



**INFRA FINANCIALS**

# INSIGHTS ON NEW OPPORTUNITIES IN THE ETHIOPIAN BANKING SECTOR

By: Infra Financial 's – Research and Analytics

November 2022

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## Insight Focus coverage areas

**New Policy on the banking sector**  
**Possible risks related to the entry**  
**Financial sector landscape in Ethiopia**  
**Top 10 private commercial banks**  
**Foreign bank entry modalities**  
**Foreign bank requirements in other African markets**

### New Policy on the Banking Sector

A policy to open up the banking sector to foreign investment was approved by Ethiopia's council of ministers on Saturday 3rd Sept 2022.

The approved document states that opening up of the sector will strengthen linkages of Ethiopia's economy with the rest of the world as well as bring new technologies, enhanced banking skills/ knowledge, specialized products and services into the sector.

The move is further expected to enhance competitiveness, effectiveness, efficiency, and dynamism of the financial sector.

It is expected that the decision will facilitate the supply of finance, foreign currency, credit and increase job opportunities.

By ensuring economic efficiency and international competitiveness, opening up of the sector will enable Ethiopia to ensure continuous economic growth.

### Possible Risks related to the entry

In addition to the above discussed advantages, it is Infra Financials research and analytics team opinion that the followings are the main risk exposures associated with the entry of foreign banks to the sector.

- o Contagion risk: The spread of economic crisis from one market or region to another. Similarly the risk that financial difficulties at one or more international banks spill over to a large number of other banks or the financial system as a whole. This occurred in 2008/9.

- o Foreign ownership concentration: Dominant foreign ownership in the banking sector exposes the economy by a greater extent to risks from financial and economic distress in other countries or region.

- o Foreign banks might leave the market if the domestic economy faces challenges and profitability declines.

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o Supervisory challenges: Complex and cross border financial products and services that will be carried out by foreign banks might be beyond National Bank of Ethiopia's capacity.

It is the teams' opinion that the above risks can be mitigated by the formulation and implementation of strong regulations and adequate policy safeguards.

### Ethiopian Financial Sector is changing

It is Infra Financials research and analytics team opinion that:

Foreign banks will gain entry into the Ethiopian market of over 100 million plus population once the council of ministers decision and detailed implementation steps are approved by the Ethiopian parliament and duly gazetted in the Negarit Gazeta, alike other key policy decisions.

The scope of activities that will be performed by the foreign banks, entry requirements and governance standards are expected to be detailed in the Negarit Gazeta.

National Bank of Ethiopia (NBE) will be expected to prepare/ amend the regulations, change the supervision and monitoring systems before the entry of foreign banks. It is also expected to continuously strengthen them after the entry. In addition to the system, NBE should

review its structure and build the capacity of its staff.

Formerly a protected strategic area closed to foreign participation, the Ethiopian financial sector encompasses banks, insurance and micro finance entities. After the opening of the telecom sector to foreign participation, the financial sector was expected to be next in line.

NBE directive dated 12th April 2021, increased banks min capital from ETB 500 Million to ETB 5 Billion. Banks are expected to comply by target date of 30th June 2026 and have 4 years to meet the requirement. The enhanced capital requirement is likely to trigger mergers/ acquisitions as banks seek to meet the requirement. The opening up of the banking sector to foreign participation will provide a further source of capital besides domestic sources.

The banking sector in Ethiopia is one of the most lucrative sectors with returns on investment of between 20%-50%<sup>1</sup>.

Currently 29 commercial banks, 1 development bank, 18 insurance companies, one reinsurance company, 40 microfinance institutions, 6 Capital goods Finance/Lease companies, and 8 payment instrument issuers/system operators are operating in Ethiopia<sup>2</sup>.

There are about 28 privately owned banks currently operating in Ethiopia, while the state owned Commercial Bank of Ethiopia

<https://newbusinessethiopia.com/finance/ethiopia-finally-opens-door-for-foreign-banks/>

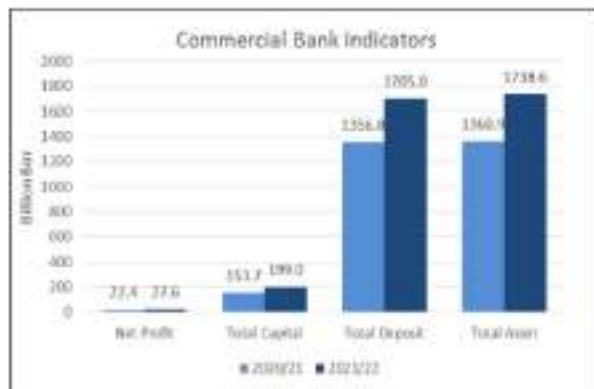
<sup>1</sup>NBE





has close to half the market share in the industry.

According to the NBE, the number of banks has increased from 23 to 30, and their branches rose to 8,944, as of June 30, 2022, from 6,595 June 2021. With the expansion of bank branches, the ratio of branch per population stands at 1: 11,516 (one bank branch serves 11,516 people). Total deposit has increased from 1.4 Trillion Birr to 1.7 Trillion Birr over the last one year. The total capital of the banks has boosted from 153.7 Billion in 2020/21 to 199.1 Billion Birr in 2021/22, rose by 29.5 percent. Moreover, total asset of banks has increased from 1.4 Trillion Birr to 1.7 Trillion Birr registering an increment of 21.4 percent. Net profit of banks has increased from 22.4 Billion Birr in 2020/21 to 27.6 Billion Birr in 2021/22.

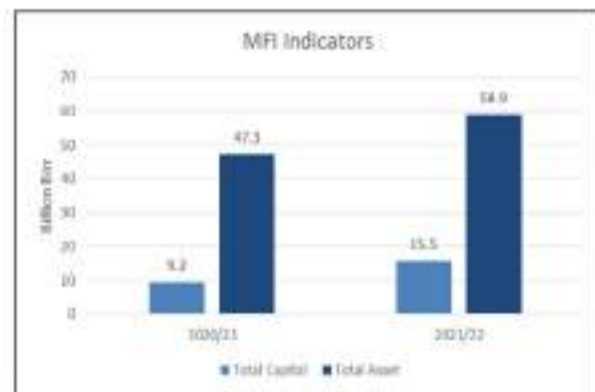


Source: NBE

In 2021/22, the number of insurance companies stood at 18, whose branches rose to 690 from 635 last year. Moreover,

Business info Ethiopia

insurance companies increased their total capital by 20.9 percent to Birr 13.4 Billion. Microfinance Institutions (MFIs) reached 40 in number, their total capital and total asset increased by 68.2 percent and 24.6 percent and stood at Birr 15.5 Billion and Birr 58.9 Billion, respectively in 2021/22.



Source: NBE

There are around 9 foreign bank representative offices operating in Ethiopia, namely: European Investment Bank, Standard Bank, CIB-Egypt, Commerz Bank, KCB Bank, Bank of Africa, Ziraat Bank, Export-Import Bank of India, and Equity Bank3.

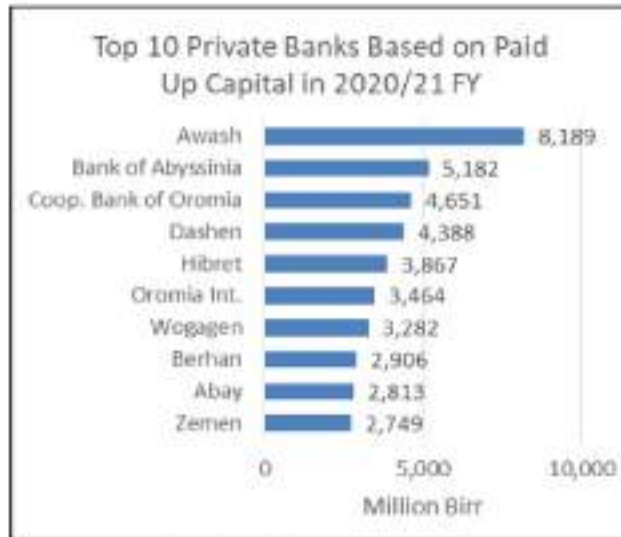
Top 10 Private Commercial Banks

In 2020/21 FY, among the top 10 private banks selected based on their paid up capital, Awash International Bank has registered 8.2 Billion Birr by creating a very wide range from the second ranked bank, Abyssinia, that recorded 5.2 Billion Birr. The third, fourth and fifth placed banks are

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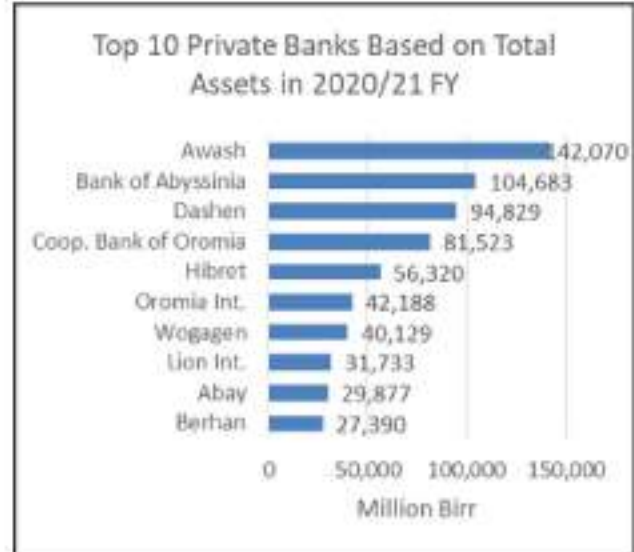


Cooperative Bank of Oromia, Dashen and Hibret Bank, they have reached 4.7, 4.4 and 3.9 Billion Birr respectively.



Source: Research and Analytics Team Compilation

In terms of the total assets registered in FY 2020/21, Awash Bank has attained 142 Billion Birr by creating a wide gap from the second ranked bank, Abyssinia, which recorded 104.6 Billion Birr. Dashen bank has ranked third place by registering 94.8 Billion Birr followed by Cooperative and Hibret that recorded 81.5 Billion Birr and 56.3 Billion Birr respectively.



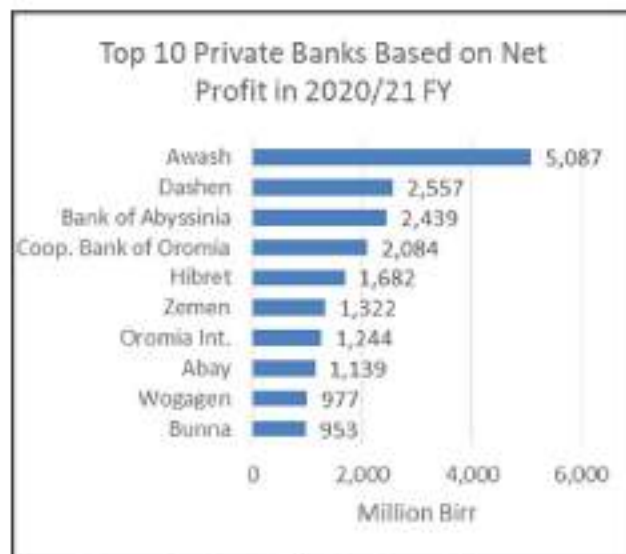
Source: Research and Analytics Team Compilation

In terms of net profits<sup>4</sup> earned in 2020/21, Awash, Dashen, Abyssinia, Cooperative bank of Oromia and Hibret are the top 5 ranked private commercial banks. Awash bank has earned 5.1 Billion Birr, almost double of the profit earned by the second ranked bank, Dashen (about 2.6 Billion Birr in amount). Bank of Abyssinia, Cooperative bank of Oromia and Hibret banks ranked 3rd, 4th and 5th place generating net profit of 2.4, 2.1, and 1.7 Billion Birr respectively.

Based on the above three banking indicators; paid up capital, total assets and net profits, the top 5 private commercial banks are Awash, Bank of Abyssinia, Dashen, Hibret and Cooperative Bank of Oromia for the period under review.

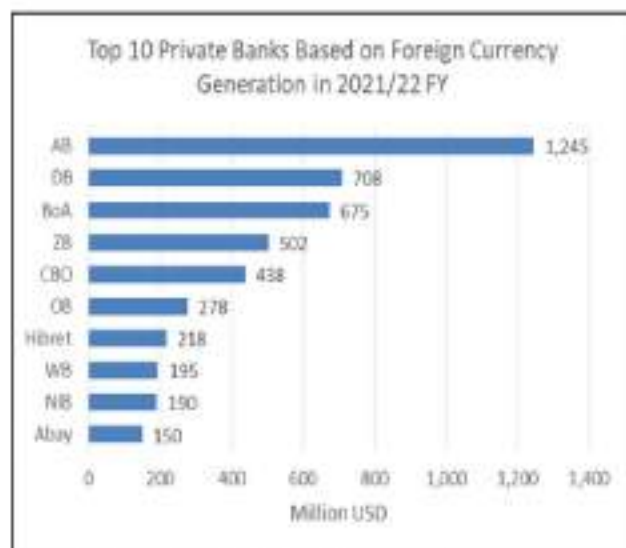
<sup>4</sup>Profit after depreciation and provisions

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Source: Research and Analytics Team Compilation

Awash, Dashen, Abyssinia, Zemen, and Cooperative bank of Oromia are consecutively the top 5 private banks that generated the highest foreign currency in 2021/22 FY. Awash alone has earned almost 1.3 Billion USD in 2021/22 FY.



Source: Research and Analytics Team Compilation

## Foreign Bank Entry Modalities

It is Infra Financials research and analytics team opinion that foreign banks, upon opening up of the banking sector will operate in four different modalities. These include opening of: -

- o Foreign bank representative office,
- o Foreign bank branch office,
- o Joint venture with local banks,
- o Foreign bank subsidiaries

**Foreign bank representative office:** such kind of office will carry out market research, advice, facilitate trade, financing and investment.

**Foreign bank branch:** it is a branch of foreign bank. This modality will help to import modern banking skills, technologies, products and services.

**Joint venture with local banks:** foreign banks buy shares of an existing and new established bank. This modality might not be effective in importing banking skills, specialized banking services and technologies.

According to the policy document approved by the council of ministers, foreign banks are allowed to acquire up to 30% stake in local banks with an additional 5% allowed each for foreign individuals and foreign non-bank investors. Hence, the maximum stake local banks can sell to foreigners is capped at

40%.

**Foreign Bank Subsidiaries:** will have a separate legal entity in the country. It is expected to bring banking expertise, specialized banking service and modern





banking technologies from developed economies and markets. It is also expected to bring foreign capital, foreign exchange into the economy in a sustainable manner.

### Foreign Banks in Other African Markets

Here below are the common practices in the neighboring Kenya.

**Representative Office:** Banks or financial institutions incorporated outside Kenya, duly authorized by Central Bank of Kenya (CBK), which transact banking or financial business offshore and are not permitted to conduct banking or financial business in Kenya. Nil capital requirement

**Foreign Branches of Banks:** Locally registered to undertake banking business but as a branch of its foreign parent entity. Does not have a local board of directors. Has assigned capital to its branch in line with CBK prudential guidelines. Example is Citibank NA Kenya which operates as a branch of Citi NY. Capital (assigned) requirement of Kes 1Bn (\$8.3Mln)

**Joint Venture/Subsidiaries:** Foreign bank or Financial institution with >50% foreign shareholding. Subsidiary is locally incorporated with a board of directors and meeting the CBK prudential guidelines. Examples include Standard Chartered, Absa Bank, Stanbic, Bank of India, Bank of Baroda, Bank of Africa, UBA, GT Bank, Access Bank, Ecobank, Dubai Int Bank etc. Capital requirement of Kes 1Bn (\$8.3Mln)

### Concluding Remarks

The Council of Ministers has passed a landmark decision to open the Ethiopian Banking Sector to foreign investors on September 2022.

The reform and opening of the Ethiopian banking sector present an immense opportunities for banks. The objectives of the policy include:

- o Increased credit supply
- o Increased foreign currency supply
  - o Enhanced banking skills and technologies, marketing know-how, and specialized products and services
  - o Enhanced competition, efficiency and dynamism in banking and financial system
- o Increased job opportunities

It is Infra Financials Research and Analytics team view that the major possible risks related to the entry of foreign banks are:

- o Contagion risk
- o Risks related to external financial and economic distress
- o Foreign banks leaving the market due to financial crises
- o Supervisory challenges

NBE will be expected to prepare/ amend the regulations, change the supervision and monitoring systems before the entry of foreign banks.

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- o **Foreign bank representative office:** such kind of office will carry out market research, advice, and facilitate trade, financing and investment.

If you would like to know more about the new opportunities in the Ethiopian banking sector, please contact Mahlet Gezahegn on [mahlet.g@infragroup.net](mailto:mahlet.g@infragroup.net).