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**Master's Thesis of International Studies
(International Commerce)**

**Investigating the Challenges of
Ethiopian Goods Export**

August, 2021

Graduation School of International Studies
Seoul National University

Tesfamariam Desie Mesfin

**Master's Thesis of International Studies
(International Commerce)**

Investigating the Challenges of Ethiopian Goods Export

A thesis presented

By

Tesfamariam Desie Mesfin

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**Graduate school of International Studies
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ABSTRACT

This study tried to figure out the main challenges of the Ethiopian goods export. Quantitative data and policy documents has been used as a sources of the data. In order to analyze, the data descriptive method of analysis has been applied. The study finds that Ethiopian commodity export from 2000-2018 was weak and instable. This is due to its high concentration on few agricultural products particularly on coffee and sesame seed export. In addition, the drought affected the export sector because the main source of the export earnings was agricultural sector. This study gives possible policy recommendations based on the applied descriptive analysis and document review findings.

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Chapter one

1. Introduction

1.1 Background

The level of technology which is applied for the production of goods and services and endowed resource makes difference among countries of world. Every country's areas of specialization in the international trade depends on their factors of production and technology which gives them comparative advantage.

Now a days it is difficult for a country to survive and prosper with closed economy. International trade is crucial for a country's development. It makes complement for countries of the world by giving many varieties of goods and services and low cost of production through comparative advantage. A country who produces using their comparative advantage can prosper easily than those who tried to produce all things by themselves. Both export and import are the drivers for a country's economic development. A country which export more than its imports has a trade surplus which every economy wants to have.

Trade deficit shows how the country is performing at the international market. Trade deficit by itself is not a sign of poor performed economy, at some point it will help to us to know how the residents of the country are expanded their varieties of goods and

services in order to improve their living standard with competitive price. Since a country cannot produce all goods and service it is obvious that domestic people will look for imported goods and services in order to maximize their utility through international trade opportunity. Because of the country demand for imported goods and services may greater than its exports. At some level trade deficit is not a problem because of the nature of demand and supply of the international market. . The problem will occur if it is very wide and persistently increasing. For this kind of problem we cannot just say that it is because of the imported demand is increased rather we have to figure out what are the root cause of the problem. It is that the poor performance of export will bring a wide trade deficit if it not balanced with the growth of import.

There are several factors that can be mentioned for the weak performance of many African countries export. the structure of many African countries export that relied on primary goods export , Lack good policies and strategies , lack of strong institutions , lack of technology and political instability are among the major factors that affected the export of African countries.

For a long period of time Ethiopia as one of African country challenged with poor performance export of the export sector. The country has experienced different economic system with different political administration. During imperial period in 1950s the country used free market economy and the export of goods were very few and the primary commodities. In 1970s the government system was changed to the military government which followed the command economy. During that period the

economy become worsen and the export of goods were very limited in volume and very limited diversification. In the first of 1980s the government system also changed with a free market economic system. During this period there has been many reforms of economic policies and strategies. The country tried to decrease many trade barriers. Due to many reforms in the export sector like export trade duty incentive, financial incentives and other incentive mechanisms, the export sector has shown some improvement (Samuel, Determinants of agricultural export in Ethiopia, 2012)

Although different policies and strategies have applied to improve the export sector development the result didn't showed the expected result and the sector is still weak and can't support the economy at its full capacity.

Due to the unsatisfactory performance of the export sector the country highly depended on foreign debt and aid in order to fulfill its foreign currency demand for its import expenditure. The share of export from the total domestic product very low and also the share of export in financing the import sector is very low and declining. The share of merchandise export from the total gross domestic product was below 10 percent which is less than the average 30 percent share of the Sub-Saharan African countries (Ciuriak, 2010).

Ethiopian commodity export is not only characterized by the primary commodities it is also relied on few export commodities such as coffee, sesame seeds , red beans , bovine animals and gold. Unprocessed coffee export and sesame seed export took around 50 percent share from the total commodity export earnings.

1.2. Statement of the problem

Lack of foreign currency and capital is the major problem that most of the developing countries faced. The huge gaps between export-import and saving –investment is the features of many developing countries. Due to this in the process of their economic development many of them experienced the shortage of finance to their investment. Improving the domestic saving is very crucial to the financial needs of the development programs. At the same time the enhancement of export is very crucial to solve the financial constraints for investment since it is a good source of foreign exchange.

Both internal and external factors are accountable for the poor performance of many African countries. For their bulk of export revenue many African countries depended on primary goods export that has a problem with a long time price fluctuation which is more volatile than the manufactured export commodities. The major challenges of many African countries that faced for their economic growth , poverty alleviation as well as export revenue are the structure of their export which is dominated by primary goods , price volatility , fluctuation in volume of export , deteriorated terms of trade commodity market instability (Adebusuyi, 2004). Especially the Sub-Saharan African countries experienced a weak export performance due to their dependence on particular commodity export earnings.

The country has a vision to become a low middle countries by 2025. In order to achieve this many middle term plans were prepared like the two consecutive Growth and

Transformation Plans. The national development agenda requires many infrastructural development which will ease other developmental agendas. For sustainable economic growth the country applied different macroeconomic policies like Export promotion and import substitution in order to boost the export sector and protect the infant industry. For this national agenda the country has to import capital goods which requires large amount of foreign currency. Export is crucial to fulfil the demand for the foreign currencies.

To improve the productivity of the economy with diversification import substitution was encouraged by several economic researches, however, in recent years export promotion policy become popular and advocated in many researches (Brooks, 2008). Enhancing the export sector by improving its competitiveness at the international market is crucial for sustainable rapid economic growth and development. In order to enhance the capacity of the export sector the challenges of the sector should have to identify in a systematic way. In this regards, there are many theories that have raised on the challenges of developing countries export. The reaction of industrialized countries is considered as a challenges for developing countries export according to the trade pessimist school of thought. Whereas the structuralism theorists raises that the developing countries problem comes from the supply side constraint which hindered the growth and diversification of the export sector. In addition to these school of thoughts many arguments are also seen for the major challenges of the export sector development.

Like other SSA African countries Ethiopia experienced insufficient foreign currency due to high dependent on few primary goods exports). Coffee, Chat, Oilseeds, pulses, gold

and live animals are the top export commodities of the country with a share of around 70 percent from the total goods export earnings (Samuel, , Determinants of agricultural export in Ethiopia, 2012).

There are several factors that determine Ethiopian goods export. Financial sector development , good infrastructures , market access condition, real exchange rate, foreign direct investment , institutional quality are among the determinants that affected the Ethiopian export performance.

For the Ethiopian export underdevelopment many constraints were identified in many researches. According to Abebe (2008) poor transport infrastuctes and high transaction costs were the problems that hindered the competitiveness of the Ethiopian goods export at the international market. Other studies showed that low income elasticity of demand for primary commodity exports , structure of the export sector which is highly dependent on few agricultural products , the major challenges of Ethiopian export sector , small number of export destination countries , poor domestic infrastructure, poor institutional quality are among the major challenges of Ethiopian export sector development (Belete, (1999),). Governemt policies low development of the industry sector, lack of quality management were also considered as the constraints (Zewdu 2008).

Although some improvements have been seen on the Ethiopian export, its performance is still very weak and the foreign exchange earnings from the sector is instable. These initiated the present study to figure out the main challenges of goods export in Ethiopia

and the reasons for which the country is not active enough in its export sector. More specifically, the following basic questions are addressed by the study:

- ✓ How is Ethiopian export trade performing during the recent years?
- ✓ Why Ethiopian exports not performing well?

1.2 Study Objectives

General Objective

The main objective of the study was to figure out the major challenges for the poor and unstable Ethiopian goods export.

Specific Objectives

- To assess the root causes for the poor performance of Ethiopian goods export
- Giving policy recommendations based on the study findings

1.4 Significance of the study

It is clear that the weak and instability of export performance will affect the overall economic growth and development. Ethiopia has faced a wider and increasing trade deficit and insufficient foreign exchange reserve due to the unsatisfactory export earnings. Since it is difficult to continue with foreign aid and debt in financing the investments that the country needed, export sector should have to enhance and stable. This study is significant in figure out the root causes for the country's low export

earnings and instability. Descriptive analysis was applied using time series quantitative data and policy documents has been used to assess the major challenges of the sector.

Assessing the main challenges of goods export will help to give important information to the policy makers and other stake holders to come up with an appropriate policies and strategies.

Even though the export sector has shown some improvement compared to the first of 2000s it is not enhanced and the data shows that the export growth rate of Ethiopia is low as compared to African countries with similar features of economic structure and other features. So in considering those gaps, the study tried to identify the root causes of commodity export performance in the country from 2000-2018 to come up with recent and reliable information that informs for responsible bodies and for deciding correct decision in policy making.

1.5 The scope of the study

The study will bound in studying the export performance determinants in Ethiopia: during the period 2000– 2018 using annual data that are collected from the UNCOMTRADE , International Monetary Fund , World bank, UNCTAD, FAO, Ethiopian National bank , Ethiopian Planning and development commission as well as different websites. This is because to make the study as up to date as possible.

1.6 Limitation of the study

The area, export performance challenges, being vast and crucial for growth and development, many determinant measures could be used for determining export performance. To analyze the supply side we have to see the quantity and quality aspects of the export sector however the study focuses only on the quantity due to lack of data. In addition, the shortage of time was one of the limitations in conducting this research paper. Lack of organized data regarding general export performance determinants in Ethiopia another limitation of the study that imposed lots of work on the researcher in organizing different sorts of data to get consistent information.

1.7 Organization of the study

The paper will be arranged and proceed as follows. Section two explains macro-economic performance of Ethiopian export. Section three will present both theoretical and empirical literature. Description of the data analysis jointly with data sources will be discussed in Section four. The last section is dedicated to conclusion and policy recommendation.

Chapter two

2. Literature Review

2.3 Theoretical Literature Review

Theoretically there is a multiplier effect of devaluation on the gross domestic product through enhancing the export. However, it may not bring the expected result due to many reasons. One of them is in the short run the Marshall Learner condition may not hold. From the elasticity side trade performance and exchange rate are linked according to the Marshall-Learner theory. The trade deficit will be improved through devaluation which the sum of demand elasticity for imports and exports is greater than one. However, many empirical studies showed that many countries didn't achieve improved investment, output and employment after they devalued their currencies and the short run the elasticity was smaller than the long run elasticity

The second reason is that Lausen –Metzler (LM) effect which says the devaluation will improve the country trade balance if the rise in the national product is offset by the import increase due to depreciation of currency. In order to hold the LM effect there should have to be changes in some variables. If these conditions are true the trade balance will be improved otherwise the multiplier effect of devaluation will not bring such result.

The third reason that the devaluation may not give the expected multiplier effect on the national income because the immediate benefits of this policy may be weak due to the J curve effect. This happens due to the nature of the agricultural goods which takes time

to harvest so in the short run the Ethiopian export earnings may not rise because of these supply side problem even though the Marshal- Lerner condition is fulfilled. In addition , Ethiopia's demand for import especially for the oil and capital goods is inelastic so the devaluation may not decrease the expenditure of imports on the other hand the export will not increase immediately due to this the devaluation policy. Therefore, before it improve the country trade deficit will get worse.

In general, the performance of export and devaluation policy has different in relation with the economies nature according to many empirical findings that have done in different economies. The technical approach like methodology and sample that has been used by different researchers also bring different relationship with the effect of this monetary policy.

If there is no a net positive change in the prices after the real devaluation (nominal decrease of domestic currency with adjusted price) the trade performance of the country will not improve when we see it at the flip side. The devaluation policy may cause inflation by making the imports prices high and make the overall goods and services price will rise and decrease the economy competitiveness at the international market. Several empirical results have shown that inflation will increase after the nominal devaluation if the country is high dependent on imported goods. Devaluation is expected that to make imports less attractive and increase the demand for domestic production at the domestic market as well as the international market, however, its effect may differ based on the economy character.

2.2 Empirical literature

The share of African trade in the world trade has declined due to policies problem like the appreciation of exchange rate and the industrial policies which was anti agriculture. These policies make decline the performance of the agriculture export which most African countries have a comparative advantage (Schiff and Valdes, 1992). The share of the region in world export decreased constantly and reached about 2 percent in 1990 from its share 6 percent in 1980s. After a little recovery from the 1990s performance it reached to 3 percent during 2000s (Mold and Prizzon, 2008).

In the world market the African export is not influential due to its nature and many other factors. Even though the African export showed weak performance and steadily declined, it is crucial for their economic development. African economy needs foreign exchange to its investments that will boost the economy. Export sector development is a key to the continent (Morrissey).

Any country's export performance is also determined access to market which has a significant effect on the international trade. Market access should be included in the development strategy of African countries to increase the supply of the export. For the export sector improvement increasing the capacity of supply is also crucial in addition to expanding access to market (Fugazza 2004).

For many developing countries sustainable economic growth and poverty alleviation agriculture is the main source from other sectors. The Sub-Saharan African countries have suitable climate for agriculture and cheap labor which gives the comparative advantage

in exporting agricultural products. It is also a key for their development process (Alwang Siegel 1994). Exporting primary commodities and raw materials didn't bring the expected impact on the Sub Saharan African countries even if have a comparative advantage which is recommended by the trade theory.

African agricultural export is characterized by weak performing, not competitive and undercapitalized compared to other developing economies. This is because it has a challenges of low crop production, high variability of production, high concentration of export on few products, price volatility and reliance on primary commodities export. This problem is mostly seen in SSA. The Africa agricultural export is limited in the global trade even though it has a comparative advantage. This because of it faced price competitive with the agricultural export of advanced economies that produce in large scale than the African farm which is produced by small scale and house hold farming (Mkpado,2013).

Before 1974 Ethiopia had a free trade policy during the Imperial Regime. Both the public and private sector has taken different actions in relation with the enhancing the export sector, improving the quality of import. During this period the imports of goods were taxed except raw materials and capital goods which were free from duty to encourage the manufacturing sector. After the fall of the Imperial Regime the military group the so called Derg regime was taking the power and led the country for 17 years starting from 1974. During this period the economic system was changed to command economy and the external trade was dominated by the state owned enterprises. The

international trade policy was focused on increasing the role of the government in export as well as import sector.

The quantity, price and distribution of goods was controlled. Many economic activities are under the control of the state and the private sector participation in the international trade was limited. In 1991 the new government came to power and changed the socialist ideology to capitalist. In order to improve the country's international trade many restrictions were canceled like the limited participation of the private sector, quantitative restriction and other trade restricted policies. Enhancing the export sector through private sector development and other promoting strategies were applied (Geda, 1999)

It is obvious that the Ethiopian economy is highly depended on the agriculture. About 80 percent of the population engaged on the production of agriculture. The sector is the backbone of both the service and industry sector. Most of the country's manufacturing companies used agriculture as an input because they produced agricultural manufactured goods. The service sector like hotel service used agriculture as the input. In addition to that more than 70 percent of the foreign currency was obtained from the export of the agricultural products. Although it is the main source of the Ethiopian economy because of technological problem, poor infrastructure, dependent on the rainfall, frequent drought the sector has underdeveloped. As a result the export earnings which is highly depended on the agricultural sector faced a problem (Samuel, Determinants of agricultural export in Ethiopia, 2012).

For the Ethiopian economy agriculture sector which accounts about 46.3 percent of the total domestic production, about 75 percent of export earnings, and around 80 percent of employment can be called as a backbone. The agricultural products are the first leading sources of the export earnings. Major export commodities of the country were coffee, oilseeds, vegetables, pulses, cut flower and live animals (Samuel 2012).

Weather with its direct or indirect effect around 25 percent of Ethiopian people led its life on the coffee product. The government collected around 20 percent of its revenue from this crop. It is the backbone for the export earnings. Before 1974 revolution it accounted about 50 to 60 percent of the total commodity export income. In 1989 its share reached 63 percent (Wubneh, Mulatu ,1991)

Next to coffee oilseeds and pulses contributed significantly for the export earnings. In 1974 the share of oilseeds and pulses from the total commodity export was 34 percent , however, it declined to 3 percent in 1989 due to drought that has occurred in the country. During this time the country faced large famine and was difficult to export (Wubneh, Mulatu, 1991)

Real exchange rate is the significant factor in relation with the export performance. Export of a country will increase if its price of export decline compared to the world price. In order to make export price cheaper at the international market a country will follow a depreciation against other currencies. In relation with the fall of Indian export price the earnings of the country export increased. And the export revenue was highly declined due the Indian currency appreciation (Sharma, 2000).

The argument about the relationship between real exchange rate and growth export has been continued in different studies. No significant relationship has been found between the volume of export and real exchange rate in Uganda according to Antingi-Ego and Kasekende (1999). On the hand the devaluation of Tanzanian currency against other currencies boost the growth of export and its effect was significant (Lakew, 2003).

Ethiopian export growth constraints

For the growth of the Ethiopian goods export sector many constraints can be mention market access problem, the surtax on coffee , overvaluation of the domestic currency, deteriorating terms of trade , lack of capital for the investment , imported raw martials have high tariffs are among the list. The private consumption and export tax were significantly affected the growth of export among other variables like real effective exchange rate, real Gross domestic Products , unit value index of export deflated by the implicit gross domestic product deflator. The model used the log linear supply of export for the volume of the export and took the log of other explanatory variables (Bank, 1987).

According to the Transitional Government of Ethiopia (1991) the past unfavorable trade policies were blamed for the country's unpleasant position of foreign exchange through weakening performance of goods export particularly the agricultural products export.

To improve the export of goods policy revision and actions are required according to Ciurak and claudious (2010). The following factors affected the sector in their findings.

- a) The weak performance of Ethiopian export more domestic problem than external problem. In the developed economies such as USA, EU, and other major export destiny countries Ethiopia has market access which is tariff free or very low. However, due to policy problems and other domestic constraints the country could not earn foreign exchange with its full capacity from the export sector (Ciuriak, 2010).
- b) The macroeconomic policy mix was one of the factors that hinder the country export sector growth. For instance the country export competitiveness at the international market has declined because of the REER was rises in 2000s in relation with the domestic inflation that was created by policy the effect of exchange rate.
- c) The high trade cost is the constraint that the country can't get the expected foreign exchange earnings from the export sector. According to the World Bank report of 2010 Ethiopia was ranked 123 most difficult places in the globe from 155 countries. Inaddtion, because the country is landlocked in terms of trading across borders was ranked 159th out of 183 countries which drives the country's export price to be high at the global market. The road transport which is expensive and slow than rail makes the country trade cost high. The import and export process complexity and unfavorable custom procedure makes the trade cost expensive.
- d) A stunned private sector also the factor for the poor export performance of the country. For the export sector development the role private sector is

immense ,however, it's under development results in a weak supply response to the new market opportunities by liberalization of trade. Lack of industry zones which will have spillover effect within firms also another problem for the export sector. The structure of the industry which was featured by a high degree concentration of market, government owned enterprises and starting business is not ease, small number of manufactures contributed for the slow and weak export growth.

- e) Lack of efficient services like transport, telecommunications, finance and other related services contributed for the insufficient performance of the country's export. When we see the structure of the economy the share of service sector become higher than agriculture as well as industry. However, the development of the service sector is not on the good side of the economy which means the financial service is not developed rather the rents took high share in the service sector. This doesn't support the industry sector as well as the export sector. Most producers of exportable products could not get the producers services at a low cost. This drives out the manufacturing goods from the export market.
- f) Because of the zero tariff in the major developed economies Ethiopia has easy access to use the benefit of world market. However, due to the high tariffs in African partners the country face tariff barriers to its export performance.

Foreign direct investment is one of the determinants that can positively affect the supply of export. Many studies show that it had a significant impact on the growth of the economy as well as the export of the country while other studies indicated that it has no significant effect. The nature of the policy of one country determine the contribution of foreign direct investment to the growth of export (Sharma, 2000). A country will receive FDI based on its comparative advantages of other countries. So it can boost the export sector if the investment is made on export oriented areas otherwise if it is invested on non-export oriented activities it may not contribute to the export growth (World Bank 1993). FDI will increase the country's capital stock and hence it will increase productivity and output if it is used efficiently.

Institutional quality determines the supply of one country's export. A country who has a good policies with a strong institutions can maximize the benefit from international trade (UNCTAD, 2008). Quality of the institutions can make a difference among countries by giving a comparative advantage earnings from export depends by Institutional quality (Francois, 2006). Most of the countries who have successful export story have a strong and quality institutional arrangement. The export income declined when the institutional quality become weaker and weaker (Anderson, 2002). International trade and Institutional quality have a high correlation (Dollar, 2002). Mostly the low income countries are not using effectively the advantage of world market due to their institution are weak.

Real GDP and Real effective exchange rates had a positive significant relationship on the OECD countries (Beng ,1999). While in Uganda REER had no significant effect on the growth of export rather the terms of trade and the previous export growth had a positive and significant effect on the export growth (Nimrod, 2006).

(Edwards, 2005) used panel data set to analyze the supply manufacturing export determine factors. Generalized Method of Moments and dynamic fixed effects were used for the study. The determinants for the supply of export in South Africa's showed that REER, income of importing countries, ratio of skilled to unskilled labor, capacity of rail and import penetration had a statistically positive significance on the volume of manufacturing export.

(Eshetu, 2006) on his study of determinants of manufacturing performance in Ethiopia used Ordinary Least Squares (OLS) estimation method using annual data from 1970 – 2004. The results from the model reveal that Ethiopian manufacturing exports are positively & significantly influenced by investment to GDP ratio, total factor productivity and foreign income while real effective exchange rate was found to have insignificant influence on exports.

YISHAK (2009) analyze determinants of export performance of Ethiopia. A gravity model is employed with panel data using 30Ethiopia's trading partners for the period 1995–2007. The model is estimated with the Generalized Two Stages Least Squares (G2SLS) method. Endogeneity of FDI and GDP to exports, heteroskedasticity and serial correlation for AR (1) are controlled. The results show that good institutional quality and

internal transport infrastructure appear to be major determinants, whereas the real exchange rate and FDI have no statistically significant effect on Ethiopia's export performance. Likewise, the growth of domestic national income affects Ethiopian exports positively.

Foreign market access conditions also play a significant role. The results indicate that import barriers imposed by Ethiopia's trading partners do play an important role in determining the volume of Ethiopian exports. Moreover, export performance is positively related to Ethiopia's trading partners' national income, and distance, which is a proxy for transport costs, affects Ethiopian exports negatively.

Sisay (2010) in his study analyses factors affecting export supply of Ethiopia, during the period 1981 – 2004, have been made using co integration analysis. Data trend reveals that Ethiopian export performance was highly volatile during the period, on average merchandise exports have been growing at 7% per annum, while manufacturing exports were growing at 4% per annum. The trend also reveals that Ethiopia's export sector is mainly dominated by few primary commodities, where manufacturing exports account for less than 15% of merchandise exports on average.

The two models estimated depict that merchandise export volumes are significantly influenced by gross capital formation (proxy for production capacity) and share of trade in GDP (proxy for trade liberalization) while other variables; terms of trade, real effective exchange rate, foreign income, and foreign direct investment were found to be insignificant. Manufacturing exports equation reveals an interesting result,

manufacturing exports supply was found to be negatively & significantly affected by foreign income. Similar to merchandise export results, manufacturing exports were also found to be positively affected by gross capital formation. Terms of trade, real effective exchange rate, share of trade in GDP, and foreign direct investment were found to be insignificant. The study concludes with recommendations to increase share of manufactured exports and diversify export base of the country.

“Barriers to trade in services are more complex than are barriers to trade in goods. The empirical literature confirms that service sector performance critically depends on human capital, the quality of the telecommunication network, and the quality of institutions. The gravity framework has been widely used to explore the determinants of trade in services. Results of gravity models suggest that human capital skills and electronic infrastructure are important determinants of trade in services. The literature also suggests that the quality of institutions, as measured by the degree of corruption, complexity of 19 export procedures, and rigidity in employment law (Lennon 2006), or the economic freedom index (Kimura and Lee 2006) also positively influence trade in services.” (Lennon, 2006)

“Identifying the reasons for the success or underperformance of developing countries in exporting services remains challenging because of the lack of reliable data. Mattoo (2005) and Maurer and others (2008) describe some of the inadequacies in the data relating to trade in services. Service exports conform in certain respects to the predictions of the theory of comparative advantage with some degree of factor specificity. Broadly, a

country's exports of services depend on its endowments at any time of infrastructure, factors of production, and institutions relevant to services, in comparison to its endowments of these factors relevant to manufacturing. However, this is not as need of it in SSA country special in EA country it is still infant." Yishak 2009

"Trading partners influence the export performance of a country through their trade policies (tariff and non-tariff measures). In the world economy since 1950 there has been a massive liberalization of world trade, first under the auspices of the General Agreement on Tariffs and Trade (GATT) and now under the auspices of the World Trade Organization (WTO)¹ (Thirlwall, 2000). Due to these and other trade negotiations, access to international markets has improved. However, it is likely that there is still much to gain from further improvements in market access conditions." (Yishak, 2009).

"It has been shown that infrastructure affects trade via altering transport costs. In this context, they argue that infrastructure directly affects transport costs by determining the type of transport used (for example, the type and quality of roads determines the maximum size of trucks) and delivery time for the goods. Bougheas, Demetriades and Morgenroth (1999) have analyzed the effects of infrastructure on trade through its influence on transport costs and found a positive relationship between the quality of infrastructure and the volume of trade. Fugazza (2004) also finds that the internal transport infrastructure has a significant and positive impact in raising exports." (Yishak, 2009).

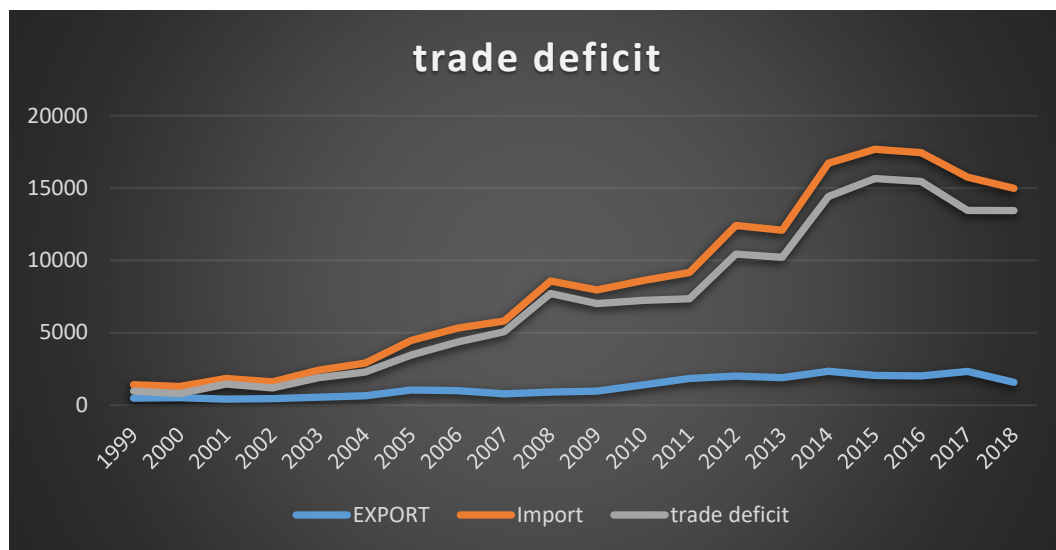
Chapter Three

3. Overview of Ethiopian External trade

3.1 Trade Balance

Ethiopia experienced a wider and increasing deficit in merchandize trade for more than fifteen years as shown in figure 1. Trade deficit occurs when the country's export is less than its import. It is normal to observe trade deficit in many economies including the developed economy like USA, however, the huge gap with consistent deficit is the problem of developing countries like Ethiopia.

Figure 1 Trend of external trade in million USD from 1999-2018



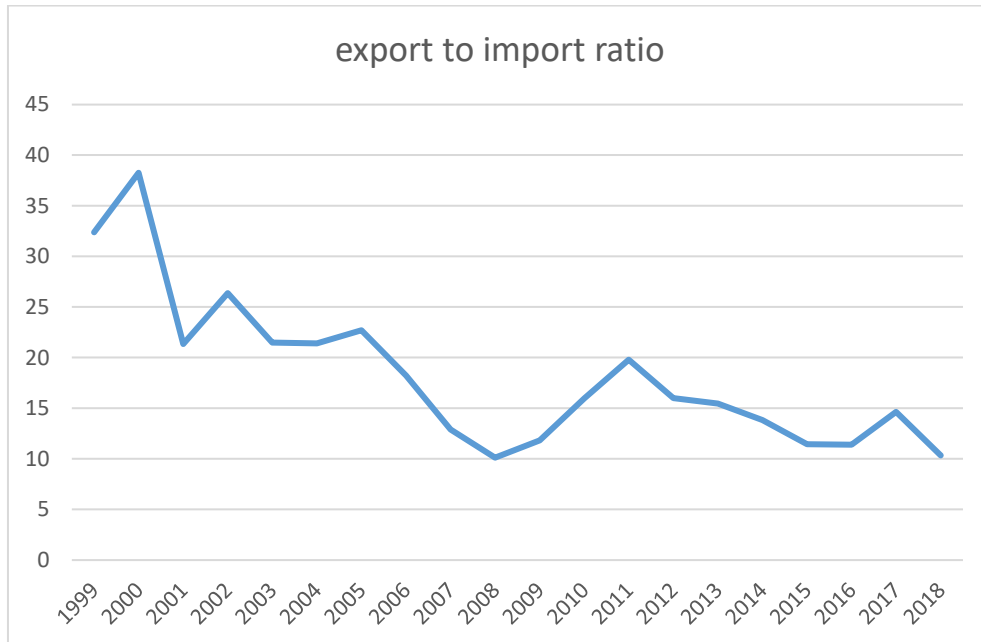
Source: UNCOMTRADE

According to the data from the UNCOMTRADE the gap was high in 2015 and 2016. This is because of the imbalance growth between import and export of goods. Compared to the growth and amount of the import of goods the export sector is low and weak. This drives the country to stay with an increasingly wide trade deficit.

3.2 Export to Import Ratio

Export to import ratio is used to measure the capacity of the country's export to finance the payment of import. As can be seen in figure 2 the ratio of export to import has shown a declining trend from 2000-2018. In 2000 the export sector finances 38.3 percent of import expenditure and reached to 10.3 percent in 2018. The export to import ratio reached at its lowest in 2008 which is almost equal to the 2018 ratio. This shows that the export sector is not performing well and /or the import sector is highly increased than the export sector. This trend indicates that the country has been financed its import payment through other means of financing like debt, remittance, foreign aid and etc. In relation with the country's economic development especially with the construction of infrastructures, the demand for import especially for capital goods increased. Although the imported capital goods are crucial for development journey, the country faced the problem in financing its import expenditure due to the weak performance of the export sector. This leads the country to finance its imports with debt which makes the country at high debt risk.

Figure 2 The export to import ratio in percent from 1999-2018



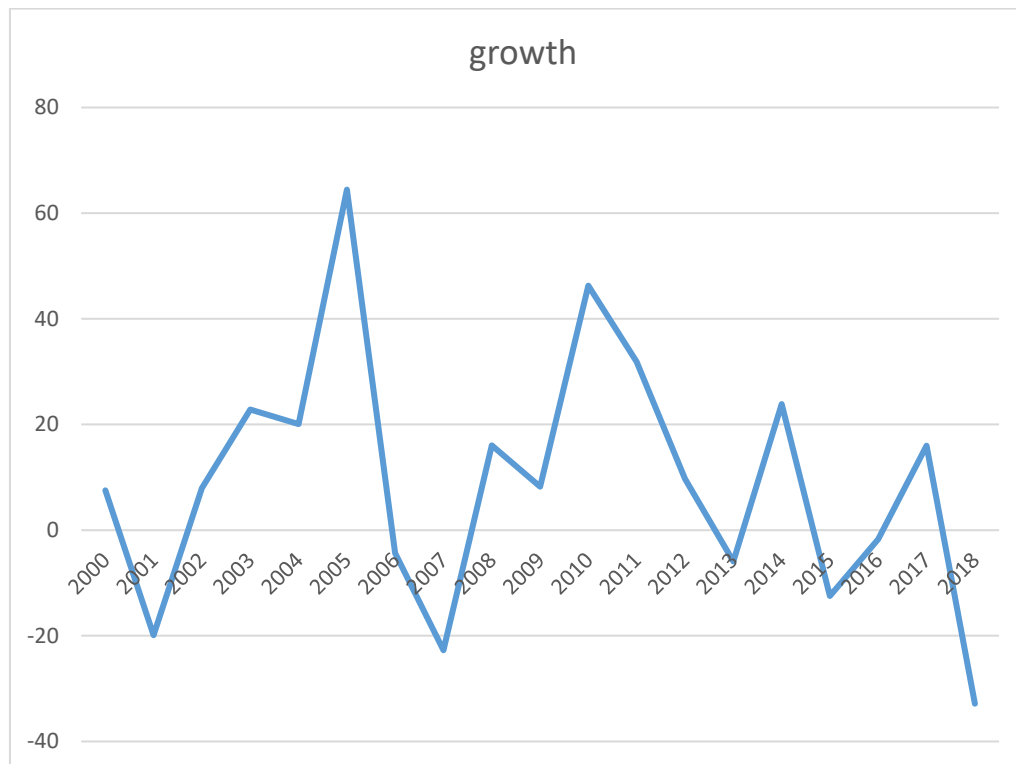
Source: UNCOMTRADE

3.3 Export growth

It is natural that the growth of export fluctuation, however, the growth of Ethiopian export sector has shown highly fluctuating and declining in recent years. Its instability may arise from the supply or the demand side of the export sector. As can be seen from the above figure the growth of the export trade has shown negative growth in 2001, 2006, 2007 2013, 2013 and 2018. During the rest of the study period though it has shown a positive growth still with strong fluctuation. In 2018 the of the export trade declined by 32.8 percent which is the highest decline among the study period. During this period

the amount of the export revenue was 1548.5 million USD which is lower than the export revenue that has been registered from the 2011-2017 consecutive periods

Figure 3 The growth rate of export sector from 2000-2018

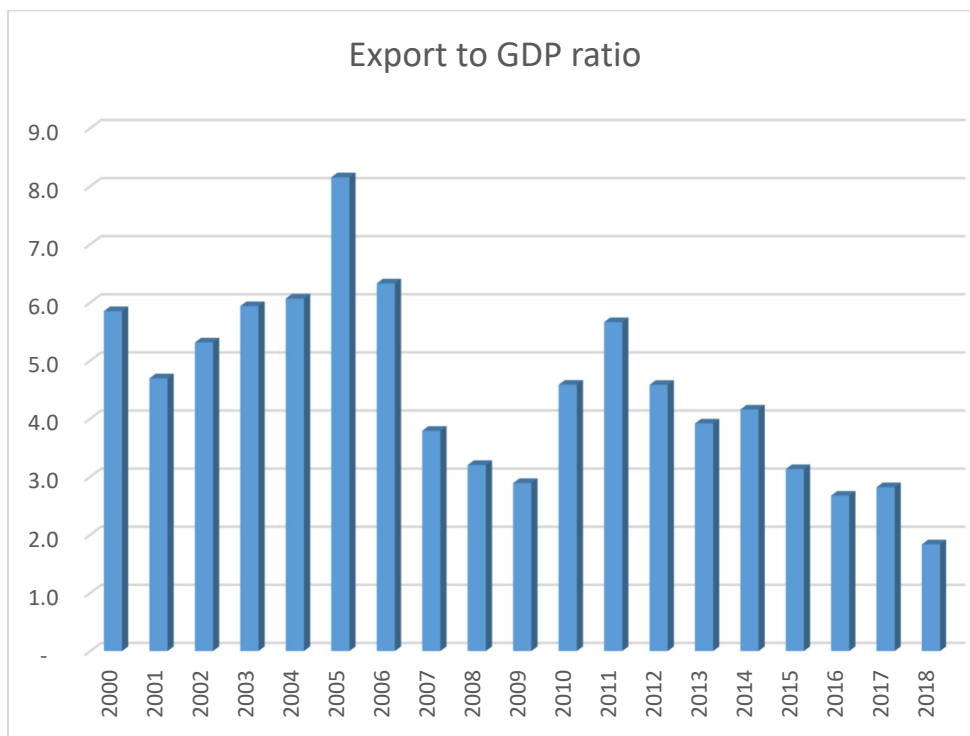


Source: UNCOMTRADE

Basically external trade (the sum of Export and import) to GDP ratio helps us to measure the openness of a country economy to international market. Measuring the share of export to GDP indicates that how much the country exports from its gross domestic products. When we see the share of Ethiopian export to GDP it is very low and shows a declined trend. Between the period 2005 -2018 its share to GDP has been declined except 2010 and 2011 . The country's export to GDP ratio was 8.2 percent in 2005

which is the largest share among the study period. And a 1.8 percent share was registered in 2018 which is the lowest export to GDP ratio. This indicates that on average the share of merchandise export from the total domestic production is around 5 percent.

Figure 4 Export to GDP ratio

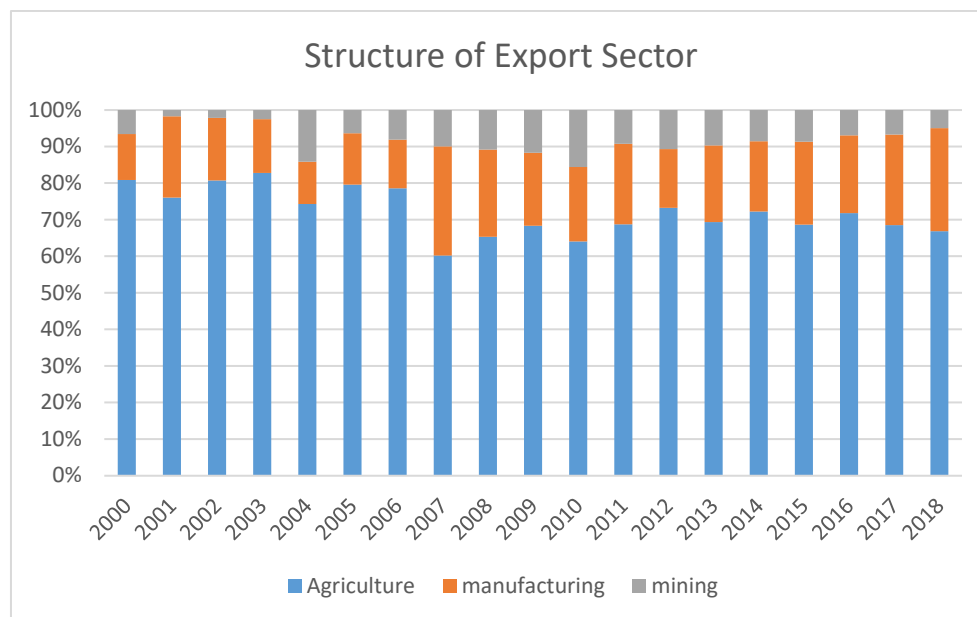


Source : UNCOMTRADE

3.4 The structure of the merchandise export sector

The export structure helps us to know about the country's area of specialization and understand about the characteristics of the export sector on that country. As can be seen in figure on average 70 percent of Ethiopian merchandise export was agricultural products and below 20 percent manufacturing and the mining export was below 10 percent. This indicates that the country's export comes from low skill production sector, and highly dependent on primary production which is agriculture. In 1999 the agriculture export was 80 percent but declined to 67 percent in 2018. The manufacturing export share increases from 11 percent to 18 percent.

Figure 5 The share of sectors in total merchandise export



Source : UNCOMTRADE

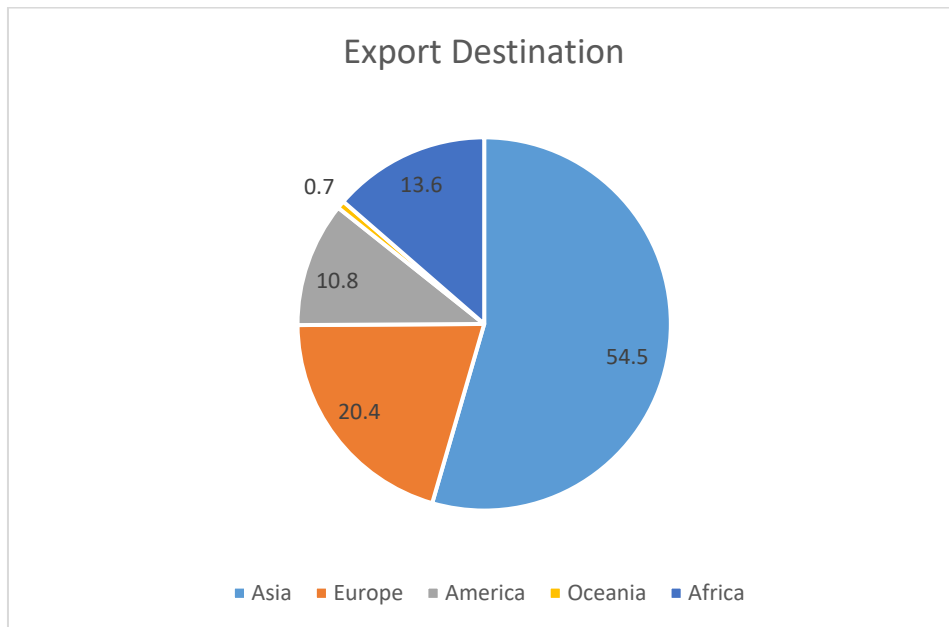
Generally, the country has been vulnerable to instability of merchandise export due to its dependent on primary commodities. This is due to the structure of the economy. Ethiopian economy is agriculture based economy. Though in recent years the share of the service sector become higher than the agricultural sector, the economy is highly dependent on the agricultural sector.

3.5 Export of goods by destination

Among the whole countries of Ethiopian goods export recipient countries, in 2018, China was the first largest destination, followed by Saudi Arabia and USA took the second and third market shares.

When we categorize in continent, Asia was the major destination for Ethiopian goods export by accounting 54.5 percent of total goods export in 2018. Among Asian countries Middle East countries are the major destination for Ethiopian goods export even though China took the first largest market from the whole Asian countries with a share of 8.94 percent from the total goods export. Saudi Arabia took the second largest share of Ethiopian goods export with 8.88 percent, followed by United Arab Emirates took the third largest market share for the country's export of goods with a 7.3 percent share.

Figure 6 Export of goods destination in 2018



Source: UNCOMTRADE

Europe was the second largest destination next to Asia. Among European countries Germany and Switzerland are the major importing countries of Ethiopian goods export during the same period.

Africa and North America took the third and fourth market share of Ethiopian goods export with 13.6 and 10.8 percent share, respectively. As can be seen from the graph the country's export of goods in Africa is low this is due to the nature of the export items. Like Ethiopia export commodities many African countries are exporting primary

commodities, so it is difficult to have the largest market in Africa even though there is a distance and free trade area advantages.

Export Trade Promotion in Ethiopia

One of the important factor for increasing the foreign market access of domestic producers is export trade promotion agencies. This agency will help the domestic firms by giving important information regarding the foreign market and also find market. Many countries that have this organization have a successful story on their export performance. Ethiopia has realized the importance of export promotion agency and established Export promotion council which was led by the prime minister and the in 1998 the country established the Export Promotion Agency. However, due to the export promotion strategy was transformed to industrial development strategy, the agency responsibilities were taken by the ministry of industry. After the transformation of the promotion agency its focus mixed with the industrial development. Though the industrial development is necessary for the export sector the export promotion agency responsibility is shrinks and lacks focus. Due to this it couldn't find market access for the exporters.

Chapter Four

4. Methodology and Research Findings

4.1 Methodology of the study

4.1.1 Types of data and source

Secondary data has been used for the analysis that mostly obtained from UNCOMTRADE, IMF, WB, NBE, PDC and other compiled sources.

4.1.2 Methods of Data Analysis

The available data are analyzed using descriptive types of data analysis, graphs and tables.

4.2 Research Findings

In order to analyses the main challenges of the country's export of goods, the researcher first used to see the major export commodities through their export revenue, volume and price trend analysis. By observing the trend of these three issues we can see where is the main problem for the export sector of the country.

According to the 2 digit HS code categorization the number of major export items during the study period were fluctuate. In some years it increase and on the other years it decreased. This means there is a new export item entry and exit. This may be due to the supply or the demand side problem. This has an effect for the fluctuation of the export sector. In recent years the number of export items are around 60 according to two digit level of categorization. Among these 85 percent of the export earning is from 9 export

item categories especially more than 65 percent is from coffee, oilseeds and vegetable and fruits. The following table shows the five year trend of the major export items using two digit level categorization.

Table 1 The share of major export items in total merchandise export

year	2014	2015	2016	2017	2018
COFFEE	29.6	33.5	32.4	35.1	25.3
OIL SEED,OLEAGINUS FRUIT	27.6	21.2	24.3	18.6	20.9
VEGETABLES AND FRUIT	11.0	10.2	12.4	11.9	19.0
LEATHER, LEATHER GOODS	4.0	4.8	4.8	4.3	6.6
MEAT, MEAT PREPARATIONS	3.6	4.4	3.5	3.4	3.3
CLOTHING AND ACCESSORIES	2.3	3.5	2.9	3.3	3.1
GOLD, NONMONETARY EXCL ORES	6.4	7.0	5.5	5.0	2.6
FOOTWEAR	1.4	1.7	1.9	2.0	1.7
LIVE ANIMALS	1.6	0.8	0.8	0.5	0.8

Source / UNCOMTRADE

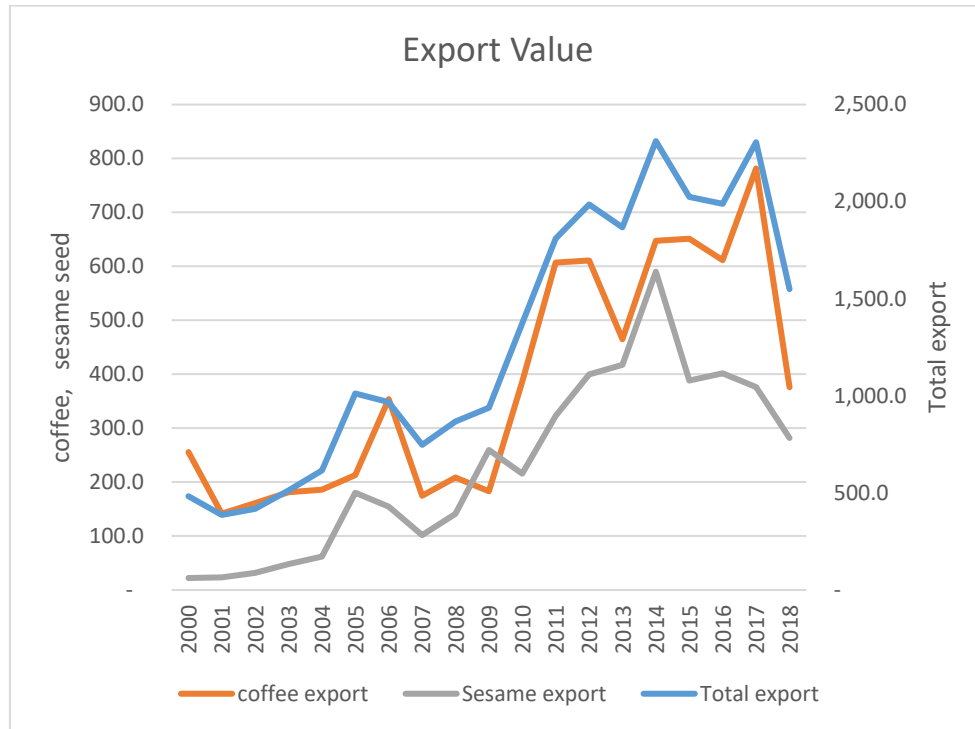
The two digit categorization helped us to see the categorized export items in terms of value, however, in order to get the volume and price of the export item we need to see the six digit HS code data. When we see the six digit export items it gives us the individual export items value and quantity. Based on this the researcher got the price data by taking the ratio of value and volume. Using the six digit level data the country's

major export commodities are coffee and sesame seeds. According to this categorization coffee, sesames seeds had around 50 percent share on average from the total goods export.

For the other two digit level categorization most of them has small share at six digit code data and the data are not consistent.

Therefore, because of the data consistent and their large share, coffee and sesame seeds are used as a sample for these study. As we have seen from the previous explanation about the structure of Ethiopian goods export, agricultural export commodities took around 70 percent of the total export of goods, of which coffee and sesame seed which had 50 percent share from the total goods export will take the lion share of the agricultural export. This indicates that Ethiopian export is highly depended on these two agricultural products. If we can understand the two commodities export problem we can easily understand the total goods export problem.

Figure 7 The trend of Total export , coffee and sesame export in millions USD



Source : UNCOMTRADE

The above graph shows us how the total export is highly affected with the coffee and sesame seed export value. If we see the coffee and sesame export value both have almost the same trend during the study period. Except in 2005 and 2009 both commodities export showed the same direction increased or decreased trend at the same time even though the magnitude of increment or decline is different. . This may come from the nature of the export items which is agricultural commodities. We can observe from the above graph the total goods export showed high fluctuation when both commodities

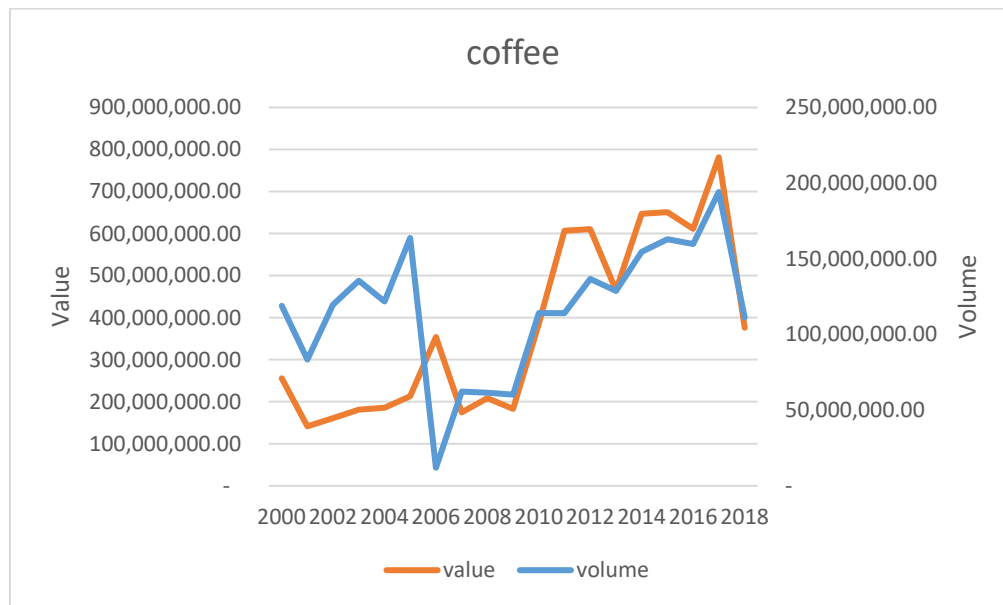
export value fluctuate. From 2012-2018 the total export value has shown high fluctuation than the previous period because of the high fluctuation of both commodity exports.

i. Coffee export

Ethiopia is known for its coffee export in the world. The coffee export is the first export commodity with a lion share of the total export revenue more than 50 years. The major source of Ethiopian foreign currency is coffee with a largest share of total export goods income, however, the coffee export is not stable. This indicates that how the country's export earning is relied on coffee export. During the study period we can see a high drop and increment of the commodity export earnings. Its share become declined from 48.5 share in 1999 to 25.3 percent in 2018 due to the other export commodities export increment. However, it has still the largest share from the export revenue and . However, 99 percent of coffee was exported with no value addition. This made disadvantaged the country since its price is low at international market.

Income and volume of coffee export

Figure 8 The Coffee export value and volume



Source: UNCOMTRADE

As we can see from the above graph both the export volume and value of coffee were instable. For most of the study periods they are going in the same direction. However, in some years they went in different direction. In 2005 the volume of coffee export was high, however, in 2006 it shows a high drop. The same fluctuation continue till 2018. The volume coffee export recorded a 111.8 million quintile in 2018 which is less than is less than from 167.7 million quintals and 114 million quintals of coffee export in 2005 and 2010, respectively. On the other hand in 2006 the volume was 11.9 million quintal and on the next year it increased to 62.2 million quintals which is 5 times from

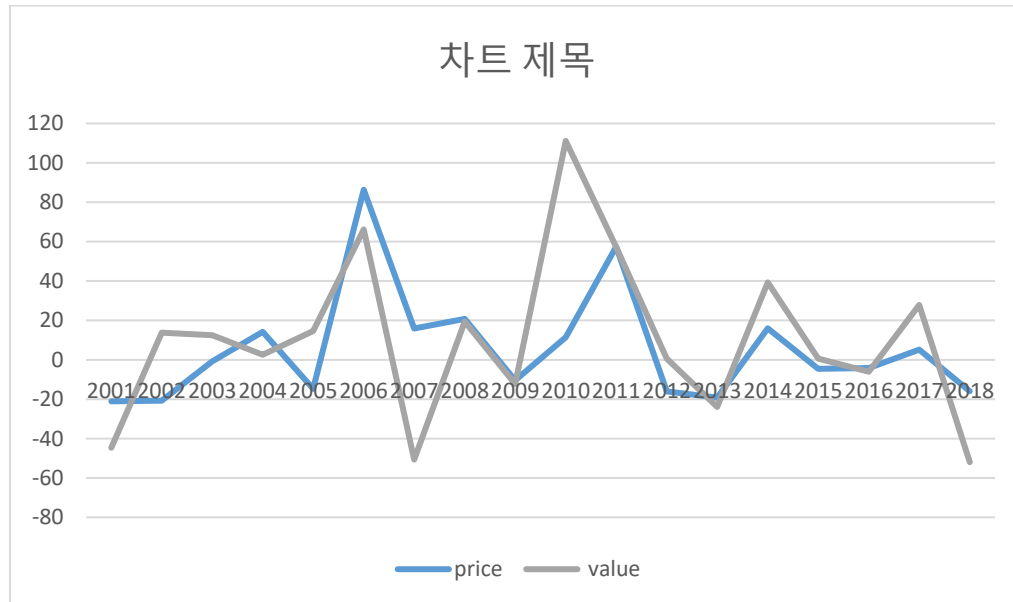
the previous export volume. This indicates that how the volume of the coffee export instable and drives the coffee export earning to unstable.

The export value/income of coffee is increased when both the volume and price of coffee export increased or decreased except in 2006 and 2007. Though it is clear that the export value will increase/decrease when the volume is increased/decreased, we can see some different situation in 2006 and 2007. In these two consecutive years the export value of coffee has shown inverse relationship with its volume.

In 2006 the coffee export value increased even though the volume has shown a high drop this is due to the price increase. When we see the 2007 case, coffee export value declined though the volume is increased due to the decrease of coffee price.

In general we can see that how the instability of the volume of coffee export affects the income of coffee export stability. This indicates that how the volume of the coffee export affects the income of coffee export. One of the main challenge for the coffee export is the volume problem which we can say it is the internal or supply side problem of the country.

Figure 9 The growth of Coffee export value and price



Sources: UNCOMTRADE

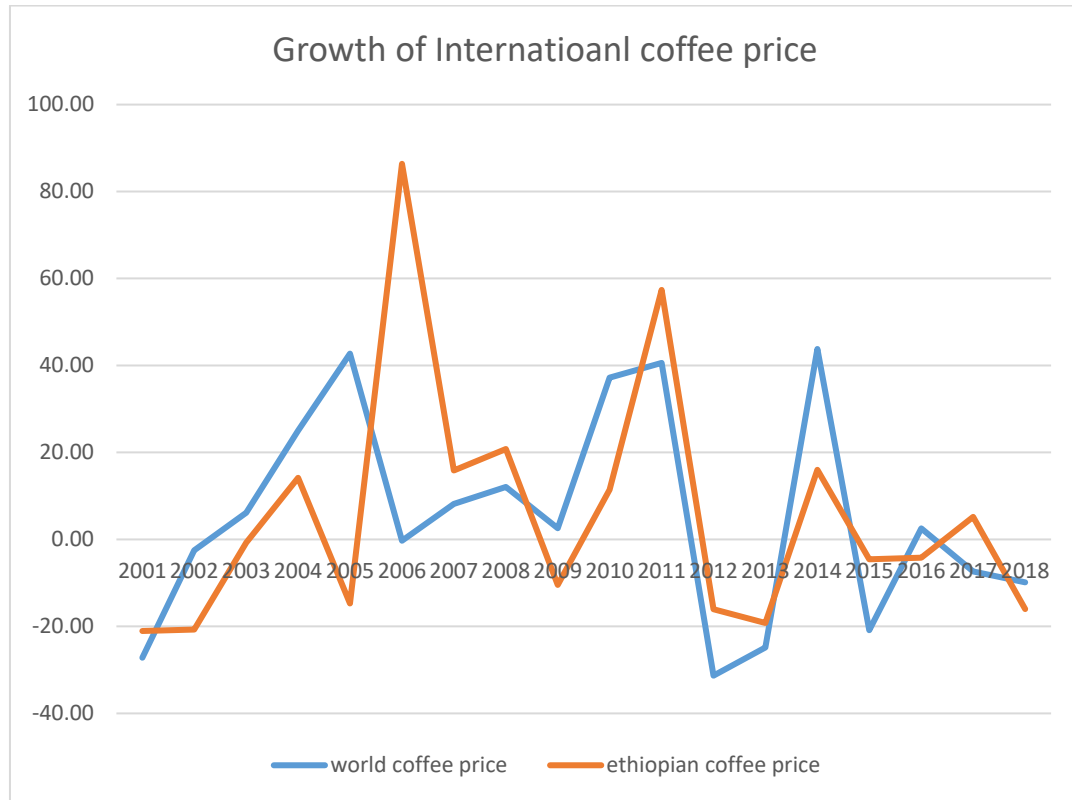
The growth of both coffee export price and its value shown a high fluctuation during the study period. This tells us how the price fluctuation affects the earnings of coffee export. For instance in 2005 the growth of coffee price was negative which 14.7 percent is - and in the next year (2006) its growth become positive and 86.4 percent. The coffee price instability comes from the price instability of primary commodity prices at the international market. Since coffee is the country's major export item its vulnerability to price volatility affects the total export earnings of the country.

In addition, when we see the structure of Ethiopia coffee export unroasted coffee has 99 percent share whereas the roasted coffee export is only 1 percent from the total coffee export earnings. And the roasted coffee price is much higher than the unroasted coffee.

Due to this the total Ethiopian export earning is weak since the coffee export has a larger export share.

In order to make sure the price volatility of Ethiopian coffee export is due to the nature of the primary commodity price which the country cannot control or due to the quality of the product the researcher used comparative trend analysis between Ethiopian coffee price at the international market and the general coffee price at the international market. For this study the Ethiopian coffee price was taken by taking the ratio of coffee export earnings to the volume of coffee. Whereas, the general world coffee price was taken as a representative for the other countries coffee price. So based on this when we see the trends of both Ethiopian and world coffee price, they have the same trend except in 2005 and 2006. Therefore we can infer that that the Ethiopian coffee had no that much quality issue at the international market.

Figure 10 Ethiopian Coffee price versus general coffee price at international market



Sources : UNCOMTRADE

The world coffee price is the general coffee price at the international market and Ethiopian coffee shows the price of Ethiopian coffee at the international market. It is known that the primary commodities price is highly volatile than other commodities price. However, we can specifically compare the price of a country's specific commodity price at the international market with the other countries commodity price at the international market in order to see its competitiveness. If the World coffee price increases and Ethiopian coffee price at the same market increases, however, in two

consecutive periods of the study (2005 and 2006) they went in different directions. So we can infer that Ethiopian coffee export is competitive at the international market though it is volatile due to the nature of the product which is the price of primary goods is highly volatile than the other goods and services.

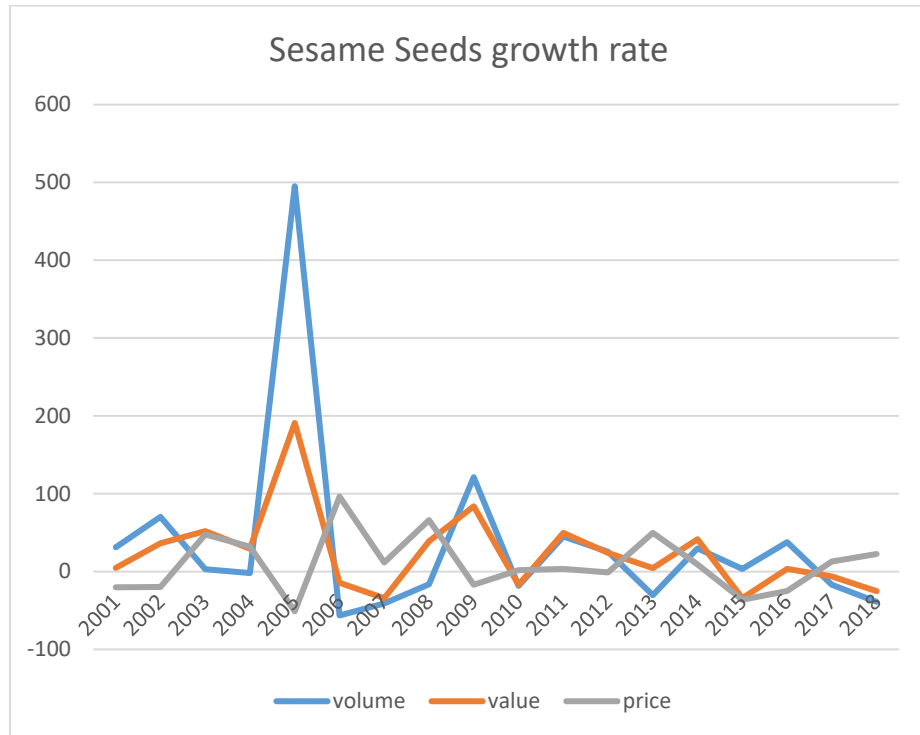
In general we can say that from the three graphs that we have seen above, the coffee export earning is unstable due to both volume and price of coffee exports were fluctuating.

ii. Sesame seed export

Though oilseeds has the second largest share from the total export more than 90 percent of the oilseeds comes from sesame seeds.

Next to coffee export earning sesame seeds export is the second largest source of the country's foreign currency. For the more than twenty consecutive years it was the second contributor of export earnings. So the export volume and price of this export commodity has a significant effect on the total export performance. In 2018 sesame seed generated 18.2 percent of the total export earnings. This commodity had registered a 25.5 percent share which is the largest share among the study periods. This shows us how the country export earning relied on sesame seed next to coffee export.

Figure 11 Sesame seed export growth



Sources : UNCOMTRADE

As we can see from the above graph though both the growth of volume and price sesame seed export has shown high fluctuation during the study period. This leads to instable the export earning of sesame seed. However, if we see carefully the trend of both volume and price growth, the export earning of the sesame seed is highly affected by its volume. In all the study periods when the growth of the volume declined the export earning of the commodity declined. On the contrary we see that the export earning has increased while the growth of the price showed decrease. For instance in 2005 and 2009 the export earning from sesame seed increase though growth of the price declined due to the

increase of the volume. In 2013 we can observe that the export earnings declined even though the price showed increment due to the decline of the volume export of sesame seed. From this we say that the income of export from sesame seed is much affected by the volume /supply of the commodity than its price /demand problem.

iii. Drought and export in Ethiopia

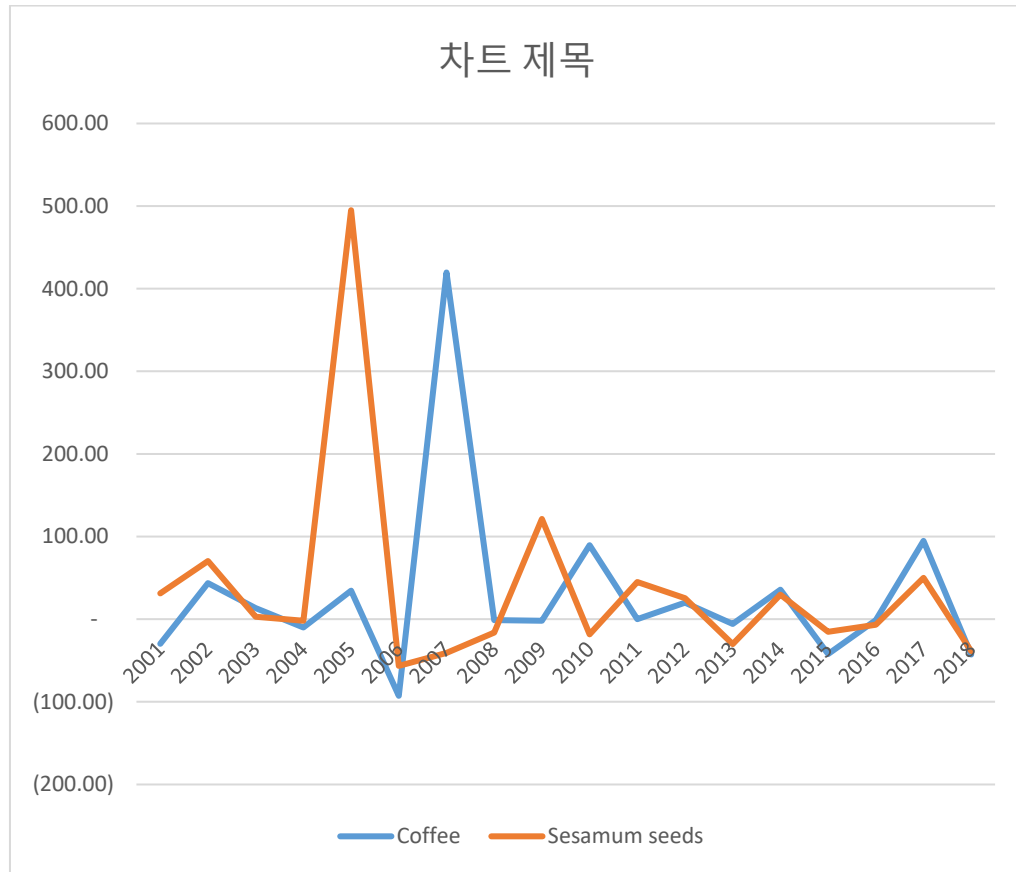
From the two major export commodities of the country we have figure out that the price and volume of coffee export affected the export earning of coffee , and hence the total export earnings. For the price volatility problem we have checked that weather it is due to the quality problem which the country should improve or the nature of the market demand for the product which the country cannot control. So based on this analysis we have seen that the problem came from the price volatility problem. For the sesame seed the researcher didn't compare the price of sesame seed with the world sesame seed price like coffee price due to the data problem as well as its low effect compared to the volume of sesame seed export. However, by observing the nature of primary commodity prices in general we can say that most of the price fluctuation is due to the international primary commodity price volatility.

For the supply /volume fluctuation we have to check that weather it is a production problem or other supply side constraints. In order to check this we have to this the drought and export volume of the two products trend.

In 2006 ,2015 and 2016 Ethiopia sefered a lot due to the occurrence of drought. Since the country export is agriculture dominated export it is directly affected by the drought. Due to drought it is clear that coffee ,oilseeds, pulses and live animals were damaged and thus the export volume of the agricultural products declined and the overall export value also declined.

The major delcined years of the export volume of both coffee and sesame seed are coincided with the occurrence of drought . As the above graph shows that 2006, 2015 and 2016 the volume of coffee and sesame seed export growth was below zero. the volume coffee export declined by 92.7 percent, 42.2 percent and 1.2 percent in 2006, 2015 and 2016 , respectively. Like the coffee volume of export the sesame seed export volume has shown a negative growth during these periods. the sesame seed volume of export was declined by 56.4 percent , 15.4 percent and 6.8 percent in 2006, 2015 and 2016 respecively. During these periods the counrty faced drought which affected highly the agricultural sector.

Figure 12 Growth of the Coffee and sesame seed volume



Source: UNCOMTRADE

More than 166 million USD was needed for around 1.7 million people who were at high risk of hunger and disease due to the occurrence of the drought in the country in 2006. During this period the country lacked the rainfall which drives the agricultural products to fall and farmers and pastoralists exposed to starvation. Among East African countries Ethiopia, Somalia and Kenya were in danger of drought effect (CERF, 2006).

During the same year FAO released the news that mentioned about the drought in Ethiopia and demanded 18.5 million USD for farmers and pastoralists who were affected by the drought and faced food crisis (FAO, 2006). During this period the crop and livestock was highly affected and then widespread human and livestock migration was appeared. The main reason for this drought was a fall of rainfall in autumn season. This indicates that how the Ethiopian economy in general and the agricultural sector in particular are relied on rainfall.

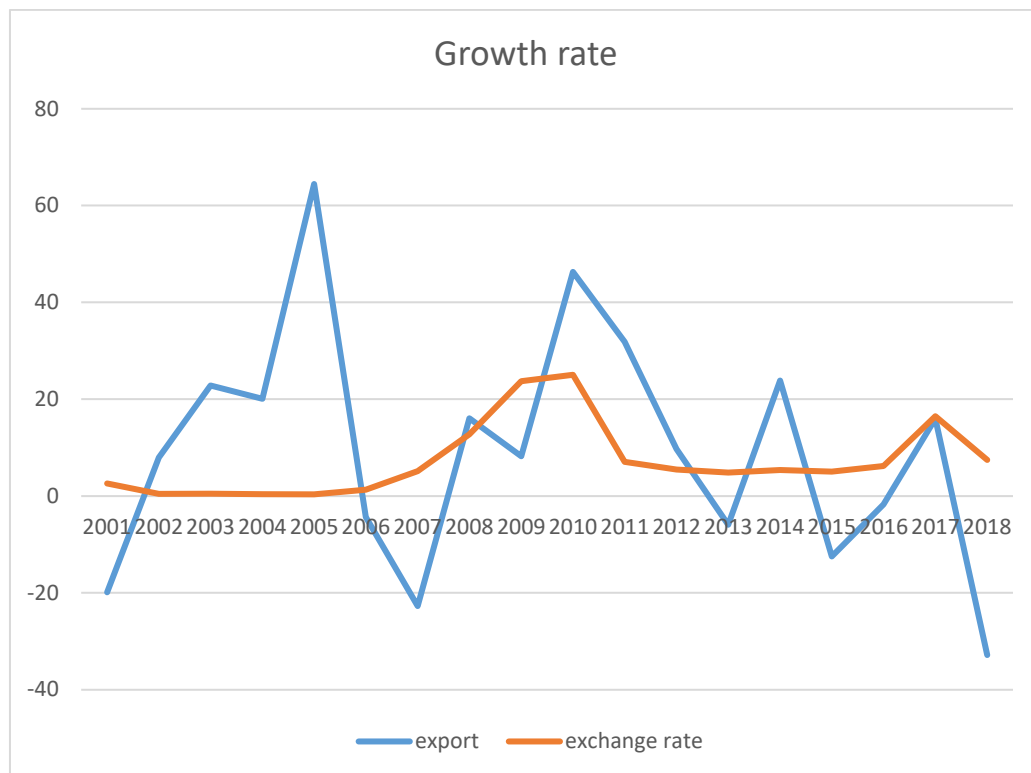
In order to help the affected groups of society particularly the farmers and pastoralists, the international organizations like FAO and the Ethiopian government worked together in mitigating the effects of the drought to save the livelihoods. And also they worked on other supporting system to save the assets of the farmers and pastoralists. Because of different kinds of support like technical and financial support including seed, drugs, vaccine the production of the agricultural sector increased in 2007 and hence the volume and earning of export also increased.

Due to the incidence of the El Niño induced drought phenomenon in 2015 and 2016 the country's export earning was negatively affected. According to the BBC news around 10.1 million people were in danger of food security due to the drought. The Pacific Ocean warming caused the so called El Niño drought in these consecutive periods which was the worst in the 50 years, however, due to the effort of the Ethiopian government in mobilizing national resources with international humanitarian organization aid its effect was less than the expectation (BBC, 2015)

Generally the Ethiopian export is highly dependent on the production of agriculture and easily affected with the rain fall. Relying on agricultural sector by itsel is not a problem , however, relying on the rain fall will be a critical problem for the agricultural sector as well as the export sector.

iv. Export and exchange rate

Figure 13 The growth rate of export and exchange rate



Source: UNCOMTRADE

Ethiopia used the devaluation monetary policy on its currency in 2009, 2010 and 2007 to increase the competitiveness of commodity export. However, the export sector is not that much affected with the exchange rate policy. As can be seen from the graph the export sector after 2009 and 2010 devaluation it didn't show the expected result rather it declined for the consecutive three years. When we see the 2017 devaluation the export sector increased at the same year but declined in 2018. This indicates that even though the country's currency devaluation make its export cheaper in the international market the export earning is not increased as it is expected. This shows that the export sector is much affected by other issues than exchange rate.

Chapter Five

5.1 Conclusion

The vital question investigated in this paper is which factors significantly determine the export performance of Ethiopia. To address this question the study used the time series data trend analysis for the period 2000-2018. The secondary data are collected from different sources and document reviews. In this study total merchandise export, the major export items, exchange rates, drought, documents on Ethiopian export are used to investigate the challenge of the country's export.

Ethiopian export structure remains undiversified and highly depended on few agricultural commodities. Such as coffee, oilseeds, vegetables and fruits, leather and leather products , meat and meat products , gold, footwear, clothing and accessories and live animals which accounted 80 percent on average . Of which Coffee and sesame seed has 50 percent share on average in total merchandise export.

Ethiopia has taken different measures such as export financing incentive schemes, export trade duty incentive scheme and duty free importation scheme to those wholly engaged in supplying their products to foreign markets. However, the export sector is not satisfactory.

Agricultural export have a massive contribution in the country's export, agricultural export performance of a country still did not achieve to the preferred step caused by a

number of constraints. High dependence of exports on primary exports has many drawbacks for the country.

The basic constraints for Ethiopian exports include the low volume of exportable products, the limited degree of diversification of exports, which are made up mainly of unprocessed primary products.

Ethiopia's external trade has major problems both on the supply side – its dependency on few primary products, characterized by large fluctuations in volume; and a very high degree of concentration of exports on few commodities – and on the demand side – a low income elasticity for the type of commodities that Ethiopia exports, declining prices for its exports, and limited destinations for Ethiopian exports. Both supply and demand side problems are typical African problems: For example, more than 50% of African countries 'export earnings are derived from only three principal commodities such as coffee, tropical beverages and cocoa.

In theory devaluation of the domestic currency against to foreign currency will make the price of the export and competitive at the international market, however, in Ethiopia case it doesn't boost the export. This indicates that the problem of the export sector is supply problem.

Furthermore, weather condition affected the production of export goods so the export sector easily collapse with the occurrence of climate change.

Lack of strong export promotion institution which handle export related issues contributes for the poor performance of the export sector.

5.2 Policy Recommendations

The Ethiopian economy is growing from time to time. To be continued the growth our country should or strongly work growth contributed variables. Among growth contributed variable export is the major one. Therefore, Ethiopian exports highly dependent on agricultural commodity. The study identified that even though there is a demand side problem the supply side problem is the major challenge of export performance of a country that contributed.

Therefore, based on the finding can be recommended to the countries policy makers the following points;

- ✓ Ethiopian export commodities offer should be diversified and in addition to primary agricultural products export more attention should be given to fully and better processed, value added manufactured items, which can increase level of foreign currency reserves and facilitate import substitution.
- ✓ The country should build a climate-resilient economy to recover quickly from climate impacts in the short and long terms.
- ✓ Strengthening the irrigation system for the agricultural sector which is the main source of export.
- ✓ Expanding and strengthening the Insurance service for the agricultural sector in order to make farmers to survive from the drought season.

- ✓ A need to establish strong Export Development and Promotion Agency which is responsible for handling export related activities. Export market intelligence, trade policy facilitation, product identification, development and adaptation and capacity building and information dissemination and other related issues can be handle by the agency. Inaddtion to that National productive sector competitiveness support council, National economic and business coordination committee diplomacy committee , National export coordinating committee should be establish to support the Export Development and Promotion Agency. In order to have such kind of organization the government should take South Korea's KOTRA , Matrad of Malesia and VIETRADE of Vietnam which has registered remarkable achievements on their export sector as a bench mark.
- ✓ The country should also strengthen the service sector export.

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요약

이 연구는 에티오피아 상품 수출의 주요 과제를 파악하는데 주안점을 두었다. 양적 데이터 및 정책 문서가본 연구의 기초자료로 사용되었다. 연구방법으로는 데이터를 분석하기 위해 기술적인 분석 방법이 적용되었다. 이 연구에서는 2000-2018 년의 에티오피아 상품 수출이 취약하고 불안정한 것으로 나타났다. 이는 농산 수출품목이 특히 커피와 참깨에 많이 집중되어 있기 때문이다. 또한 가뭄이 수출 부문에 영향을 미쳤는데 이는 수출 수입의 주요 원천이 농업 부문이었기 때문이다. 본 연구는 궁극적으로 적용된 기술 분석 및연구결과를 바탕으로 실현 가능한 정책을 제언하였다.