing and conflict-affected states. On one level, the reform agenda has produced measurable progress. Fiscal imbalances have been gradually stabilized through tighter expenditure controls and improved revenue mobilization, while efforts to rationalize public spending and reduce quasi-fiscal liabilities have begun to ease the pressure on government finances. The reform process has also opened limited space for private sector participation in previously state-dominated sectors, signaling a cautious but significant shift away from the long-standing state-led development model. Foreign exchange earnings have shown signs of recovery through a combination of export promotion, remittance inflows, and improved diaspora engagement. Meanwhile, targeted support for high-growth sectors—particularly in agriculture, manufacturing, and services—has reinforced Ethiopia's aspiration to transition from an aid-dependent economy toward a more diversified and market-oriented growth structure.

Yet beneath these gains lies a series of persistent vulnerabilities that continue to erode the sustainability and credibility of the reform agenda. Inflationary pressures triggered by the sharp depreciation of the Birr have undermined household purchasing power and exposed structural weaknesses in Ethiopia's monetary transmission mechanisms. The persistence of a sizeable parallel foreign-exchange market premium indicates that reforms in currency management and financial liberalization remain incomplete, revealing the tension between bold policy announcements and cautious or uneven implementation. Debt sustainability concerns remain prominent, especially given Ethiopia's substantial external liabilities accumulated during the period of rapid infrastructure expansion.

At the same time, the economy's narrow export base—dominated by a limited range of primary commodities—continues to constrain foreign exchange generation and exposes the country to external price volatility. Socio-economic disparities across regions, high unemployment among a rapidly growing youth population, and uneven institutional capacity across government agencies further complicate the reform landscape. Taken together, these factors suggest that Ethiopia's reforms remain caught between the promise of liberalization and the drag of structural weaknesses that limit their transformative reach.

This duality reflects a broader dilemma that characterizes reform politics in many developing economies: the need to stabilize macroeconomic fundamentals while simultaneously confronting deep-seated structural, institutional, and social inequities. Ethiopia's experience illustrates the difficulty of sequencing reforms in an environment where immediate crises—ranging from conflict-related fiscal shocks and humanitarian pressures to persistent foreign-exchange shortages—require urgent policy responses even as long-term structural transformation remains incomplete. Policymakers must therefore navigate a complex balancing act. On the one hand, reforms must restore macroeconomic stability and rebuild investor confidence; on the other, they must avoid exposing fragile domestic industries and vulnerable social groups to abrupt external competition or economic shocks. Achieving this balance requires careful calibration of liberalization measures alongside targeted industrial policies and social protections that prevent the costs of adjustment from falling disproportionately on the most vulnerable segments of society.

Equally important is the recognition that Ethiopia's reform agenda represents not only an economic transition but also a profound institutional transformation. The credibility of liberalization ultimately rests on the strength of the institutions responsible for regulating markets, enforcing contracts, and maintaining fiscal discipline. Although the government has embarked on structural reforms at an unprecedented scale—including partial privatization initiatives, financial

sector liberalization, and the creation of new market institutions—governance deficits remain a critical constraint. Weak regulatory enforcement, risks of corruption, and entrenched political-economy interests threaten to undermine the transparency and accountability necessary for market reforms to succeed. Sustaining reform momentum, therefore, requires embedding institutional integrity at the core of the reform process. Strengthening public financial management systems, enhancing regulatory independence, improving data transparency, and reinforcing anti-corruption frameworks are essential steps toward ensuring that macroeconomic reforms translate into broad-based and sustainable development outcomes. Without such institutional foundations, liberalization risks deepening inequality, entrenching rent-seeking networks, and generating new forms of economic concentration.

In this sense, Ethiopia's macroeconomic reform agenda must also be understood as a governance challenge as much as an economic one. The durability of reform depends not only on the technical design of fiscal and monetary policies but also on the extent to which these policies are supported by political consensus and inclusive governance structures. Building such a consensus requires transparent communication about the objectives and costs of reform, meaningful engagement with the private sector and civil society, and credible mechanisms for managing social tensions that may arise during periods of economic adjustment. Recent initiatives—such as currency realignment, plans to open the banking sector to foreign participation, and efforts to establish a national stock exchange—signal an intention to deepen market-based reforms and modernize Ethiopia's financial architecture. These steps also align Ethiopia more closely with emerging continental economic frameworks such as the African Continental Free Trade Area, which seeks to integrate African markets and promote regional trade. However, the effectiveness of these initiatives will ultimately depend on whether institutional reforms keep pace with economic liberalization.

Beyond domestic policy considerations, Ethiopia's macroeconomic trajectory is increasingly shaped by its regional and global strategic environment. As a landlocked country located in the geopolitically sensitive Horn of Africa, Ethiopia's economic prospects are deeply intertwined with regional stability, access to maritime trade corridors, and the evolving dynamics of international partnerships. Political instability in neighboring states, competition among external powers for influence in the Red Sea region, and the broader reconfiguration of global supply chains all exert pressure on Ethiopia's reform agenda. External shocks—particularly those linked to energy markets, commodity prices, and geopolitical tensions—can rapidly alter the macroeconomic environment in which reforms unfold. At the same time, Ethiopia's relationships with key international partners, including multilateral financial institutions and major trading partners, remain essential for financing development, restructuring debt, and sustaining investor confidence. The challenge, therefore, lies in leveraging these partnerships in ways that strengthen domestic resilience rather than deepen structural dependency.

Ultimately, Ethiopia's reform experience underscores a fundamental lesson of economic transformation: macroeconomic adjustment alone cannot guarantee sustainable development without parallel advances in institutional governance, social inclusion, and regional stability. The country's economic path is inseparable from the broader political and security dynamics of the Horn of Africa and its wider geopolitical environment. Sustaining reform momentum will require not only disciplined fiscal and monetary management but also long-term investments in institutional capacity, export diversification, human capital, and social cohesion. If successfully implemented, Ethiopia's reforms could lay the foundation for a more diversified and competitive economy capable of integrating more fully into regional and global markets. However, if structural weaknesses and governance challenges remain unaddressed, the bold ambitions of the reform agenda risk producing unintended outcomes—ranging from persistent inequality to renewed macroeconomic instability. The future of Ethiopia's macroeconomic transformation will therefore depend on its ability to reconcile ambition with institutional strength, ensuring that reform not only stabilizes the economy but also delivers inclusive and resilient growth.