

Addis Ababa University

College of Law and Governance Studies

School of Law

Regular Graduate Program

Master of Laws (LL.M.) in Public International Law

The Regulation of Foreign Currency under International Financial Law and its Relevance in Ethiopia

By: Fitsum Sitotaw (GSR/8718/14)

THESIS Submitted in Partial Fulfillment of the Requirements for the Degree of Master of Laws (LL.M.) in Public International Law at Addis Ababa University's School of Law, College of Law and Governance Studies

Advisor: Firemarkos Merso (Ph.D.)

July, 2023

Addis Ababa, Ethiopia

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Declaration of Originality

I, Fitsum Sitotaw, hereby affirm that the work included in this thesis is entirely my own creation and has never before been presented to this or any other institution in order to be considered for a degree, diploma, or other credentials. I finished it after enrolling in Addis Ababa University's LLM program for public international law.

I have reviewed the current research ethical policies of the University and the College and accept responsibility for carrying out the procedures in accordance with them. I tried to take into account any potential hazards or wrongdoings when conducting my research. I have also acknowledged my obligations, respected the rights of the participants, and secured the required ethical and/or safety permits.

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Acknowledgement

My appreciation goes out to my advisor, Dr. Fikremarkos Merso, for his timely feedback, comments and constructive criticism. I am also grateful to Dr. Tewodros Makonnen, Dr. Solomon Abay, Fikadu Petros, and Dr. Yared, who open-handedly provided their knowledge and expertise. Additionally, this endeavor would not have been possible without the generous support from my family and friends.

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Acronyms

BCBS - Basel Committee on Banking Supervision

CEO – Chief Executive Officer

DSB - Dispute Settlement Body

FSB - Financial Stability Board

GATT - General Agreement on Tariffs and Trade 1994

GTP II – Second Growth and Transformation Plan

IAIS - International Association of Insurance Supervisors

IASB - International Accounting Standards Board

IFAC - International Federation of Accountants

IMF – International Monetary Fund

IOSCO - International Organization of Securities Commissioners

NBE – National Bank of Ethiopia

SDR – Special Drawing Rights

SOFR – Secured Overnight Financing Rate

US – United Countries

USD – United Countries Dollar

WTO – World Trade Organization

Abstract

Foreign exchange restrictions are highly condemned by the international financial regime instituted by the International Monetary Fund (IMF). Member countries of the IMF are expected to uphold this obligation. Failure to adhere to this obligation may entail consequences from the IMF, individual countries, and other international actors. Ethiopia, as a member of the IMF, is a beneficiary of different arrangements by the IMF that stimulates the country's economy positively. However, measures against the IMF's Articles of Agreement are maintained and regularly introduced by "the National Bank of Ethiopia (the NBE)." Ethiopia claims that the measures to restrict foreign exchange emanate from balance of payment reasons and other social and economic goals. Overall, Ethiopia seems far behind in liberalizing the foreign exchange regime while the whole world is harmonizing with the IMF into an integrated foreign exchange scheme. This study assesses the different restrictions introduced by the NBE. It also shows how these measures do not conform with Ethiopia's international obligations and provide insight as to why reform in Ethiopia's forex regime is very much needed.

Key Terms: Financial Regulation, Foreign Currency, Foreign Exchange, the National Bank of Ethiopia, the International Monetary Fund, Ethiopia

Chapter One: Introduction

1.1. Research Background

“The Articles of Agreement” that formed the International Monetary Fund [hereinafter ‘the IMF’] was adopted on July 22, 1944 at the United Nations Monetary and Financial Conference.¹ The Articles of Agreement, under Article I sets out purposes of the IMF:

- I. To encourage permanent institutions to cooperate in international finance;
- II. To encourage and maintain high levels of employment and real income as well as the growth of the productive resources of all members, which are the major goals of economic policy; to facilitate the growth and stable development of international trade;
- III. To encourage exchange stability, uphold orderly member exchange agreements, and prevent competitive exchange depreciation;
- IV. To help remove foreign exchange restrictions that impede the expansion of global trade and to establish a multilateral system of payments for current transactions between members;
- V. To instill confidence in members by making the general resources of the IMF provisionally available to them; and
- VI. To shorten the duration and lessen the degree of disequilibrium in the international balances of payments of members.

With regard to these main purposes, the IMF assesses Countries' financial policies, as well as practices, to evaluate their conformity with IMF's Articles of Agreement and other IMF recommendations.

As stated above, the IMF was established with the goal of, among other things, assisting in the elimination of foreign exchange restrictions that impede the expansion of global trade.² The

¹ IMF, *Articles of Agreement of the International Monetary Fund* (United Nations Monetary and Financial Conference, Bretton Woods, New Hampshire 1944)., p. iii

² *Ibid.*, Article I (i-iv)

Agreement includes a clause that forbids any member Country from undermining another member Country's lawful currency.³

An assessment of the IMF's Executive Board⁴ in 2019 identified that four measures by the National Bank of Ethiopia [hereinafter 'NBE'] are not consistent with Section 2(a) of Article VIII of the Articles of Agreement. The measures identified to be inconsistent were:

- i. the allocation of foreign currency to debt repayment, invisibles, and certain imports of commodities and services;
- ii. limitations on the repayment of legitimate external debts and the creditors of foreign partners;
- iii. the requirement for tax certification for repatriating profits and other investment income, and
- iv. a clearance certificate from the NBE must be shown in order to secure import permits.⁵

The study mainly focuses on the first two measures identified above and other foreign exchange restrictions by the NBE as they directly relate to the NBE's foreign exchange regime. NBE regulates foreign exchange by the power vested to it by Article 20 of the National Bank of Ethiopia Establishment (as Amended) Proclamation No. 591/2008.⁶ In carrying out its mandates, the NBE has enacted numerous directives regulating foreign exchange. For instance, Article 4 and the following of the External Loan and Supplier's Credit (as Amended) Directive No. FXD/82/2022

³ IMF, *Articles of Agreement of the International Monetary Fund* (n 1), Article VIII (2) (b)

⁴ By using the authority granted to it by the Board of Governors, the Executive Board, chaired by the Managing Director, manages the day-to-day operations of the IMF. The Board of Governors is the IMF's policy-making body and it is in charge of approving all lending transactions. (see Margaret Garristen de Vries, *The International Monetary Fund*, vol II, p. 999 and International Monetary Fund (IMF), *International Monetary Fund Handbook: Its Functions, Policies and Operations* (2007), p. 72)

⁵ IMF, '2019 Article IV Consultation and Requests for Three-Year Arrangement under the Extended Credit Facility and an Arrangement under the Extended Fund Facility—Press Release and Staff Report' (2018) IMF Country Report No. 20/29, p. 19.

⁶ "The National Bank of Ethiopia Establishment (as Amended) Proclamation, 2008, Proclamation No. 591/2008, Federal Negarit Gazette, Year 14, No. 50, Addis Ababa, Ethiopia."

imposes different requirements as to how to access external loans. This, however, is in violation of Article VIII, Section 2(a), of the IMF's Articles of Agreement, according to the IMF.

The IMF also noted that it was in violation of its Articles of Agreement when it prioritized and limited foreign currency to certain imports. The NBE still maintains the prioritization of some import goods over others in allocating foreign currencies as per Article 6 of the Transparency in Foreign Currency Allocation and Foreign Exchange Management (as Amended) Directive No. FXD/77/2021.

While this inconformity subsists in Ethiopia, the foreign exchange regulation regime is prone to different criticism. A crisis with hard currency exists as there is a foreign currency shortage⁷ as well as a heavily criticized exchange rate policy in the country. The IMF, as part of its mandate to stabilize foreign exchange rates, recommends adopting a more flexible exchange rate policy that responds to movements in the hard currencies and actual inflation.⁸ Hence, these policies and measures by the NBE seem to disregard Ethiopia's international obligations.

According to the NBE, the current account balance of Ethiopia is USD 1.6 billion, and the capital account is recorded at USD 558.6 million as of the start of 2023.⁹ The overall balance of payment (reserve) by the start of 2023 has shown a deficit of USD 114.3 million.¹⁰ The international reserves of Ethiopia were around USD 2.8 Billion, including gold reserves in the fourth quarter of 2021/22.¹¹ For the same quarter, the world's foreign exchange reserves were around USD 11.5 Trillion¹², which means Ethiopia's share of the world's international reserves is approximately

⁷ Fasika Tadesse and Simon Marks, 'Dollar Squeeze, Accelerating Inflation Pummel Ethiopian Currency' (*Bloomberg*, 9 June 2022) <<https://www.bloomberg.com/news/articles/2022-06-09/dollar-squeeze-accelerating-inflation-pummel-ethiopian-currency>> accessed 21 September 2022.

⁸ Rupa Duttagupta, Gilda Fernandez and Cem Karacadag, *Moving to a Flexible Exchange Rate: How, When, and How Fast?* (International Monetary Fund 2005) 6–8.

⁹ National Bank of Ethiopia, 'Quarterly Bulletin: First Quarter 2022/2023' (NBE 2023) Vol. 39, No. 1 62.

¹⁰ *ibid* 63.

¹¹ National Bank of Ethiopia, 'Quarterly Bulletin: Fourth Quarter 2021/2022' (NBE 2022) Vol. 38, No. 4., p. 92

¹² "International Monetary Fund (IMF), 'Currency Composition of Official Foreign Exchange Reserves (COFER)' (*IMF Data*, 23 December 2022)" <<https://data.imf.org/?sk=E6A5F467-C14B-4AA8-9F6D-5A09EC4E62A4>>.

0.024%. To prevent Ethiopia's economy from imploding owing to a lack of foreign currency, the World Bank, the European Union, the IMF, and other donors and lenders cover Ethiopia's foreign exchange deficit.¹³ Ethiopia might quickly turn into a hard currency illiquid economy that cannot pay for its imports or pay its obligations in hard currency without assistance from outside and remittances from the diaspora.¹⁴

Although several legal reforms were conducted frequently by the NBE, nonconformity exists between Ethiopia's foreign exchange and "Sections 2(a), 3, and 4 of Article VIII of Articles of Agreement."¹⁵ For instance, Ethiopia, under the Homegrown Economic Reform policy, declared that it will make "efforts to institute a mechanism where there are no controls on current account transactions (e.g. imports) and the value of the exchange rate reflects market fundamentals."¹⁶ According to this policy instrument and its revised second version which is set to be tabled for approval, the Ministry of Finance and the Ministry of Planning and Development put in place some reforms to liberalize the foreign exchange regulation regime. Unfortunately, this study is finalized before even the first draft of the Homegrown Economic Reform Policy II is out for public consultation.

1.2. Statement of the Problem

International financial regulation controls foreign currency operations. Particularly the IMF's Articles of Agreement articulates how countries should promote exchange stability and maintain

¹³ Beakal Tafesse, 'The Impact of Currency Devaluation on Economic Growth: Its Benefits and Costs on Ethiopian Economy' (Unpublished, St Mary's University, School of Graduate Studies, Department of General MBA 2019)., p. 9

¹⁴ *ibid.*

¹⁵ IMF, 'Staff Report for the 2017 Article IV Consultation—Press Release; Staff Report; and Statement by the Executive Director for the Federal Democratic Republic of Ethiopia' (2018) IMF Country Report No. 18/18, p. 17.

¹⁶ Federal Democratic Republic of Ethiopia, *A Homegrown Economic Reform Agenda: A Pathway to Prosperity* (2020).

orderly exchange arrangements. Ethiopia, as a member of the IMF and as a country in the process of acceding to the WTO, needs to conform to these laws regarding the regulation of foreign currency. Although the IMF has issued annual reports with recommendations for Ethiopia to conform its Articles of Agreement, there is a lack of research concerning this topic.

As elaborated in the above section, the allocation of foreign currency to debt repayment, invisibles, and certain imports of commodities and services, limitations on the repayment of legitimate external debts and the creditors of foreign partners, the requirement for tax certification for repatriating profits and other investment income, and a clearance certificate from the NBE must be shown in order to secure import permits were identified as measures taken by the NBE against Article VIII, Section 2(a) of the IMF's Articles of Association. However, a concrete explanation as to why the NBE resorted to these measures cannot be found easily. The implication of these measures and the extent of legality in the sense of international financial regulation are not defined clearly.

If Ethiopia decides to revise the aforementioned measures and conform with the IMF's Articles of Association, there will be financial and economical implications to such revisions. For a country that is experiencing a shortage of foreign currency and has a poor economy, measures of this magnitude need to be examined thoroughly. Evaluating Ethiopia's duty to comply with international financial regulation on one hand, and the importance of robust foreign currency regulation on the other is important and needs to be addressed. To this end, the research will assess the impact of international financial regulation on Ethiopia and it will appraise the conformity of Ethiopian laws and policies with international financial regulations.

1.3. Objectives of the Study

The general objective of the study is to investigate whether or not international financial regulations and Ethiopian financial laws are harmonious with a particular focus on the regulation of foreign currency.

With that in mind, the study has the following specific objectives:

- ✓ to highlight the importance and relevance of international financial regulation for the regulation of foreign currency at the national and international levels;

- ✓ to understand the standing of Ethiopian financial laws on foreign currency in comparison to international financial regulations; and
- ✓ to recommend ways to harmonize Ethiopian financial law on foreign currency with international financial regulations.

1.4. Research Questions

The core questions addressed by this study are: “What is the relevance of international financial regulation in Ethiopia with regard to foreign currency regulation?” and “Are Ethiopia’s forex regulations in conformity with international financial regulation?”

In doing so, the study addresses the following specific research questions:

- a) How is foreign currency regulated under international financial regulation?
- b) How is foreign currency regulated under Ethiopian financial laws?
- c) Are Ethiopian financial laws on foreign currency in conformity with international financial regulations?
- d) Which measures of the NBE could be regarded as foreign currency restrictions as per Article VIII of the IMF’s Articles of Agreement?
- e) Is there a need to reform Ethiopia’s foreign currency regulation mechanism to conform with international financial regulation?

1.5. Significance of the Study

This study exhibits different argumentative points from different perspectives. It observes the importance of regulating foreign currency at the national level as well as the importance of adhering to international financial regulations. It raises a critical issue that has affected Ethiopia’s economy from an international law point of view. It has significance in evaluating Ethiopia’s duty to comply with international financial regulation on one hand, and the importance of robust foreign currency regulation on the other.

From international financial law advocates’ point of view, the research gives a comprehensive explanation as to why Ethiopia resorts to measures that are contradictory to international financial regulation. The study also identifies the different challenges that Ethiopia may face in trying to conform with international financial regulations. This is important for future researchers and

policymakers to navigate through Ethiopian and international financial regulations on foreign exchange since there is a dearth of research on this particular issue.

1.6. Scope of the Study

The study principally focuses on Ethiopian financial law on foreign currency. It is limited to assessing Ethiopian laws, regulations, and directives affecting foreign currency as well as the relevant rules of the IMF.

1.7. Research Methods

1.7.1. Method of Analysis and Type of Research

The research will use a qualitative research method. The qualitative methods to be used in the research are legal rule analysis and analysis of practice. Domestic and international financial laws will be analyzed to demonstrate whether they are in harmony or contradictory.

1.7.2. Sources of Data

The main data sources for the research are primary sources. These include legal texts, primarily, the IMF's Agreement of Articles, international legal texts, the National Bank of Ethiopia Establishment Proclamation, and different NBE Directives on foreign currency. Moreover, semi-structured interviews with officers from the NBE and an economic advisor to the Governor of the NBE have been conducted.

Supplementary data is also used from secondary sources such as literatures, commentaries on statutes, and reports from the NBE, the IMF, and other institutions.

1.7.3. Methods of Legal Interpretation

Legal texts, where necessary, were interpreted as per Article 31 of the Vienna Convention on the Law of Treaties (1969). Textual, systematic, purposive, and historical interpretative methods were deployed in the study to critically analyze both international and national laws.

1.8. Referencing and Citation Style

The study uses footnotes to acknowledge others' work within the text or to further explain concepts raised in the text. For referencing, OSCOLA referencing style is used throughout the study. The citation rules of Addis Ababa University, School of Law, and Journal of Ethiopian Law are used

for citing domestic laws. Zotero software was used to track, document, and generate citations for every literature work.

1.9. Organization of the Study

This study is structured into five chapters. Accordingly, the first chapter is an introductory part consisting of the contents of this proposal. Chapter two gives an overview of the essence of regulation of foreign currency from an international financial law perspective. Chapter three explains the international and Ethiopian foreign currency regulation frameworks. The fourth chapter analyzes the relevance of international laws on the regulation of foreign currency in relation to Ethiopia and compliance of Ethiopia with the IMF's legal framework. Finally, the last and fifth chapter provides concluding remarks and offer recommendations as to what needs to be done in order to address the problems identified in the study.

Chapter Two: Overview of the Essence of International Financial Regulation and Foreign Currency Regulation

2.1. International Financial Regulations

The foundations of international economic law are laws of international finance and trade. Trade and finance are both essential domains of international economic law, and the laws that govern both have significant implications for global markets and market stakeholders. With this in mind, the focus of this study lies only on one of the two pillars of international economic law, which is international financial law.

Since both financial regulation and financial law could be considered “law,” the terminology difference between the two is unclear. Financial law is concerned with whether a party can legally enforce a claim that was formed through a contract, or some form of financial transaction.¹⁷ In contrast, financial regulation aims to support societal objectives like consumer protection or stability by enabling country authorities to regulate the conduct of market actors.¹⁸ As a result, behavioral rules in the form of orders and restrictions form the basis of financial regulation. For instance, financial regulation may require countries to arrange their accounts in a certain way, and establish and maintain a minimum level of liquidity reserves.

Financial law and regulation are very different in terms of the repercussions of non-compliance. For domestic jurisdictions, financial laws entail more repercussions than financial regulations. In this sense, regulation refers to a more vertical relationship between the country and its market participants, one that is defined by subordination, as opposed to financial law, which deals with the horizontal relationship between market part actors.¹⁹ The dichotomy between public law and private or commercial law refers to essentially the same duality in numerous jurisdictions. Therefore, financial regulation, either international or domestic, falls under the public law category.

¹⁷ Philipp Paech, *International Financial Law* (LSE Department of Law 2018), p.3

¹⁸ *ibid.*

¹⁹ *ibid.*

2.1.1. Purpose of International Financial Regulation

According to the International Center for Monetary and Banking Studies (ICMB), traditional economic theory suggests that there are three main purposes of financial regulation. These are:

- a) to prevent major distortions of competition and to maintain market integrity by restricting the exercise of monopolistic power;
- b) to protect ordinary people's basic requirements in situations where knowledge is difficult or expensive to obtain and mistakes could harm wellbeing; and
- c) in cases where there are enough externalities that the overall social costs of market failure outweigh both the individual costs of failure and the additional costs of regulation.²⁰

While the above three purposes remain relevant for both international and domestic financial regulation, it can be further explained that international financial regulatory initiatives serve at least two major functions.

Communication is the first and typically the most important function. This entails sharing best practice information with other countries. It is a means of assisting countries in learning from the accomplishments and shortcomings of other regulatory endeavors. This is done in an effort to establish regulatory schemes more suitable for developing jurisdictions.²¹ It is a teaching exercise rather than a compliance exercise.

The second function of international financial regulation, which has grown significantly more prominent since the 2007-08 financial crisis, is to encourage governments to rein in international externalities caused by actors in their financial systems.²² Hence, the importance of financial regulation at the international and domestic levels will protect countries as an entity and ordinary people as finance affects everyone's activities.

²⁰ International Center for Monetary and Banking Studies (ICMB), 'The Fundamental Principles of Financial Regulation' (2009) Geneva Reports on the World Economy 11., pp. 1-2

²¹ John Armour and Daniel Awrey, *Prioritising the Implementation of International Financial Regulation* (Commonwealth Secretariat 2015), p. 14

²² *ibid.*

2.1.2. Soft Law Vs. Hard Law Nature of International Financial Regulation

Since the 2008 Financial Crisis, efforts to regulate the global financial system have attained significant advances. Global regulators have collaborated to create a set of institutional and legislative reforms to rebuild the financial system and address the critical flaws that the 2008 financial crash highlighted, guided by the Pittsburgh Declaration.²³ The Financial Stability Board (FSB)²⁴, the Basel Committee on Banking Supervision (BCBS)²⁵, and the International Organization of Securities Commissioners (IOSCO)²⁶ are examples of reformist institutions that

²³ The Pittsburgh Declaration is an official statement by G20 States after the 2009 G20 Pittsburgh Summit. It was the third meeting of the G20 heads of state and/or heads of government to discuss financial markets and the world economy. According to the Preamble of The Leaders' Statement, the Pittsburgh Summit, (September 24 – 25 2009), the declaration was necessary to make sure our regulatory system for banks and other financial firms reins in the excesses that led to the crisis.

²⁴ The Financial Stability Board (FSB) is an international organization that oversees and provides recommendations for the world financial system. It was founded in April 2009 to replace the Financial Stability Forum (FSF). The FSB works to advance global financial stability by collaborating with national financial regulators and international standard-setting organizations to create effective regulatory, supervisory, and other financial sector policies. See: FSB, 'About FSB' (*Official Website of FSB*) <<https://www.fsb.org/about/>> accessed 12 May 2023.

²⁵ The Basel Committee on Banking Supervision (BCBS) is an international committee that was established to define banking regulatory standards. It has 45 members as of 2022 and is composed of central banks and other banking regulatory bodies from 28 different countries. The Basel Accords, significant policy suggestions, are part of the BCBS. See: BCBS, 'About BCBS' (*Official Website of BCBS*) "<<https://www.bis.org/bcbs/index.htm>>" accessed 12 May 2023.

²⁶ The International Organization of Securities Commissions (IOSCO) is a supranational organization that serves as the global standard-setter for the securities industry. Its members govern over 95% of the world's securities markets in over 130 jurisdictions. IOSCO develops, implements, and encourages compliance with internationally recognized securities regulation standards. It collaborates closely with the G20 and the Financial Stability Board (FSB) on global regulatory reform. See: IOSCO, 'About IOSCO' (*Official Website of IOSCO*) <https://iosco.org/about/?subsection=about_iosco> accessed 12 May 2023.

have developed specific standards to be incorporated into the national legal frameworks of countries.²⁷

The fact that the international efforts for financial regulation are informal, non-binding systems that depend on extralegal processes for enforcement, like peer review, disclosure, and reputation, makes them stand out as soft law.²⁸

By evaluating national regulatory systems in order to assess their compliance with accepted international norms, the IMF and the World Bank have strengthened these initiatives. The IMF and the World Bank have given the generally soft character of international financial regulation a hard edge through the implementation of their own standards and regulations in conjunction with this informal framework of global legislative institutions (like the BCBS). Domestic financial systems all over the world have undergone an extensive transformation, which is a testament to the effectiveness of this framework.²⁹

In international initiatives where the issue is rapidly evolving, soft law is widely employed as a means of progressing rather than formal or common treaties. It enables greater responsiveness than would be possible if a treaty was to be renegotiated by allowing rule production to be delegated to a specialized organization.³⁰

The requirements of membership in other international organizations to which countries join, or the conditions connected to financing, may include compliance with international financial regulatory standards. Then, non-compliance may entail immediate financial consequences. The IMF, in its part, undertakes assessments of member countries' compliance under various guises.³¹ This is the most glaring example of this type of incentive. Each member country commits to working together to ensure orderly exchange arrangements and advance stable exchange rates

²⁷ Yesha Yadav, 'Fintech and International Financial Regulation' (2020) 53 *Vanderbilt Journal of Transnational Law.*, pp. 1115-1116

²⁸ Armour and Awrey (n 21), p. 8

²⁹ Yadav (n 27).

³⁰ AT Guzman and TL Meyer, 'International Soft Law' (2010) 2 *Journal of Legal Analysis* 171., pp. 197-201

³¹ Armour and Awrey (n 21), p. 9

pursuant to Article IV of the IMF's Articles of Agreement. The IMF regularly conducts Article IV consultations, in which technical specialists visit a member country to assess economic and financial trends and to evaluate progress.

In principle, failure to adhere to obligations under the IMF's Articles of Agreement, including Article VIII, can subject a member country to escalating denial of membership benefits, including initial ineligibility from using the IMF's resources, followed by denial of voting rights and, in worst-case scenario, complete removal from membership.³²

Compliance with international financial standards may also be included as criteria in the terms of IMF loans, even though no enforcement action has ever been launched under the IMF's Articles of Association.³³ In this case, the IMF's surveillance serves as a proxy for creditor oversight. Borrowers will face the repercussions associated with a breach of the condition specified in the relevant loan documentation if they fail to achieve these criteria.

Despite the fact that they can act as observers of regulatory action, the IMF and World Bank do not typically develop regulatory standards. Additionally, the General Agreement on Trade and Services (GATS), the only agreement made by the World Trade Organization (WTO) that pertains to financial services, is not of a prudential nature.³⁴ Similar to trade agreements, it focuses on how national authorities should handle foreign investment instead and establishes the boundaries of regulatory authority rather than coordinating particular regulatory measures.

Therefore, it can be concluded saying that international financial regulation stands out as soft law. This means that it is not legally binding, but rather based on voluntary compliance and cooperation among different actors. Soft law can be seen as a flexible and pragmatic approach to addressing the complex and dynamic challenges of the global financial system. However, soft law also has some limitations, such as a lack of enforcement, accountability, and legitimacy. Thus, it is

³² "IMF, *Articles of Agreement of the International Monetary Fund*" (n 1), Art. 26

³³ Armour and Awrey (n 21), p. 9

³⁴ Chris Brummer, 'Why Soft Law Dominates International Finance - And Not Trade' (2010) 13 *Journal of International Economic Law* 623., p. 627

important to balance the benefits and drawbacks of soft law in international financial regulation and to explore ways to enhance its effectiveness and responsiveness.

The fact that international financial regulation stands out as a soft law could suggest that it cannot be regarded as a 'regulation' to begin with. However, international financial regulation has a distinct type of cross-border cooperation that is strengthened by reputational, market, and institutional processes. It is therefore more coercive than what is predicted by traditional theories of international law.³⁵ A regulator's track record of adhering to international norms can have an impact on its reputation, which will then have an impact on its capacity to forge coalitions and alliances in the future.³⁶ It has been urged and recommended for the creation of a moderate regulatory reform plan that shuns more extreme (and unrealistic) calls for a global financial regulator and instead seeks to use transparency in ways that more forcefully compel national authorities.³⁷

2.1.3. Institutional Framework for International Financial Regulation

International financial regulation is the result of a regulatory division, in which authorities from a variety of national and foreign institutions collaborate to establish international guidelines and norms.³⁸ Hence, international financial regulation heavily depends on the efficiency and power of regulatory institutions.

Rulemaking and participation in international institutions that create standards are the responsibilities of national regulators. International standard-setting bodies act as inter-agency forums. Their members, which are national regulators, manage them by cooperation, and they are in charge of putting their legislative output into practice. Meanwhile, the main actors responsible

³⁵ Chris Brummer, 'How International Financial Law Works (and How It Doesn't)' (2011) 99 *The Georgetown Law Journal* 1 <<http://ssrn.com/abstract=1542829>>.

³⁶ Chris Brummer, 'A Compliance-Based Theory of International Financial Law', *Soft Law and the Global Financial System: Rule Making in the 21st Century* (Cambridge University Press 2015).

³⁷ Brummer, 'How International Financial Law Works (and How It Doesn't)' (n 35).

³⁸ Benedict Kingsbury, Nico Krisch and Richard Stewart, *The Emergence of Global Administrative Law* (2005), pp. 15-29

for ensuring that countries are following international norms and best practices are international financial institutions.³⁹

The majority of sources of international financial regulation are informal, intergovernmental institutions that define agendas and standards for the international regulatory system. These institutions typically operate in accordance with consensus and non-binding bylaws rather than being anchored by treaties. The Group of 20 (G-20)⁴⁰, in which heads of countries engage directly, as well as the Financial Stability Board, which is in charge of overseeing systemic risk, are probably the two most well-known of these organizations.⁴¹ “The International Organization of Securities Commissions (IOSCO)”⁴², “the International Association of Insurance Supervisors (IAIS)”⁴³, and “the Basel Committee on Banking Supervision (BCBS)”⁴⁴ and are additional significant organizations that are in charge of establishing global standards for banking, securities regulation, and insurance.⁴⁵

Other significant standard-setting institutions that focus on extremely particular financial subfields and have far more constrained mandates exist alongside these core regulators. “The International

³⁹ Brummer, ‘How International Financial Law Works (and How It Doesn’t)’ (n 35)., p. 273

⁴⁰ The Group of Twenty (G20) is an intergovernmental forum consisting of 19 countries (Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Republic of Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkey, the United Kingdom, and the United States) and the European Union. See: G20, *G20 – Background Brief* (2023) <https://www.g20.org/content/dam/gtwenty/gtwenty_new/about_g20/G20_Background_Brief.pdf> accessed 12 May 2023.

⁴¹ Brummer, (n 34)., p. 628

⁴² About IOSCO (n 26).

⁴³ Since its founding in 1994, the International Association of Insurance Supervisors (IAIS) has served as the body responsible for developing and assisting in the implementation of global standards, guidelines, and supporting documentation for the regulation of the insurance industry. 97% of the world's insurance premiums are represented by this voluntary membership organization comprising insurance supervisors from more than 200 jurisdictions. See: IAIS, ‘About IAIS’ (*Official Website of IAIS*) <<https://www.iaisweb.org/about-the-iais/>> accessed 12 May 2023.

⁴⁴ About BCBS (n 25).

⁴⁵ Brummer, (n 34).

Federation of Accountants (IFAC)”⁴⁶, in conjunction with “the International Accounting Standards Board (IASB)”⁴⁷, among others, promulgates international standards on how specific types of transactions and other events should be reflected in financial statements.⁴⁸

The final significant group of international regulatory actors consists of organizations that conduct surveillance and monitoring. Although other organizations occasionally conduct isolated monitoring tasks, the IMF and the World Bank have historically significant roles.⁴⁹ Notably, they are the only international organizations in the global financial architecture whose founding agreements, or Articles of Agreement, have been explicitly recognized as binding legal precedents.⁵⁰

Particularly flagrant violations of international standards may result in fines from international organizations as well as financial institutions, in addition to reputational and commercial losses. The IMF and World Bank have extensive latitude in deciding whether to make adherence to international standards a requirement for receiving loans because they serve as both monitors and suppliers of development assistance in addition to serving as lenders of last resort.⁵¹

⁴⁶ The IFAC was established on October 7, 1977, at the 11th World Congress of Accountants in Munich, Germany, to promote the worldwide accounting profession in the public interest. 63 professional accounting bodies were among IFAC's original members. See: IFAC, ‘About IFAC’ (*Official Website of IFAC*) <<https://www.ifac.org/who-we-are/our-purpose>> accessed 12 May 2023.

⁴⁷ The IFRS Foundation is a nonprofit, public interest organization created to create the IFRS Standards, high-quality, easily understood, enforceable, and globally accepted accounting and sustainability disclosure guidelines, and to encourage and support their use. See: IFRS, ‘About IFRS’ (*Official Website of IFRS*) <<https://www.ifrs.org/about-us/who-we-are/>> accessed 12 May 2023.

⁴⁸ Brummer, (n 34).

⁴⁹ Michael Blair and George Walker, *Financial Markets and Exchanges Law* (2007), p. 462

⁵⁰ Brummer, ‘How International Financial Law Works (and How It Doesn’t)’ (n 35), p. 280

⁵¹ Kern Alexander, Rahul Dhumale and John Eatwell, *Global Governance of Financial Systems: The International Regulation of Systemic Risk* (2006), p. 89

2.1.3.1. The International Monetary Fund (IMF)

Founded in 1945, the IMF is a specialized organization of the UN⁵² that is run by its 190 member countries. It was founded along with the World Bank as part of the Bretton Woods conference convened in the aftermath of World War II.⁵³ The macroeconomic, or general economy, performance, and financial sector policies are the IMF's primary areas of focus.⁵⁴ The IMF has a Board of Governors, an Executive Board, and a Managing Director. The Board of Governors is the IMF's highest policy-making body, and each member country appoints one Governor and one alternate to serve on it. The Board of Governors typically convenes once a year and is made up of officials of comparable rank, such as ministers of finance or presidents of central banks.⁵⁵

The IMF's Board of Governors has the highest level of policymaking power. Every member country has a representative on the Board of Governors, particularly at the level of the finance minister or head of the central bank. The IMF Governors meet annually. The International Monetary and Financial Committee (IMFC), a committee of the Governors, holds twice-yearly meetings to discuss significant policy matters impacting the global monetary system and to provide recommendations to the full Board of Governors. The Board of Executive Directors, a 24-member body that convenes three or more times per week to manage and oversee the activities of the IMF, has daily power over operational policy, lending, and other issues. The IMF's Managing Director,

⁵² International Monetary Fund (IMF) and James Boughton, *Tearing Down Walls: The International Monetary Fund 1990-1999* (International Monetary Fund 2012), pp.3-34

⁵³ International Monetary Fund (IMF), *Financial Organization and Operations of the IMF* (International Monetary Fund 2010), p.1

⁵⁴ IMF, (n 1), Preamble

⁵⁵ International Monetary Fund (IMF), *Financial Organization and Operations of the IMF* (n 53), p. 4

who acts as both a Chairman and a CEO, is appointed by the IMF Executive Board to serve a five-year renewable tenure and always by member European Countries.^{56,57}

Here, it is important to note that many people mistake the IMF for the World Bank (the International Bank for Reconstruction and Development).⁵⁸ The World Bank was established to support long-term infrastructural development, such as investments in education, health, public administration, agriculture, and environmental and natural resource management, even though its work complements that of the IMF.⁵⁹ In contrast, the IMF helps its members deal with short-term balance of payments issues rather than supporting specific industries.⁶⁰

The IMF's mandate is derived from its Articles of Agreement, which is an international treaty that balances member countries' varied views on the objectives and authority of a supranational organization as well as their opinions on related obligations.⁶¹

The power granted to the IMF by Article I of the Articles of Agreement may fall into three categories: (a) oversight powers, (b) the power to grant financial assistance; and (c) advisory powers. From these, IMF's mandate for systemic surveillance (oversight powers) stands out in this research.

The mandate for systemic surveillance (oversight powers): Multilateral surveillance has its roots in Article IV, Section 3(a) of the IMF's Articles of Agreement, which calls on the IMF to "oversee the international monetary system in order to ensure its effective operation."

⁵⁶ International Monetary Fund (IMF), *International Monetary Fund Handbook: Its Functions, Policies and Operations* (n 4) 2–6.

⁵⁷ International Monetary Fund (IMF), *Financial Organization and Operations of the IMF* (n 53) 10–12.

⁵⁸ International Monetary Fund (IMF) and Boughton (n 52).

⁵⁹ *ibid.*

⁶⁰ IMF, (n 1).

⁶¹ International Monetary Fund (IMF), 'The Fund's Mandate: An Overview' (Strategy, Policy, and Review Department of the IMF in Consultation with the Legal Department of the IMF 2010) "<<http://www.imf.org/external/np/pp/eng/2010/012210a.pdf>>" accessed 24 January 2023., para. 3

In principle, the IMF's surveillance includes both the evaluation of economic policies in member Countries (bilateral surveillance) and systemic developments (multilateral surveillance, primarily in the form of the World Economic Outlook (WEO), the Global Financial Stability Report (GFSR), and the Early Warning Exercise (EWE)).⁶² However, there are no concrete legal duties placed on the members, and the IMF's authority is only limited to the international financial and monetary system.⁶³ This notion is distinct from the international financial system since it only refers to official agreements concerning the balance of payments, such as exchange rates, reserves, and rules governing current payments and capital flows. Despite being a legitimate target of regulation, the financial sector is a second-order activity because of its potential influence on the stability of the international financial system.⁶⁴

According to Article IV, Section 3 (b) of the Articles of Agreement, the IMF shall exercise strict oversight over the exchange rate policies of members in order to carry out its obligations and shall adopt specific guidelines for the guidance of all members concerning those policies. The information required for such surveillance shall be provided by each member, and upon request, each member must engage with the IMF regarding its exchange rate policies. The IMF's principles shall be compatible with cooperative agreements that allow members to preserve the value of their own currencies relative to the value of the currency or currencies of other members, as well as other exchange arrangements that a member chooses that are in line with the objectives of the IMF.⁶⁵

The IMF has consistently used bilateral surveillance, which focuses on domestic and exchange rate policy, as the basis for its research and has supported many of its multilateral outputs. Bilateral surveillance offers members a global perspective on their domestic policies, a feature that member Countries appreciate most.⁶⁶ With this particular power to conduct bilateral and multilateral

⁶² *ibid.*, para. 6

⁶³ *ibid.*, para. 7

⁶⁴ *ibid.*

⁶⁵ IMF, (n 1)., Article IV, Section 3 (b)

⁶⁶ International Monetary Fund (IMF), 'The Fund's Mandate: An Overview' (n 61)., para. 13

surveillance, the IMF has the mandate over the regulation of international finance and foreign exchange schemes.

Chapter Three: Comparison of the International and Ethiopian Foreign Currency Regulation Frameworks

3.1. International Foreign Currency Regulation Frameworks

Foreign currency is regulated by countries through currency restrictions and currency control. The system of international settlements used by actors in an international economic transaction is regulated by each country when it comes to currency. Foreign currency regulation establishes, among other things, the scope and procedure for carrying out foreign exchange transactions, creating and using the country's currency reserve, creating and using the currency funds of economic entities, and carrying out currency management.

Regulating international payments and capital transfers, repatriation of export earnings, profits, notes, and securities, and the limitation on the free sale of foreign currencies are the most common types of foreign exchange restrictions that countries use to set a mechanism for carrying out operations with currency values.⁶⁷ These measures by countries, at the international level, are regulated through international legal and institutional frameworks in place.

3.1.1. International Legal Framework for Foreign Currency Regulation

Foreign exchange is a critical factor in any economy. It influences the cost of imported goods as well as the profitability of export sectors, thereby driving the rate of inflation, output, employment,

⁶⁷ Bohdan Stetsiuk, Oleksandr Slyvka and Oleksandr Bashynskyi, 'The Legal Framework for the Implementation of Currency Regulation in Some Foreign Countries and in Ukraine' (2018) 4 *Baltic Journal of Economic Studies* <DOI: <https://doi.org/10.30525/2256-0742/2018-4-1-358-365>>., p. 359

and other economic subject matters. The decision on exchange arrangement might also affect how much a country's economy is impacted by economic booms and recessions internationally and establishes the parameters for the autonomy of domestic monetary policy. Therefore, it is expected that foreign exchange regulation is a contentious topic and has become even more so in recent years as real-world concerns could surface.

Narrowly defined, foreign exchange regulation may pertain to how the domestic currency price of a foreign currency is established. This shouldn't be viewed as an exclusion from other macroeconomic policy measures. The international financial and monetary system was built on par values from the time the IMF was founded until 1973.⁶⁸ With a few notable exceptions, member countries continued to peg their national currencies to the US dollar or straight to gold.⁶⁹

Nonetheless, individual countries are free to peg their currencies to any other currency or basket of currencies, such as the Special Drawing Right (SDR) of the IMF, or to enable the exchange rate to fluctuate in accordance with market forces or another type of adjustment scheme.⁷⁰ The Second Amendment to the IMF's Articles, adopted in 1978, officially approved the freedom of IMF members to determine their exchange arrangement.⁷¹ The revised Articles also stressed that in order to maintain a stable exchange rate system, member countries must focus their economic and financial policies on promoting orderly fundamental economic conditions, orderly economic growth, and reasonable price stability.

Article VIII of the Articles of Agreement

Subject to certain exceptions, Article VIII, Section 2(a) prohibits members from enacting exchange restrictions, also known as "restrictions on the making of payments and transfers for current international transactions." The test for whether a measure falls under Article VIII, Section 2(a)'s

⁶⁸ David Burton and Martin G Gilman, 'Exchange Rate Policy and the IMF', *Finance and Development* (International Monetary Fund 1991) 19.

⁶⁹ *ibid* 18.

⁷⁰ *ibid*.

⁷¹ *ibid*.

definition of an exchange restriction is identifying whether a measure entails a straight governmental constraint on both availability and transferability of forex. When a member country limits the ability to transfer or make payments for current foreign transactions or makes them subject to "undue delays," this constitutes an exchange restriction. Article XXX (d) defines payments for current operations as "payments which are not for the purpose of transferring capital." This includes current account payments such as those for trade, services, interest, and income. It also includes things that, from an economic standpoint, are capital in character such as payments for the amortization of loans or the depreciation of direct investments.

As previously mentioned, with few exclusions, members are not permitted to participate in discriminatory exchange arrangements under Article VIII, Section 3 of the IMF's Articles of Agreement. Accordingly, the IMF made the decision that official action shouldn't produce foreign exchange disparities and cross-rate quotations that deviate excessively.⁷² A country could be in violation of the Articles of Agreement and susceptible to face sanctions by the IMF through Article XXVI if it implements exchange measures that are inconsistent with its obligations under Article VIII. These penalties include being declared ineligible to access the IMF's different resources, having different rights suspended, and being forced to withdraw.⁷³

In order for a member to implement exchange measures complying with Article VIII, there are two important requirements that must be met. (1) The measures must be authorized by the IMF; (2) they must be maintained in accordance with Article XIV, Section 2 of the Articles of Agreement. Furthermore, the terms of Article VIII, Section 2(a), which permit the Fund to designate a member's currency to be "scarce," are subject to the clauses of Article VII, Section 3.

Under Article VIII, exchange restrictions may be legally applied with the IMF's prior approval. Exchange measures are typically approved by an Executive Board decision if it is convinced that such measures are: (1) implemented for balance of payments purposes, (2) implemented in a way

⁷² Certain requirements with regard to the convertibility of officially maintained balances are outlined in Article VIII, Section 4. Since interbank foreign currency markets have grown, these requirements currently have little operational significance.

⁷³ IMF, *Articles of Agreement of the International Monetary Fund* (n 1) Article XXVI .

that does not discriminate between IMF members, and (3) is provisional in the sense that there is a clear timeline for its elimination.⁷⁴ A predetermined time frame is given for approval. For limitations put in place for security purposes, a different process is used.⁷⁵

Under Article XIV, Section 2, a member could maintain a restrictive exchange measure. A member country may use Article XIV, Section 2 as a transitional provision upon entering the IMF. This clause enables a member country to continue using the exchange measures in place as of the date of membership while also adapting them to changing conditions without obtaining IMF's permission. However, members are required to introduce new measures subject to Article VIII . Even then, such measures could only be implemented upon the IMF's permission, even for member countries that utilize Article XIV, Section 2 as a transitional provision.⁷⁶

A member country may officially inform the IMF that it accepts Article VIII obligations in accordance with the IMF's Articles. Such formal notice carries with it some legal ramifications. It is not essential for a member country to formally accept the obligations set forth in Article VIII, Sections 2, 3, and 4 once it joins the IMF. That member country cannot then depend on Section 2 of Article XIV to preserve or modify the restrictive measures once it joins the IMF. This is the only legal repercussion of a member notifying the other parties of their acceptance of Article VIII obligations.

The distinction between accepting Article VIII duties and maintaining a non-restrictive exchange system is crucial. There are some instances where member countries informed that they accepted

⁷⁴ 'Discrimination for Balance of Payments Reasons', , *Decision No. 955-(59/45)* (1959); International Monetary Fund (IMF), 'Payments Arrears', *Decision No. 3153-(70/95)* (1970); IMF, 'Policy on Multiple Currency Practices', *Decision No. 6790-(81/43)* (1981); "IMF, 'Article VIII and Article XIV', *Decision No. 1034-(60/27)*" (1960).

⁷⁵ Ibid.

⁷⁶ In extraordinary cases, the IMF may convince a member that the conditions are right for the full or partial abolition of these restrictions. The continuance of the measures upheld by Article XIV, Section 2 must be discussed annually by members with the IMF.

Article VIII but kept restrictive measures.⁷⁷ In contrast, a member country may abolish all such steps without informing the IMF that it has agreed to the terms of Article VIII.⁷⁸

3.1.2. International Institutional Framework for Foreign Currency Regulation

A. The IMF

As part of the bilateral and multilateral surveillance procedure, member countries are required to inform the IMF of the arrangement they have chosen. The IMF's Executive Board frequently holds meetings aimed at discussing exchange rate policy, with talks primarily centered on changes in developed countries.⁷⁹ The semi-annual World Economic Outlook, which is reviewed by the Executive Board and provides the fundamental analytical framework for the IMF's assessment of the global economy and the exchange system as a whole, also analyzes exchange rate developments.⁸⁰ The primary tool for surveillance at the national level is the Article IV consultation, a yearly check-up for members that typically ends with an Executive Board discussion of the Country's economic position and policies. The Chairman of the Executive Board and its Executive Director will then present a summary of the Board's opinions to the member's Government.⁸¹

The IMF's foreign exchange policy advice roughly falls into three general areas:

1. *Choice of exchange arrangement*: IMF staff follows a member country's preferred arrangement and adjust their overall policy recommendations correspondingly.⁸² The staff may

⁷⁷ Monetary and Financial Systems and Legal Departments, *Article VIII Acceptance by IMF Members: Recent Trends and Implications for the Fund* (International Monetary Fund 2006) para 16.

⁷⁸ *ibid.*

⁷⁹ Burton and Gilman (n 68), p. 19

⁸⁰ *ibid.*

⁸¹ *ibid.*

⁸² Burton and Gilman (n 68), p. 20

suggest using suitable financial policies in conjunction with an exchange rate depreciation to improve the balance of payments where an exchange rate change is feasible.⁸³ A particular exchange arrangement may occasionally be recommended by a country's institutional, economic, and political objectives.⁸⁴ For instance, a fixed exchange rate as a benchmark rate may be appealing when lowering inflation is a top priority, but greater exchange rate flexibility may be required if international reserves are at a low level and improving the balance of payments is the highest priority.

2. *Removal of exchange restrictions:* Promoting currency convertibility is a key part of the IMF's mission.⁸⁵ It basically refers to the unrestricted use of a country's currency in international trade and the freedom to freely exchange it for different exchanges.

However, it should be stated that this concept is restricted as stated under Article VIII. Members are required to maintain financial convertibility, but not commodity convertibility which is the absence of restrictions (quotas and bans) in trade transactions. The IMF's notion in this regard only pertains to current transactions. Though trade restrictions have comparable effects to exchange restrictions and can lessen the advantages of currency convertibility, the IMF also supports the freedom of capital transactions and urges its members to liberalize trade.⁸⁶

3. *Technical assistance in designing or modifying systems:* Technical support can be given in a variety of ways. However, the majority of exchange rate assistance for many developing countries comes from IMF initiatives that were specifically created for them⁸⁷ which Ethiopia is a beneficiary of as discussed in the next chapter. The IMF doesn't recommend a single

⁸³ *ibid.*

⁸⁴ *ibid.*

⁸⁵ Martin G Gilman, 'Heading for Currency Convertibility', *Finance and Development* (International Monetary Fund 1990).

⁸⁶ Burton and Gilman (n 68), p. 21

⁸⁷ *ibid.*

exchange rate policy that works best; instead, it bases its recommendations on the specifics of each country.⁸⁸

B. The World Trade Organization (WTO)

Article XV of the General Agreement on Tariffs and Trade 1994 (GATT)⁸⁹ is the only WTO provision that explicitly deals with exchange arrangements. The WTO and IMF have the objective of collaborating in order to control currency manipulation. According to the GATT, Article XV paragraph 1, the WTO members must collaborate with the IMF and implement a coordinated exchange policy.⁹⁰ The members must "consult fully with" the IMF and "accept all findings of statistical and other facts presented by the Fund relating to foreign exchange" as well as its assessment of whether a particular action violates the IMF Articles of Agreement, according to paragraph 2.⁹¹ In addition, the two institutions came to the Agreement Between the IMF and the WTO based on their shared respect for cooperation. According to paragraph 8 of the agreement, the IMF is required to inform the WTO as to whether exchange activities that fall within its purview are in line with IMF policies.⁹²

Article XV of the GATT refers to the close relationship between foreign commerce and exchange rates.⁹³ The aim of the GATT rules and the IMF's Articles of Agreement may not be defeated by contracting parties through exchange or trade action, according to paragraph 4.⁹⁴ This rule

⁸⁸ *ibid.*

⁸⁹ World Trade Organization (WTO), 'General Agreement on Tariffs and Trade 1994' (55 UNTS 194 (GATT) 1994).

⁹⁰ World Trade Organization (WTO), *General Agreement on Tariffs and Trade 1994* (1994), Article XV, para. 1

⁹¹ *ibid.*, Article XV, para. 2

⁹² Agreement Between the International Monetary Fund and the World Trade Organization (adopted 18 November 1996) Decision No. 11381-(96/105) in WTO Agreements with the Fund and the Bank WT/L/195, para 8.

⁹³ World Trade Organization (WTO) (n 89), Article XV

⁹⁴ *ibid.*, Article XV, para. 4

specifically acknowledges the potential effects of exchange rates on trade and completes IMF Article IV's prohibition on foreign exchange restrictions.

However, it should be highlighted that, aside from the specific instances of multiple currency practices or exchange restrictions, the IMF lacks the authority to assess exchange acts that would breach trade obligations under the WTO. This could be seen in *the Dominican Republic – Imports and Sales of Cigarettes* case.⁹⁵ The case was brought to the WTO's Dispute Settlement Body (DSB) by Honduras after the Dominican Republic levied a foreign exchange fee on all transactions involving foreign exchange that was calculated using the price of the imported items at the selling exchange rate.

One issue raised in this case was how to classify the questioned measure. The DSB asked if it could be considered as an import charge which relates to the WTO's jurisdiction or could it be an exchange control falling under the IMF's jurisdiction? According to the Dominican Republic, the measure was permitted by the IMF and, therefore, complies with the Articles of Agreement.⁹⁶ The WTO's DSB consulted the IMF asking if the Dominican Republic's measure could be classified as a restriction to forex pursuant to the Articles of Agreement.⁹⁷

Therefore, the WTO has the authority to rule on the legality of a member state's currency exchange regime based on the IMF's finding of manipulation, while the IMF has the authority to determine whether a member state's currency intervention constitutes an illegal currency manipulation either at the request of the WTO or on its own initiative.⁹⁸ The GATT's Article XV(4) serves as a link between the two accords.

⁹⁵ WTO, *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes*, Panel Report, 26 November 2004, WT/DS302/R

⁹⁶ Vera Thorstensen, Daniel Ramos and Carolina Muller, *Exchange Rate Measures, Who Judges the Violation? Sorting out Prerogatives* (2013) 15.

⁹⁷ *ibid* 16.

⁹⁸ Haneul Jung, 'Tackling Currency Manipulation with International Law: Why and How Currency Manipulation Should Be Adjudicated?' (2012) 9 *Manchester Journal of International Economic Law* 184, 189.

3.2. Ethiopian Foreign Currency Regulation Framework

3.2.1. National Legal Framework for Foreign Currency Regulation

In accordance with Article 51(7) of the Constitution of the Federal Democratic Republic of Ethiopia [hereinafter referred to as “the Constitution”]⁹⁹, the federal government has the authority to manage the National Bank, print and borrow money, mint coins, regulate foreign exchange and money in circulation. It goes without saying, almost every matter relating to money in general and foreign exchange, in particular, comes under the sole purview of the federal government's power.

Regarding the legislative power over financial and monetary issues, Article 55(10) of the Constitution grants the House of Peoples’ Representatives the authority and responsibility to pass laws pertaining to the local currency, the management of the National Bank, and foreign exchange. Using this authority as a basis, the House of Peoples’ Representatives enacted the National Bank of Ethiopia Establishment (as Amended) Proclamation No. 591/2008.¹⁰⁰

The National Bank of Ethiopia Establishment (as Amended) Proclamation No. 591/2008, subsequent to the FDRE Constitution, lays the foundation for the legal framework for foreign exchange regulation in Ethiopia. Within this framework, there are numerous directives issued by the NBE, which is entrusted with the duty and power to regulate foreign currency. As discussed in the next chapter, the NBE has issued 82 Directives on foreign exchange as of March 2023. To say the least, these Directives are specific and cover extensive areas of foreign exchange.

3.2.2. National Institutional Framework for Foreign Currency Regulation

Concerning the institutional framework for foreign exchange matters, Article 77(4) of the FDRE Constitution empowers the Council of Ministers and the National Bank of Ethiopia (NBE) to regulate foreign currency.

⁹⁹ Constitution of the Federal Democratic Republic of Ethiopia, 1995, Proclamation No.1, Federal Negarit Gazette, Year 1, No.1 [hereinafter referred to as “the FDRE Constitution” or “the Constitution”]

¹⁰⁰ “The National Bank of Ethiopia Establishment (as Amended) Proclamation” (n. 6)

Consequently, the NBE acts as the central bank of Ethiopia. The NBE was established by Order No. 30/1963.¹⁰¹ It was later re-structured by the Monetary and Banking Proclamation No. 83/1994.¹⁰² It is currently operating pursuant to the National Bank of Ethiopia Establishment (as Amended) Proclamation No. 591/2008.¹⁰³

By virtue of the National Bank of Ethiopia Establishment (as Amended) Proclamation No. 591/2008¹⁰⁴ and other related directives, guidelines, and letters (seculars), the NBE prudently monitors all foreign currency transactions. the National Bank of Ethiopia Establishment (as Amended) Proclamation No. 591/2008,¹⁰⁵ under Article 5, gives broad power to the NBE and mandates the following:

- ✓ Restricting foreign currency transactions to banks and authorized dealers only;
- ✓ Imposing restrictions on who may own and use foreign money or instruments of payment in foreign exchange, including restrictions on residents and non-residents;
- ✓ NBE's oversight of banks' foreign currency activities, etc.¹⁰⁶

Article 20 (2) of the National Bank of Ethiopia Establishment (as Amended) Proclamation No. 591/2008¹⁰⁷ authorizes the NBE to issue directives that regulate the conditions, limitations, and circumstances under which residents of Ethiopia, and nonresidents visiting Ethiopia, or any other person may possess and utilize foreign currency or instruments of payments in foreign exchange.

¹⁰¹ “National Bank of Ethiopia Charter, Order No. 30, Monetary and Banking Proclamation, No. 206/1963, Negarit Gazette Year 22, No. 20, December 1963, Addis Ababa, Ethiopia.”

¹⁰² Monetary and Banking Proclamation, 1994, Proclamation No. 83/1994, Negarit Gazette of the Transitional Government of Ethiopia, Year 53, No. 40, Addis Ababa, Ethiopia.

¹⁰³ “The National Bank of Ethiopia Establishment (as Amended) Proclamation” (n. 6)

¹⁰⁴ Ibid.

¹⁰⁵ Ibid.

¹⁰⁶ *ibid*, Art. 5

¹⁰⁷ *Ibid*, Art. 20(2)

With these directives, the NBE aims to keep the national currency's purchasing power to maintain price stability in accordance with the Monetary Policy Framework (MPF).¹⁰⁸

The Ethiopian Revenues and Customs Authority, now restructured and split into the “**Ministry of Revenue**” and “**Ethiopian Customs Commission**”, also plays a regulatory role in the foreign exchange regime. Article 20(4) of the National Bank of Ethiopia Establishment (as Amended) Proclamation No. 591/2008¹⁰⁹ provides that the Ethiopian Customs Commission shall not allow the import or export of valuable goods or foreign exchange unless conditions, circumstances, and terms determined by the NBE are fulfilled. The Commission is mandated with regulating the import and export and foreign exchange in accordance with the NBE’s regulatory standards. **Ethiopia’s Financial Intelligence Centre**¹¹⁰, **the Ministry of Finance**¹¹¹ and the **Ethiopian Investment Commission**¹¹² also play crucial roles in regulating foreign exchange.

Commercial Banks are also vested with the power to regulate foreign currency as per the Directive to transfer NBE's Foreign Exchange Functions to Commercial Banks Directive No. FXD/07/1998. According to this Directive, and a subsequent one (Directive No. FXD/75/2021), Commercial Banks can involve in transactions of forex. In doing so, Commercial Banks approve and disapprove applications for different foreign exchange inquiries from their customers, including approval of payment modes such as Letters of Credit, Advance Payment, and Consignment. However, the NBE closely monitor and inspect the operations of Commercial Banks in their transactions in foreign currency.

¹⁰⁸ National Bank of Ethiopia, *NBE’s Monetary Policy Framework* (NBE 2009) 2.

¹⁰⁹ “The National Bank of Ethiopia Establishment (as Amended) Proclamation” (n. 6)

¹¹⁰ “Prevention and Supersession of Money Laundering and the Financing of Terrorism Proclamation, December 2009, Proclamation No. 657/2009, Federal Negarit Gazette, Year 16, No. 1, Addis Ababa, Ethiopia,” Article 21.

¹¹¹ Definition of Powers and Duties of the Executive Organs Proclamation, 2022, Proclamation No. 1263/2022, Federal Negarit Gazette, Year 28, No. 4, Addis Ababa, Ethiopia, Article 26.

¹¹² Investment Proclamation, April 2020, Proclamation No. 1180/2020, Federal Negarit Gazette, Year 26, No. 28, Addis Ababa, Ethiopia, Articles 35 and 38.

Chapter Four: Relevance and Conformity of Ethiopian Foreign Currency Regulation Regime with International Financial Laws

4.1. Relevance of International Financial Regulation Schemes in Ethiopia

4.1.1. Ethiopia's Membership at the IMF and the Benefits

Ethiopia became a member of the IMF on 27 December 1945.¹¹³ Ethiopia's quota at the IMF is SDR¹¹⁴ 300.70 million.¹¹⁵ This amounts to a 0.06% share of the total SDR 476,272 million.¹¹⁶ This leaves Ethiopia with 4,466 votes amounting to 0.09% votes from the total votes.¹¹⁷ For reference, the Republic of South Sudan has 0.08% votes; Kenya has 0.14% votes; South Africa has 0.63%; the Russian Republic has 2.59%; China has 6.08%, and the United States of America has 16.50% votes.¹¹⁸ The voting share of Ethiopia is very low that even Luxembourg, which has only half a million population, has twice more vote shares as Ethiopia.

The IMF rates Ethiopia as a high-intensity technical assistance recipient since there have been 38 technical assistance missions by the IMF in Ethiopia.¹¹⁹ The technical assistances include training on tax policy, revenue administration, money and training exchange markets, and developing other policies.

¹¹³ IMF, (n 5) 2 of Index 1.

¹¹⁴ SDR stands for "Special Drawing Rights" and it is an international reserve asset created by the IMF to supplement the official reserves of its member countries. The currency value of the SDR is determined by summing the values in U.S. dollars of a basket of major currencies. See "the Articles of Agreement", and "<https://www.imf.org/en/Topics/special-drawing-right>" for more information.

¹¹⁵ IMF, (n 5) 2 of Index 1.

¹¹⁶ IMF, 'IMF Members' Quotas and Voting Power, and IMF Board of Governors' <<http://www.imf.org/external/np/sec/memdir/members.htm>>.

¹¹⁷ *ibid.*

¹¹⁸ *ibid.*

¹¹⁹ IMF, (n 5) 4 of Index 1.

Member countries are known to be following the IMF code of conduct and this encourages investment and trade, leading to fuller employment.¹²⁰ Therefore, Ethiopia, as a member whose membership hasn't been revoked, is regarded as a country having good compliance with the IMF's Articles of Agreement. Moreover, it was reported that most investors and lending-countries frequently use IMF reports and policy documents as a foundation of their decisions.¹²¹ However, the correlation between IMF's membership and increased investment in Ethiopia is not studied and cannot be asserted with evidence.

Other than this, Ethiopia is also a beneficiary of IMF's loans because of its membership in the IMF. Since 1984 and until 2023, Ethiopia has had an outstanding loan of SDR 524,550,000 from the IMF.¹²² Ethiopia, as a country that passed or is passing through the impacts of the Covid-19 pandemic and a domestic war, clearly needs support to address humanitarian and economic challenges. This was acknowledged by the IMF and was brought up by the Communications Director at the Media Briefing in March 2023.¹²³ It is to be recalled that regardless of the domestic war that broke out in 2020, the IMF had supported Ethiopia with emergency assistance of USD 400 million just for Covid-19-related measures.¹²⁴

¹²⁰ IMF, 'Why Join the International Monetary Fund?' <https://www.imf.org/external/np/exr/center/mm/eng/mm_bnfts.htm> accessed 2 March 2023.

¹²¹ Muhumed Mohamed Muhammed and Sayid Aden Gaas, 'The World Bank and IMF in Developing Countries: Helping or Hindering?' (2016) 28 *International Journal of African and Asian Studies* 47.

¹²² IMF, 'Ethiopia: IMF Credit Outstanding as of February 28, 2023' <<https://www.imf.org/external/np/fin/tad/exportal.aspx?memberKey1=290&date1key=2023-02-28&category=EXC>> accessed 20 March 2023.

¹²³ International Monetary Fund (IMF), 'Transcript of IMF Press Briefing: March 23, 2023' (*Transcript of IMF Press Briefing*) <<https://www.imf.org/en/News/Articles/2023/03/23/tr032323-imf-press-briefing>> accessed 30 March 2023.

¹²⁴ International Monetary Fund (IMF), 'IMF Executive Board Approves US\$411 Million in Emergency Assistance to Ethiopia to Address the COVID-19 Pandemic' (30 April 2020) <<https://www.imf.org/en/News/Articles/2020/04/30/pr20199-ethiopia-imf-executive-board-approves-emergency-assistance-to-address-the-covid-19-pandemic#:~:text=Ethiopia%20is%20facing%20a%20pronounced,under%20the%20Rapid%20Financing%20Instrument.>>> accessed 11 March 2023.

The IMF provides different financing facilities and arrangements to which Ethiopia is a beneficiary. From which the “Poverty Reduction and Growth Facility” is the most important facility to Ethiopia.¹²⁵ The IMF implements the Poverty Reduction Strategy Framework and the HIPC Initiative in combating poverty in Ethiopia. The former includes advisory and aid coordination support while the latter provides debt relief assistance.¹²⁶

The other benefit of being an IMF member is that membership to the IMF is a precondition to becoming a member of the World Bank.¹²⁷ Additionally, when dealing with problems involving monetary reserves, the balance of payments, and foreign currency arrangements, the WTO is required to consult the IMF. The assessment of the IMF on member countries’ balance of payments condition serves as the foundation for the Balance of Payments Committee of the WTO to evaluate restrictions.¹²⁸ This is to show that IMF’s assessments on financial restrictions are used as one indicator to prove the persistence of trade restrictions by a Country.

Ethiopia is a beneficiary of the IMF’s Poverty Reduction and Growth Trust. Under this arrangement, Ethiopia received SDR 133,640,000 in 2020, SDR 80,220,000 in 2010, SDR 106,960,000 in 2009.¹²⁹ In total, Ethiopia has received loans amounting to SDR 500,007,000 over the past 40 years.¹³⁰ IMF’s Poverty Reduction and Growth Trust (PRGT) carries zero interest rates

¹²⁵ International Monetary Fund (IMF), *International Monetary Fund Handbook: Its Functions, Policies and Operations* (n 4).

¹²⁶ *ibid.*

¹²⁷ Muhammed and Gaas (n 121) 42.

¹²⁸ International Monetary Fund (IMF), *International Monetary Fund Handbook: Its Functions, Policies and Operations* (n 4) 69.

¹²⁹ International Monetary Fund (IMF), ‘Ethiopia: Transactions with the Fund from May 01, 1984 to April 30, 2023’ (*IMF Data*)

<https://www.imf.org/external/np/fin/tad/extrans1.aspx?memberKey1=290&endDate=2099%2D12%2D31&finposition_flag=YES> accessed 16 May 2023.

¹³⁰ *ibid.*

aimed at further enhancing PRGT-eligible countries, such as Ethiopia, in fragile situations.¹³¹ The financing under this arrangement also has a grace period ranging from 4 to 10 years.¹³²

4.1.2. Ethiopia's Membership at the IMF and its Disadvantages

Although Ethiopia is a beneficiary as a member of the IMF, there is also another side of this story from skeptics of the IMF system. The IMF was criticized by several scholars and politicians for practicing bad governance, marginalizing the developing world, biased policies and hypocrisy, prioritizing the interests of the west, and providing harmful technical and financial assistance.¹³³

IMF's conditionality is also raised as a burdensome feature of IMF's loans. IMF provides loans to member countries after assessing three conditions: (1) performance criteria; (2) program reviews by the Executive Board; and (3) prior actions.¹³⁴ Among these, the performance criteria is deemed to be more challenging to borrowers. Two major categories can be used to divide performance criteria. The first is the quantitative performance criterion, which includes quantitative goals that must be met while considering important macroeconomic factors during the member's program.¹³⁵ The amount of net foreign reserves, the size of the budget deficit, and the amount of non-concessional external borrowing are typical examples.¹³⁶

The second type of performance criteria consists of structural measures, or structural actions, the implementation of which is seen as being essential to the program's success. These requirements

¹³¹ International Monetary Fund (IMF), 'IMF SUPPORT FOR LOW-INCOME COUNTRIES' (*IMF Data*) <<https://www.imf.org/en/About/Factsheets/IMF-Support-for-Low-Income-Countries>> accessed 15 May 2023.

¹³² *ibid.*

¹³³ *See for instance:* Griffith-Jones, S., "Governance of the World Bank". Report prepared for DFID, (2002); Moyo, D., "Dead aid: Why aid is not working and how there is a better way for Africa". Macmillan, (2009); Elsayid, E., "The Hidden Role of WB and IMF in Developing Countries. Egypt, Malaysia and Turkey". Saarbrücken: AV Akademikerverlag, (2016); Gerber, J., "International Economics (6th ed.)". Boston: Pearson, (2014).

¹³⁴ International Monetary Fund (IMF), 'Guidelines on Conditionality' <<https://www.imf.org/External/np/pdr/cond/2002/eng/guid/092302.pdf>> para. 11.

¹³⁵ Ross B Leckow, 'Conditionality in the International Monetary Fund', *Current Developments in Monetary and Financial Law*, vol 3 (International Monetary Fund 2005) 56.

¹³⁶ *ibid* 57.

frequently entail legislative changes, such as the adoption of new banking or bankruptcy laws.¹³⁷ To be eligible to receive funding from the IMF with regard to these various performance criteria, a member must show that the pertinent performance criteria have been satisfied.¹³⁸

Regarding Ethiopia, a Technical Memorandum of Understanding (TMU) detailing the statistical and structural evaluation criteria agreed by the Ethiopian government and the IMF for oversight of the IMF's initiatives was signed. According to this memorandum of understanding, Ethiopia has set quantitative targets on¹³⁹:

- The National Bank's reserve money,
- The National Bank's net international reserves,
- The Government's primary balance or net financing

In addition to the above quantitative targets, Ethiopia has agreed to adhere to the following conditionalities:

- i. *“non-imposition or intensification of restrictions on the making of payments and transfers for current international transactions;*
- ii. *non-introduction or modification of multiple currency practices, excluding the introduction or modification of a multiple price auction system developed in consultation with Fund staff;*
- iii. *prohibition of entering into bilateral payments agreements that are inconsistent with Article VIII of the Fund's Articles of Agreement; and*
- iv. *non-imposition or intensification of import restrictions for balance of payments reasons.”*¹⁴⁰

¹³⁷ *ibid.*

¹³⁸ International Monetary Fund (IMF), 'Guidelines on Conditionality' (n 135) para. 1.

¹³⁹ IMF and FDRE, *Technical Memorandum of Understanding between FDRE and IMF* (2019) para. 6.

¹⁴⁰ *ibid* para. 6.

Moreover, according to a macroeconomic advisor to the Governor of the NBE, the IMF's stance is to foster a more competitive financial sector with low interference from the public sector. Hence, Ethiopia enters into a lending agreement with the IMF based on specific measures to that goal.¹⁴¹

These conditions seem burdensome but the IMF manages to justify them stating that the conditions are intended to ensure that member countries are assisted in resolving their balance of payments problems in a manner that is consistent with the IMF's Articles of Agreement.¹⁴² The conditions, according to the IMF, are necessary to establish adequate safeguards for the temporary use of the IMF's resources by member countries.¹⁴³

Conditionality has been a subject of controversy since its introduction in the 1950s.¹⁴⁴ According to a study done on 81 developing countries between 1986 and 2016, those under IMF structural conditions tend to witness rises in poverty, and those under stabilization conditions tend to see relatively little change in poverty.¹⁴⁵ The study concludes that structural reforms included in IMF loan agreements increase the number of people caught in the poverty cycle because they entail extensive changes that often increase unemployment, decrease tax revenue, raise the price of basic services, and alter taxation, pensions, and social security programs.¹⁴⁶

Overall, there is a scant study and evidence that specifically assesses the impact of the IMF on Ethiopia's economy to conclusively say whether the country is advantageous or not. The above two sub-sections show that Ethiopia has been benefiting from the poverty-related loan programs set by the IMF at zero interest and other emergency loan programs during the Covid-19 pandemic. On the contrary, IMF's conditionality could be criticized for imposing burdensome policy reforms on Ethiopia.

¹⁴¹ Interview with Tewodros Makonnen (Ph.D.), a Microeconomics Advisor to the Governor of the NBE (Addis Ababa, Ethiopia, 10 March 2022).

¹⁴² International Monetary Fund (IMF), 'Guidelines on Conditionality' (n 135) para. 1.

¹⁴³ *ibid* para. 1.

¹⁴⁴ Leckow (n 136) 25.

¹⁴⁵ Glen Biglaiser and Ronald J. McGauvran, 'The Effects of IMF Loan Conditions on Poverty in the Developing World' (2022) 25 *Journal of International Relations and Development* 806, 807.

¹⁴⁶ *ibid* 833.

4.1.3. Ethiopia and Article VIII Obligations

Members agree not to place restrictions on payments and transfers for current foreign transactions or engage in discriminatory currency arrangements unless the IMF approves. After joining the IMF, exchange restrictions applied by Article XIV members are regarded as having been implemented under Article VIII. With respect to nations that have benefited from Article XIV's transitional provisions, acceptance of Article VIII has improved to some extent since 2000. In 2000, there were 34 of them; by the end of 2022, there were only 17.¹⁴⁷

Turkmenistan, Syria, Somalia, So Tome and Principe, Nigeria, Myanmar, Maldives, Liberia, Iraq, **Ethiopia**, Eritrea, Burundi, Bosnia and Herzegovina, Bhutan, Angola, and Afghanistan are among the Article XIV members who use the transitional measures.¹⁴⁸ From the 17 countries listed Ethiopia is among the 9 countries identified by “the Annual Review of Exchange Arrangements and Exchange Restrictions (AREAER)”¹⁴⁹ each year for arranging an overall restrictive foreign exchange regime.

As of 2023, Ethiopia hasn't accepted Sections 2, 3, and 4 of Article VIII. This indicates that Ethiopia is still able to take use of Section 2 of Article XIV's transitional provisions. However, new forex measures are bound by Article VIII and could only be implemented upon the IMF's permission, even for member countries that utilize the transitional provisions of Article XIV, Section 2. Therefore, Ethiopia still needs the approval of the IMF to introduce new measures that restrict foreign exchange transactions.

Article 26 of the Articles of Agreement provides that failure to adhere to obligations under Article VIII can subject a member country to escalating denial of membership benefits, including initial disenfranchisement from using the resources of the IMF, followed by denial of rights such as voting and, in the worst-case scenario, complete removal from membership. Hence, if Ethiopia is found

¹⁴⁷ International Monetary Fund (IMF), ‘AREAER’s Annual Report on Exchange Arrangements and Exchange Restrictions’ (International Monetary Fund 2022) 22.

¹⁴⁸ *ibid* 23.

¹⁴⁹ The AREAER is a report prepared in consultation with national authorities. It provides details on various nations' exchange controls, foreign trade policies, and exchange rate arrangements.

to violate the Articles of Agreement by putting in place restrictive measures on foreign exchange, then the above consequences may follow.

Expulsion from the IMF is not a common occurrence. So far, there has not been an incident causing the expulsion of an IMF member Country due to unconformity with Article VIII obligations. However, back in 2002, Zimbabwe was suspended from voting and related rights for not “sufficiently strengthening its cooperation with the IMF in areas of policy implementation and payments.”¹⁵⁰ Zimbabwe was suspended from using its right to appoint a Governor or Alternate Governor to the IMF, participate in the election of an Executive Director for its Board, or cast its vote in decisions on IMF policy or country matters.¹⁵¹

4.2. Measures under the Ethiopian Foreign Currency Regulation Regime Contrary to International Financial Regulations

IMF’s Executive Board¹⁵² made the latest assessment of Ethiopia’s overall monetary and financial regulatory operations in 2019. The assessment concluded that four particular measures by the NBE “are not consistent with the Articles of Agreement’s Section 2(a) of Article VIII.” The measures identified to be inconsistent were the prioritization of specific imports to access forex, restrictions on repayment of legal external loans, tax certification requirement for repatriation of dividends, and clearance certificate requirement to obtain import permits.¹⁵³

¹⁵⁰ International Monetary Fund (IMF), ‘Press Release No. 03/80: IMF Suspends Zimbabwe’s Voting and Related Rights’ (6 June 2003) <<https://www.imf.org/en/News/Articles/2015/09/14/01/49/pr0380>> accessed 5 February 2023.

¹⁵¹ *ibid.*

¹⁵² The Managing Director serves as the Executive Board's chairman. The Board of Governors has delegated to the Executive Board the authority to manage the day-to-day operations of the IMF. All IMF financing activities must receive its approval because it is the IMF's policy-making body. (see Margaret Garristen de Vries, *The International Monetary Fund*, vol II, p. 999 and International Monetary Fund (IMF), *International Monetary Fund Handbook: Its Functions, Policies and Operations* (2007), p. 72)

¹⁵³ IMF, ‘2019 Article IV Consultation and Requests for Three-Year Arrangement under the Extended Credit Facility and an Arrangement under the Extended Fund Facility—Press Release and Staff Report’ (2018) IMF Country Report No. 20/29, p. 19.

This chapter unpacks the first two measures and other similar restrictions on foreign currency put in place by the NBE and evaluates the conformity of the measures with international financial regulations.

4.2.1. Restrictions on Allocation of Foreign Exchange for Import Goods

As of 2022, twenty-one countries have adopted a method for allocating foreign currency.¹⁵⁴ Allocation of forex is usually utilized when foreign exchange reserves are low to supply foreign exchange for imports of food or medicine. It has occasionally been used to fund important sectorial initiatives in Ethiopia and to fund strategic imports in Sudan. It may also be used to purchase inputs for manufacturers just like they do in Bangladesh.¹⁵⁵ This may boost exports by facilitating funding in foreign currencies for exporting manufacturers.

The NBE instituted foreign currency allocation standards as the foreign currency shortage grew worse aiming to (i) preserving the banking system’s reliability and stability, (ii) defending the objectives of the Second Growth and Transformation Plan (GTP II)¹⁵⁶, (iii) improving transparency in foreign currency allocations.¹⁵⁷ In 2016 and 2017, the allocation Directives were amended. Then, in September 2018, the NBE issued Directive, FXD/57/2018. This was, again, amended in 2020 and 2021. As of March 2023, Directive No. FXD/77/2021, “Transparency in Foreign Currency Allocation and Foreign Exchange Management (as Amended)”¹⁵⁸ serves as the latest Directive to oversee forex allocation.

¹⁵⁴ International Monetary Fund (IMF), ‘AREAER’s Annual Report on Exchange Arrangements and Exchange Restrictions’ (n 147) 19.

¹⁵⁵ *ibid.*

¹⁵⁶ Federal Democratic Republic of Ethiopia, ‘Growth and Transformation Plan II (GTP II) (2015/16-2019/20)’ (National Planning Commission 2016).

¹⁵⁷ James Llyod and Bisrat Teshome, *Foreign Exchange Allocation and Access for Businesses in Ethiopia (Redacted Version)* (Business Environment Reform Facility 2018) 7.

¹⁵⁸ Transparency in Foreign Currency Allocation and Foreign Exchange Management (as Amended) Directive, Directive No. FXD/77/2021, National Bank of Ethiopia, Addis Ababa.,

In accordance with Directive No. FXD/77/2021, the board of directors of banks must establish guidelines that help overseeing operations of forex. The Directive additionally ensures that bank's allocation committee meetings enable evaluations of compliance with the regulation, including the most recent data on requests for and allocations of forex.¹⁵⁹

Directive No. FXD/77/2021 categorizes requests for forex based on the items for import as “on-demand items, priority imports, and non-priority imports.” The following are the top primacies, which are free from registration requirements and call for the immediate (on-demand) sale of foreign currency¹⁶⁰:

1. Foreign currency requests from foreign currency and retention accounts;
2. Forex request from the Foreign Exchange Bureau (under Directive No. FXD/17/2001);
3. Invisible payments (consultancy fees, royalty fees, aviation service payments, communication service payments, salaries and allowances of Ethiopian diplomatic missions, naval personnel, Ethiopian Orthodox church transfer abroad, travel allowance for religious institutions, etc.);
4. External debt repayments and supplier credits where the payments are authorized by the NBE;
5. Salary transfers from foreign employees.

Imports of essential goods come in second when it comes to foreign currency. FXD/51/2017 required that at least 40% of the foreign currency that banks designate for imports be used for imports of goods that are completely essential. This was revised by Directive No. FXD/57/2018 by at least 50%. Directive No. FXD/77/2021 also maintains this share of allocation.¹⁶¹ If less than 50% of the total is allocated for essential goods, the remainder must be given to the National Bank. Foreign exchange queries for imports of goods that are essential should be submitted in writing and then processed in accordance with three tiers of priority, starting with the top priority.

¹⁵⁹ *ibid.*, Article 4

¹⁶⁰ *Ibid*, Article 6.4

¹⁶¹ *Ibid*, Article 6.1.1

- 1) “First priority:
 - a. Pharmaceuticals (medicine and input for the manufacturing of pharmaceuticals and laboratory reagents)
 - b. Fuel (liquefied petroleum gas)
 - c. Input for manufacturing of edible oil”
- 2) “Second priority:
 - a. Agricultural inputs
 - b. Manufacturing inputs”
- 3) “Third priority:
 - a. Nutritious foods for babies
 - b. Pharmaceutical products
 - c. Profit and dividend transfer
 - d. Lubricants and motor oil
 - e. Educational materials (exercise books, ball pens and pencils, and printing papers)
 - f. Agricultural inputs and machineries (including tractors and animal hybrids)
 - g. Request of industries for spare parts, or machines’ procurement,
 - h. Spare parts for construction machines for own use by construction companies whose total values not exceeding USD 50,000
 - i. Foreign airlines’ sales transfer”¹⁶²

A cloud-based system was created in August 2018 and sends a daily report to NBE about the queues, along with information about new registrations and allocations. Banks are required to use this method by Directive No. FXD/77/2021. The queues can only be accessed at NBE, and this method does not permit an in-depth analysis of the queues. Directive No. FXD/77/2021 also prohibits an exporter from allocating foreign currency to an importer contrary to the framework outlined. According to officers at the NBE, businesses that request foreign currency for imports must describe the imported goods using the eight-digit Harmonized System of Commodity Coding.

¹⁶² Ibid.

Commentators have criticized the various depreciation rates used to determine car minimum values. Along with their weekly submission of applications for foreign money, banks also provide NBE with documentation of their arrangement to minimum prices and a pro forma.¹⁶³

This shows that the National Bank puts restrictions on the allocation of foreign currencies for the import of goods. The restrictions are then followed by documentation requirements aimed at restraining importers' access to foreign currency.

Since the measure is implemented for balance of payments purposes, it falls under one of the grounds for the exceptions of Article VIII of the Articles of Agreement. However, it is not utterly consistent with Article VIII of the IMF's Articles of Agreement because it fails to meet two conditions; the measure was not approved by the IMF, and it is not made provisionally. Prioritizing the allocation of foreign currency for imports would affect the making of payments that are not for the purpose of transferring capital. This also affects international trade as importers of certain products cannot easily access foreign currency to make payments. In addition to that, such measures are required to be provisional in the sense that there is a clear timeline for their elimination¹⁶⁴, which was not the case for the NBE's measures.

According to the NBE, the economic rationale for this measure is to ensure that scarce forex resources should be channeled first to essential goods like fuel, fertilizer, and pharmaceuticals.¹⁶⁵ Furthermore, the measure is aimed at putting the scarce resource to productive use by prioritizing manufacturing and agricultural inputs including capital goods and machinery.¹⁶⁶

4.2.2. Restrictions against Repayments of Supplier's Credit and External Loans

Credit of Suppliers and external loan are regulated by "the External Loan and Supplier's Credit Directive No. FXD/82/2022." The very purpose of this Directive, as provided under the preamble

¹⁶³ Llyod and Teshome (n 157) 9.

¹⁶⁴ 'Discrimination for Balance of Payments Reasons' (n 74).

¹⁶⁵ Interview with Tewodros Makonnen (Ph.D.) (n 142)

¹⁶⁶ Ibid.

of the same, is to regulate foreign exchange by determining the procedures to register external loans.

The Directive provides eligibility criteria to borrow from external sources as an exporter or as a foreign investor. Accordingly, domestic investors or exporters can only acquire an external loan or supplier's credit if they are engaged in business activities that generate foreign currency.¹⁶⁷ Export license, loan agreement, pro-forma invoice, and document justifying the capacity to repay the loan are among the documents required to get an external loan or suppliers' credit approved by the NBE.¹⁶⁸

The all-in-cost ceilings (including the rate of interest, other fees, expenses, charges, guarantee fees, etc.) for an external loan are set by the Directive. Depending on the maturity period for the loans, the rate used for external loans is a six months Secured Overnight Financing Rate (SOFR)¹⁶⁹ plus a 2%, 3%, or 5% addition on the all-in-cost ceiling.¹⁷⁰ The NBE also regulates the repayment of external loans. Borrowers are required to get approval from the NBE to repay their external loans by presenting different documents¹⁷¹ which are not exhaustively provided by the Directive.

According to officers at the NBE, the necessity of this restriction emanates from the fact that there is a shortage of foreign currency in Ethiopia. With this shortage being persistent, Directive No. FXD/77/2021 instructs banks to provide foreign currency for payment of external loans and suppliers' creditors on demand. On one hand, external loans and suppliers' creditors are prioritized to get the country's share of foreign currency during the allocation arrangement; on the other hand,

¹⁶⁷ External Loan and Supplier's Credit (as Amended) Directive, Directive No. FXD/82/2022, National Bank of Ethiopia, Art. 4.1.1. and 4.1.2.

¹⁶⁸ Ibid., Art. 4.1.3.

¹⁶⁹ SOFR is an interest rate set based on the cost of overnight borrowing for banks collateralized by Treasury securities. It is set by the Federal Reserve Bank of New York for terms of 1 year, 6 months, and 3 months. See the official website of the New York Federal Reserve Bank at: <https://www.newyorkfed.org/markets/reference-rates/sofr>

¹⁷⁰ External Loan and Supplier's Credit (as Amended) Directive, Directive No. FXD/82/2022 (n. 80), Art. 6

¹⁷¹ Ibid., Art. 8

these transactions are subjected to restrictions and limitations on the interest rate of the loans, the identity (business sector) of the borrower, and the repayment of loans.

Since the measures are implemented for balance of payments purposes, they fall under one of the grounds for the exceptions of Article VIII of the Articles of Agreement. However, the measures are not consistent with the Article VIII of the Articles of Agreement because they were not approved by the IMF. Restricting the repayment of loans would affect the making of payments that are not for the purpose of transferring capital. However, one of the arguments raised by Ethiopian authorities is that the restriction is under capital and not a current transaction.¹⁷² This line of argument is misleading since payments of a moderate amount for the amortization of loans qualify as a current transaction by virtue of Article XXX(d)(3) of the Articles of Agreement. It is also worth mentioning that such measures are required to be provisional but the NBE measures were made indefinitely.¹⁷³

4.2.3. Other Restrictions on Foreign Exchange in Ethiopia

4.2.3.1. Surrender to Central Banks

The IMF advises phasing out or getting rid of laws that stifle market activity. The unification of segmented foreign exchange markets, the easing of current capital account limitations, the elimination of taxes and surcharges on foreign exchange transactions, and the elimination of requirements for foreign exchange receipts to be turned over to the central bank are all significant measures.¹⁷⁴

In this regard, the NBE finds it necessary to set foreign exchange exposure limits and foreign exchange surrender requirements on banks to “undertake activities conforming to the achievement

¹⁷² International Monetary Fund (IMF), ‘Ethiopia: 2002 Article IV Consultation and Third Review under the Poverty Reduction and Growth Facility Arrangement - Staff Report’ (International Monetary Fund 2002) IMF Country Report No. 02/220 20.

¹⁷³ ‘Discrimination for Balance of Payments Reasons’ (n 74).

¹⁷⁴ Dutttagupta, Fernandez and Karacadag (n 8) 7.

of safe and stable foreign exchange market in Ethiopia.”¹⁷⁵ Accordingly, the NBE issued numerous directives requiring private banks, exporters, individuals, and other entities in possession of foreign currency to surrender some portion to the NBE.

Private banks: are required to surrender 70% of their foreign currency earnings to the NBE every month.¹⁷⁶ Banks are subjected to a penalty of USD 10,000 per day if they are found in violation of this requirement.¹⁷⁷ Up until 2022, banks were required to surrender only 50% of their foreign currency earnings.¹⁷⁸

Exporters: are required to surrender 70% of their foreign currency earnings to the NBE and 10% to their respective banks.¹⁷⁹ For the surrender to the NBE, the rate used to be capped at 60% until 2022¹⁸⁰ and 30% until 2021.¹⁸¹

The surrender of foreign exchange to the central bank was identified as a stifling market activity by the IMF.¹⁸² According to the IMF’s report surrender of foreign exchange has a number of negative consequences, including causing a shortage of foreign exchange for import, discouraging foreign investment, creating a black market for foreign currency, and making it difficult for

¹⁷⁵ “Foreign Exchange Surrender Requirements of Banks (as Amended) Directive, Directive No. FXD/78/2022, National Bank of Ethiopia (NBE),” preamble.

¹⁷⁶ “The Retention and Utilization of Export Earnings and Inward Remittance Directive, Directive No. FXD/79/2022, National Bank of Ethiopia,” Art. 4(1)

¹⁷⁷ Foreign Exchange Surrender Requirements of Banks (as Amended) Directive (n 87), Art. 5

¹⁷⁸ Foreign Exchange Surrender Requirements of Banks (as Amended) Directive, Directive No. FXD/72/2021, National Bank of Ethiopia, Art. 3(1)

¹⁷⁹ The Retention and Utilization of Export Earnings and Inward Remittance Directive (n 88), Art. 4(2)

¹⁸⁰ The Retention and Utilization of Export Earnings and Inward Remittance Directive, Directive No. FXD/73/2021, National Bank of Ethiopia, Art. 4(2)

¹⁸¹ The Retention and Utilization of Export Earnings and Inward Remittance Directive, Directive No. FXD/70/2021, National Bank of Ethiopia, Art. 4(1)

¹⁸² Duttagupta, Fernandez and Karacadag (n 8) 7.

individuals and businesses to manage their finances.¹⁸³Therefore, the measure by the NBE requiring the surrender of foreign currency is a restrictive measure. However, given that surrender of foreign exchange to central banks is a sovereign act, it is difficult to classify it as being inconsistent with Article VIII. After all, this measure can be justified if any person or corporation surrenders its foreign currency to the central bank and gets access to foreign currency when it needs to make current transactions.

4.2.3.2. Restrictions on Foreign Currency Sale Amount

“The Amendment on the Operation of Foreign Exchange Bureaux Directive No. FXD/43/2013” provides ceilings for the amount of foreign currency a person may buy from the Forex Bureaux. Accordingly, the maximum amount of foreign currency, in cash notes, that a person can access through sale is:

- USD 4,000 limit for allowances of holiday travel,
- USD 10,000 ceiling for business travels,
- USD 4,000 for medical treatment and the balance to be transferred to the medical institution account abroad or by draft,
- USD 4,000 for educational expenses and the balance to be transferred to the institution abroad or by draft,
- USD 10,000 for government travelers.¹⁸⁴

Since the measures are implemented for balance of payments purposes, they fall under one of the grounds for the exceptions of Article VIII of the Articles of Agreement. However, they were not approved by the IMF, and the restriction affects making payments and transfers for current international transactions. This measure prevents individuals and businesses from selling their foreign currency holdings as they see fit. The restriction affects making payments and transfers for current international transactions, which is against Article VIII of the Articles of Agreements.

¹⁸³ International Monetary Fund (IMF), ‘AREAER’s Annual Report on Exchange Arrangements and Exchange Restrictions’ (n 147).

¹⁸⁴ “Amendment on the Operation of Foreign Exchange Bureaux Directive, Directive No. FXD/43/2013, National Bank of Ethiopia,” Art. 3.1

Individuals and businesses cannot make payments or transfers as they can only access the above-stated amounts.

4.2.3.3. Uncertainty of Foreign Exchange Legislation

To improve market transparency and lower transaction costs, the IMF advises harmonizing and streamlining the laws governing foreign currency and avoiding frequent, ad hoc changes to the laws.¹⁸⁵ Unfortunately, this is not the case for Ethiopian foreign currency laws.

The Ethiopian foreign exchange regime has only very progressively been liberalized.¹⁸⁶ As discussed in the previous chapter, the NBE is mandated with issuing directives that regulate foreign currency in Ethiopia by virtue of Articles 39 (1) and (2) of the Monetary and Banking Proclamation No. 83/1994. Accordingly, as of April 2023, 82 82 directives has been issued by the NBE on foreign currencies. In addition to these, there are numerous letters and guidelines. These numbers, in and by themselves, are not troublesome. However, these directives are frequently being issued on the same subjects.

For instance:

- **External Loan and Suppliers' Creditors:** Directive No. FXD/82/2022 (September 07, 2022) repealed Directive No. FXD/76/2021 (October 1, 2021). This happened within less than a year. Again, Directive No. FXD/76/2021 repealed Directive No FXD/71/2021, which was issued in the same year.
- **Retention and Utilization of Export Earnings and Inward Remittance:** Directive No. FXD/79/2022 (January 6, 2022) repealed Directive No. FXD/73/2021 (September 01, 2021) which by itself repealed Directive No. FXD/70/2021 on the same year. Going back to the promulgation history of Directive No. FXD/70/2021, it can be noted that the directive came into effect by repealing Directive No. FXD/66/2020. Thus, four directives on 'Retention and Utilization of Export Earnings and Inward Remittance' were enacted within 2 years.

¹⁸⁵ Duttagupta, Fernandez and Karacadag (n 8) 7.

¹⁸⁶ Llyod and Teshome (n 157) 6.

- **Foreign Exchange Surrender Requirements of Banks:** Directive No. FXD/78/2022 (January 6, 2022) repealed Directive No. FXD/72/2021 of September 2021. This replacement took place within 1 year and 3 months. Directive No. FXD/72/2021 was the successor of the directive it repealed back in 2018, which was Directive No. FXD/54/2018.
- **Transparency in Foreign Currency Allocation and Foreign Exchange Management:** Directive No. FXD/77/2021 (December 1, 2022) repealed Directive No. FXD/67/2020 (October 5, 2022). The latter aged for roughly 2 years, which is longer than its predecessor Directive No. FXD/62/2020, which persisted in effect for less than a year.

The above are a few examples among many that show the frequency of legislation change in the Ethiopian foreign currency regulation regime. It is also noteworthy to mention that these directives are available on the NBE official website only in English.¹⁸⁷

According to the NBE, the frequent legislation change was necessitated by the reform announced by the Home-grown Economic Reform Program three years ago.¹⁸⁸ The reform periods are expected to usually see changes in the rules and regulations.¹⁸⁹

4.2.3.4. Foreign Exchange Tax

There were 2,896 currency exchange bureaus in Ethiopia as of August 19, 2021.¹⁹⁰ For the benefit of the NBE, authorized banks are required to charge a 1.5% commission on foreign exchange transactions.¹⁹¹ This means NBE levies a 1.5% foreign exchange tax on each currency exchange deal that will be paid by the recipient of forex services. This is one form of foreign exchange restriction applied by the NBE.

¹⁸⁷ See <https://nbe.gov.et/foreign-exchange-management/> (Official website of the NBE)

¹⁸⁸ Interview with Tewodros Makonnen (Ph.D.) (n 142)

¹⁸⁹ Ibid.

¹⁹⁰ International Monetary Fund (IMF), 'AREAER's Annual Report on Exchange Arrangements and Exchange Restrictions' (n 147) 1359.

¹⁹¹ *ibid.*

As stated earlier, the imposition of taxes and surcharges on forex transactions was identified a measure that restricts foreign exchange transactions.¹⁹² Taxes on foreign exchange can have a variety of detrimental effects. They may raise the cost of using foreign currency for individuals and businesses, which may deter investment and trade. Additionally, they may develop a black market for foreign currency, making it challenging for governments to regulate the movement of funds. Recently, the IMF has been able to pressure Angola and Libya to eliminate similar exchange tax measures.¹⁹³ Ethiopia remains among the 34 countries listed by the IMF to levy exchange tax against Article VIII according to the IMF's 2022 report.¹⁹⁴

4.3. Objectives of Exchange Restrictions against Article VIII

The terms "Article XIV-members" and "Article-VIII-members" are commonly used in the IMF. The former category of members includes those who have taken advantage of the transitional provisions of Article XIV, Section 2, and informed the IMF of their intention to do so under the authority of Article XIV, Section 3. Article-XIV members are exempt from some of the obligations outlined in Section 2 and 3 of Article VIII. Article XIV, Section 2 expressly permits members to uphold and modify the restrictions on transfers and payments that applied to current transactions when the member first joined the IMF.¹⁹⁵

Regulations governing foreign currency control may occasionally be subject to public policy challenges in the same way that other foreign legal standards are. Simply put, Article VIII, section 2(b) prohibits declaring any foreign exchange control law to be in conflict with the public policy of the forum.¹⁹⁶

¹⁹² Duttagupta, Fernandez and Karacadag (n 8) 7.

¹⁹³ International Monetary Fund (IMF), 'AREAER's Annual Report on Exchange Arrangements and Exchange Restrictions' (n 147) 22–24.

¹⁹⁴ *ibid* 24.

¹⁹⁵ Hans Aufricht, *The Fund Agreement: Living Law and Emerging Practice* (International Finance Section Department of Economics, Princeton University 1969) 7.

¹⁹⁶ Ignaz Seidel-Honenveldern, 'Article VIII, Section 2(b) of the IMF Articles of Agreement and Public Policy' (1989) 23 *The International Lawyers* 958.

Regarding the impact of public policy on the enforceability of exchange contracts, the IMF's reading simply allows for the chance that public policy justifications could be used to keep reliance on article VIII, section 2(b), in place.¹⁹⁷ The question of how narrowly or widely to interpret an "exchange contract" within the meaning of Article VIII(2)(b) has been debated by courts.¹⁹⁸

One of the most well-known cases to address the subject is *Libra Bank v. Banco Nacional de Costa Rica*.¹⁹⁹ The plaintiffs issued loans totaling \$40 million to Banco Nacional, a bank that the Costa Rican government owns 100 percent of. The government enacted restrictions on forex transactions, according to Banco Nacional, preventing the repayment of a loan made to foreigners in dollars. Banco Nacional (the bank) asserted that as a result, it was unable to satisfy the terms of the loan it owed. Additionally, the bank argued that the loan was an "exchange contract"; as a result, the recently implemented restrictions, which were legitimately levied by Costa Rica (an IMF member), made the loan agreement inapplicable pursuant to the Articles of Agreements' Article VIII(2) (b).

This claim was refuted by the U.S. court, which showed reluctance to broaden the definition of "exchange contracts" to cover foreign loans. In the end, the court determined that an agreement to acquire U.S. currency that calls for repayment in U.S. currency is not "an exchange contract" as defined by the Articles of Agreement.²⁰⁰

Undoubtedly, developing countries will contend that the IMF deliberately left Article VIII(2)(b) open to interpretation so as to assist developing countries experiencing financial difficulties. Developing countries, especially those who are sensitive to swings in the price of oil, will be against this type of revision because they may ultimately need the Article the most. While it would

¹⁹⁷ *ibid* 961.

¹⁹⁸ Allan T Marks, 'Exchange Control Regulations within the Meaning of the Bretton Woods Agreement: A Comparison of Judicial Interpretation in the United States and Europe' (1990) 8 *International Tax and Business Law* 105–106.

¹⁹⁹ *Libra Bank Ltd v Banco Nacional De Costa Rica*, 570 *F Supp* 870 (SDNY 1983) (US District Court for the Southern District of New York).

²⁰⁰ *ibid* 875–897.

boost contract clarity and serve their wishes developed countries may support a modification that narrowly interprets the term “exchange contract”.²⁰¹

Some of the objectives intended to achieve by imposing foreign exchange restrictions include:

- ✓ *Restoring Adverse Balance of Payments:* By restricting imports to necessities and promoting exports through currency devaluation, restrictions are implemented to go about the declining forex assets. Imports are limited to the extent permitted by the presence of forex, and the equilibrium of balance of payments thereby created by implementing exchange control.²⁰²
- ✓ *Protecting the Value of the National Currency:* Exchange rate stability may be achieved through the adaptation of exchange restrictions.²⁰³
- ✓ *Policy of Differentiation:* A government may impose import and export restrictions on some countries by withholding its own foreign currency. A country can implement a discriminatory trade strategy through exchange restrictions. In addition to that, exchange regulation and restriction is another policy tool for the government to generate revenue.²⁰⁴
- ✓ *Prevention of Capital Flight:* The term "flight of capital" describes when residents of a nation change their cash holdings into foreign currencies. Capital flight could be the outcome of financial speculation, economic fluctuations, or political uncertainty.²⁰⁵ Countries may deploy foreign exchange restrictions to prevent this.

²⁰¹ David Litvack, ‘Losing Control: Why IMF Article VIII(2)(b) May Nullify the Enforceability of Financing Contracts When Spiraling Oil Prices Prompt the Use of Exchange Controls’ (2008) 13 Fordham Journal of Corporate & Financial Law 823.

²⁰² Asrat Abate, ‘The Effects of Foreign Exchange Control on Performance of Commercial Banks in Ethiopia’ (Unpublished, St Mary’s University, School of Graduate Studies 2021) 10.

²⁰³ *ibid* 11.

²⁰⁴ *ibid* 12.

²⁰⁵ *ibid* 13.

- ✓ *Protection of Domestic Industries:* Through foreign exchange controls, the government limits imports, giving domestic sectors the chance to grow without being concerned about foreign competition.²⁰⁶
- ✓ *Conserve Foreign Exchange:* Foreign currency control and conservation can be applied to protect the forex reserves of a country. Countries may also employ exchange controls to stop their adversaries from using their resources abroad.²⁰⁷
- ✓ *Make Imports of Preferable Goods:* A country's foreign exchange reserves ought to be boosted maintained, and used appropriately in accordance with national priorities for planned economic growth.²⁰⁸ By limiting unnecessary and wasteful import spending and promoting the flow of exports, exchange restrictions may assist in achieving economic growth.

Therefore, it can be noted that Ethiopia aims at achieving the above economic and social goals by restricting foreign exchange.

The NBE acknowledges its international obligation as an IMF member but holds on to the restrictions for the above reasons. According to the NBE Governor's Macroeconomic Advisor, *"Ethiopia has signed a membership agreement with the IMF obliging it to adhere to certain principles. These have to be adhered to just like any international agreements the country signs. Other IMF conditions are agreed upon during program negotiations for lending. Phased lending is used to ensure that the conditions in the lending agreement are fulfilled. There are regular meetings (usually twice a year) to review progress on the conditions of the program. These are mostly based on available information and data like national accounts, balance of payments data, or directives or laws to be changed entered in the agreement like changing the rules of certain markets. But given that foreign currency is a scarce resource in Ethiopia, there are restrictions on foreign currency."*

²⁰⁶ *ibid.*

²⁰⁷ *ibid* 14.

²⁰⁸ *ibid.*

Chapter Five: Conclusion and Recommendations

5.1. Conclusion

At the international level, the IMF is entrusted with the power to regulate the use of foreign currency. IMF's Articles of Agreement play a crucial role in the international foreign currency regime. The Articles of Agreement, inter alia, aim at liberalizing the foreign exchange regimes of member countries. As such, the IMF prohibits members from issuing foreign exchange-restricting measures. Ethiopia, as an IMF member, is obligated to adhere to the Articles of Agreement.

In Ethiopia, the NBE is mandated with overseeing the country's foreign exchange regime. Accordingly, it enacts different directives aimed at achieving the country's overall goals. However, these directives and measures impose restrictions on foreign exchange.

While the IMF tries to make sure that forex is accessible and transferable for international current transaction, it also provides an exception to take restrictive measures for balance of payment purposes. However, these measures need prior approval from the IMF and they need to be made provisionally.

Some of the restrictions on foreign exchange imposed by the NBE include:

- A. **Restriction on the allocation of foreign exchange for imported goods:** this measure impedes the availability of foreign exchange but it was imposed for balance of payment purposes; hence, it falls under the exceptions for Article VIII. However, Ethiopia didn't seek IMF's approval and there is no disclosed time limit for the measure.
- B. **Restriction on repayment of external loans and supplier's credit:** this affects the transferability of foreign exchange. Similarly, it was imposed for balance of payment purposes and it falls under the exceptions for Article VIII. However, IMF's approval was not obtained and there is no disclosed time limit for the measure.
- C. **restriction on foreign currency sales amount:** this also affects the availability of foreign exchange. Since, it was imposed for balance of payment purposes, it could also be justified as an exception for Article VIII. For this to happen, IMF's approval should have been obtained by Ethiopia and the measure should have been made for a disclosed provisional period.

Although they are not direct restriction of foreign exchange, requirements to surrender forex to central banks, uncertainty of forex legislation and foreign exchange tax also impedes may also impede international current transactions.

These unapproved exchange restrictions, which are also in violation of Ethiopia's responsibilities under Section 2(a) of Article VIII, are still in place. According to the authorities, there are no exchange limitations on payments made on the current account and that all current restrictions only apply to the capital account.²⁰⁹ But, this doesn't hold water as the IMF categorized that the transactions are not of a capital nature in its definition of current and capital transactions.

The IMF approached authorities in Ethiopia back in 2001 recommending that Ethiopia should accept the Article VIII obligations. The then authorities indicated that they intend to accept the obligations in the near future,²¹⁰ but 22 years later, Ethiopia still maintains these restrictions and appears inconsistent with the obligations under Article VIII.

Ethiopia is a beneficiary of the IMF. Access to information on economic policies of all member countries, the opportunity to influence members' economic policies, access to technical assistance in banking, fiscal affairs, and exchange matters, financial support in times of payment difficulties, and increased opportunity for trade and investment are few benefits among many others that Ethiopia is benefiting from being a member of the IMF. However, being an IMF member comes with the obligation not to impose restrictions on foreign exchange.

Non-compliance may entail immediate financial consequences that Ethiopia cannot afford given the poor economy and the negative impacts of the domestic war and Covid-19. Failure to adhere to obligations under Article VIII may also escalate to the denial of membership benefits, including initial ineligibility to utilize the resources of the IMF, followed by denial of different rights and, in the worst-case scenario, complete removal from membership.

²⁰⁹ IMF, '2019 Article IV Consultation and Requests for Three-Year Arrangement under the Extended Credit Facility and an Arrangement under the Extended Fund Facility—Press Release and Staff Report' (n 5) 19.

²¹⁰ International Monetary Fund (IMF), 'Ethiopia: 2002 Article IV Consultation and Third Review under the Poverty Reduction and Growth Facility Arrangement - Staff Report' (n 170) 20.

In addition to the above consequences, compliance with international financial standards may also be included as criteria in the terms of IMF and World Bank loans. Losing the financial trust will have an adverse impact on Ethiopia's ability to borrow money from these institutions and individual countries. It will also hinder Ethiopia's desire to join the WTO, which is an advocate for liberalized trade activities as opposed to restrictive and discriminatory measures.

The NBE and promoters of foreign exchange restrictions in Ethiopia argue that the measures are necessary to support the country's economy. According to some, the restrictions are beneficiary to Ethiopia in restoring the adverse balance of payments, protecting the value of the national currency, policy of differentiation, preventing capital flight, protecting domestic industries, conserving foreign exchange, and making imports of essential goods.

Overall, there are both positive and negative impacts to the NBE's measures restricting foreign exchange. From the theories of economics perspective, it is arguable to conclude either way. However, from a legal perspective, it is simply clear that Ethiopia is not in conformity with its international obligations. As the years go by, this may entail serious repercussions against Ethiopia as only a few countries are imposing foreign exchange restrictions and most of them don't have a good financial reputation. In addition to that, Ethiopia is among the highly benefited countries from the IMF system enabling it to access financial and technical support that the country badly needs.

5.2. Recommendations

It is established that Ethiopia imposes restrictions on foreign exchange and that these restrictions are not in conformity with the IMF's Articles of Association. Moving forward, the author recommends the following measures to address the issue at hand:

- ✓ Noting that the NBE's measures against the availability and transferability of forex for international current transactions were necessitated to stabilize Ethiopia's balance of payment, the measures are necessary and fall under the exception of Article VIII of the Articles of Agreement. However, Ethiopia needs to seek the IMF's prior approval before applying these measures. Therefore, it is recommendable that Ethiopia formally requests for the IMF's approval as per the appropriate procedural rules of the IMF.

- ✓ Ethiopia maintains its Article XIV-membership status, and believes that it is exempted from Article VIII. This assumption is wrong and should be rectified among the NBE officials since Article VIII applies to new measure taken by the NBE. Therefore, it is recommended that Ethiopia note its obligations under Article VIII before issuing new measures.
- ✓ In addition to getting prior approval from the IMF for necessary but restrictive measures, the NBE should project a timeline for the measures to achieve their purpose. The NBE seeks to address the balance of payment issues through these measures. Hence, it should impose the measures provisionally just to meet the purposes rather than making them permanent.
- ✓ The first Homegrown Economic Reform Policy simply emphasized instituting a mechanism where there are no controls on current account transactions (e.g. imports) and putting in place an exchange rate that reflects market fundamentals. While this was a good start, Homegrown Economic Reform Policy II, which is currently under development, shall address the issue of Ethiopia's restrictive foreign exchange regime.
- ✓ Ethiopia should consider implementing other measures to address the social goods aimed to be addressed through foreign exchange restrictions. The current measures are deemed restrictive and will not be acceptable by the IMF, the World Bank, and the WTO which promote trade liberalization.

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Interview:

- Interview with Tewodros Makonnen (Ph.D.), a Microeconomic Advisor to the Governor of the NBE (Addis Ababa, Ethiopia, 10 March 2022).

Appendices 1

Interview Questions – to an Expert

This Interview is prepared to collect information about the regulation of foreign currency under international financial law and its relevance in Ethiopia.

Part I: Introductory Questions

1. What's your full name?
2. What was your role at the National Bank of Ethiopia (brief background)?

Part II: Core Questions

1. What is the role and impact of the IMF in the Ethiopian financial regulation scheme?
2. What are the different mechanisms put in place by the IMF to ensure that Ethiopia and the NBE conform with the IMF's recommendations, Articles of Association, and other international financial regulations? (i.e., surveillance, regular meetings, reports, etc.)
3. In your opinion, is Ethiopia adhering to the IMF's Articles of Association and other financial regulations regarding the regulation of foreign currency? Please explain.
4. What is the economic rationale behind prioritizing foreign currency allocation to essential goods as it is practiced by the National Bank of Ethiopia (Directive No. FXD/77/2021)?
5. Do you think that the NBE has imposed unnecessary restrictions on foreign exchange? Please explain.
6. Is it advised to liberalize the foreign currency regulation scheme of a Country? Please explain.
7. As of March 2023, the NBE has issued more than 80 Directives on foreign exchange. Most of these Directives are amendments to previous Directives enacted within a small period of time. Do you find it necessary to enact these laws frequently as opposed to maintaining certain and relatively constant laws? What necessitated the frequent change?