AFRICAN DEVELOPMENT BANK GROUP

Interim Country Strategy Paper for Eritrea

2009-2011

OREB

September 2009

Table of Contents

Tables

List of Annexes

CURRENCY EQUIVALENTS

September 2009

Currency Unit	**=**	**Eritrean Nakfa (ERN)**
1 UA	**=**	**23.88 ERN**
1 UA	**=**	**1.566 US$**
1 US$	**=**	**15.25 ERN**

FINANCIAL YEAR

January to December

WEIGHTS AND MEASURES

Metric System

1 Kilogramme (kg) = 2.2 pounds (lbs)
1 metric tonne (MT) = 2,205 lbs

ACRONYMS AND ABBREVIATIONS

ADB	African Development Bank
ADF	African Development Fund
ASDP	Agricultural Sector Development Programme
APPR	Annual Portfolio Performance Review
BOP	Balance of Payment
BWIs	Bretton Woods Institutions
COMESA	Common Market for Eastern and Southern Africa
CPIA	Country Policy and Institutional Assessment
CPI	Consumer Price Index
CPRR	Country Portfolio Performance Review
CSP	Country Strategy Paper
CSOs	Civil Society Organizations
DHS	Demographic and Health Survey
DPs	Development Partners
DO	Development Objective
EEBC	Ethiopia-Eritrea Border Commission
EDPF	Eritrea Development Partner Forum
ERP	Emergency Reconstruction Programme
ESDP	Education Support Development Programme
ESW	Economic Sector Work
FDI	Foreign Direct Investment
FSF	Fragile State Facility
FSS	Food Security Strategy
FTZ	Free Trade Zone
GDP	Gross Domestic Product
GDI	Gender-related Development Index
GNI	Gross National Income
GoSE	Government of the State of Eritrea
GSP	Generalized System of Preferences
HDI	Human Development Index
HLC	High Level Consultation
ICSP	Interim Country Strategy Paper
ICT	Information and Communication Technology
IDPs	Internally Displaced Persons
IGAD	Intergovernmental Authority on Development
ILO	International Labour Organization
IMF	International Monetary Fund
IPRSP	Interim Poverty Reduction Strategy Paper
IRDP	Integrated Rural Development Programme
ITU	International Telecommunication Union
IP	Implementation Progress
IRDP	Integrated Rural Development Project
MDGs	Millennium Development Goals
MTDP	Medium Term Development Plan
NEPAD	New Economic Initiative for Africa
NGAP	National Gender Action Plan
NHP	National Health Policy
NPO	National Programme Office
NPV	Net Present Value
ODA	Overseas Development Assistance
PAR	Project-at-Risk
PIU	Project Implementation Unit

RBCSP	Results Based Country Strategy Paper
SSA	Sub-Saharan Africa
TB	Treasury Bills
TSZ	Temporary Security Zone
UA	Unit of Account
UNDP	United Nations Development Programme
UNFPA	United Nations Population Fund
UNHCR	United Nations Refugees Agency
UNICEF	United Nations Children Fund
UNMEE	United Nations Mission to Ethiopia and Eritrea
WHO	World Health Organization
WTO	World Trade Organization

Executive Summary

1.1 **Eritrea, one of the youngest nations in the world, gained its independence from Ethiopia in 1993 after 30 years of debilitating war.** The post independence period was characterized by rapid development in both social and economic fronts, but the border war with Ethiopia that erupted in 1998, lasting until 2000, reversed some of the gains that were made. Since then, the country has been suffering from macroeconomic imbalances and its trade activities, which were behind the strong economic performance during the post-independence period, have been badly disrupted. The situation has been made worse by the periodic drought problem given the country's dependence on rain. In the past eight years, annual crop harvest has oscillated from a high of 70-80 percent to a low of 20-30 percent of annual consumption needs, making the country vulnerable to food insecurity problems. In addition, the country has also been facing severe foreign exchange shortages making it difficult to meet all its import needs, thus forcing it to operate at low levels of capacity. On top of that, shortages of skilled manpower continue to hinder the country's ability to move fast on the growth trajectory.

1.2 **Despite all these challenges, the Government of the State of Eritrea (GoSE) has managed to improve its fiscal position through major cuts in defence spending and other expenditure rationalizing measures.** Efforts have also been made to improve public financial management and fiscal transparency, although the national budget is still not publically available. The GoSE has also undertaken measures to attract foreign investment, including the establishment of the free trade zone in Massawa, and also to resuscitate its mining industry. Already the GoSE has granted more than 17 mining licences to various foreign companies. Some, like Bisha, have advanced to actual work on exploration. Moreover, it has also been investing in infrastructure developments to promote domestic and external interconnectivity, so as to promote trade and improve the overall business environment. The construction of a new airport in Massawa is one of such activities. In addition, the GoSE has undertaken a number of measures to improve regional integration, which has resulted in the reduction of customs clearance time and the rolling out of the ASYCUDA[1] and its trade activities within COMESA has increased. On the social side, Eritrea is reported to be on track to achieve the Millennium Development Goal (MDG) goal 3 on gender equality and MDG goal 4 on child survival. Eritrea is also considered to be one of the Sub-Saharan African (SSA) countries with the best models of malaria control.

1.3 **To increase agricultural productivity, the GoSE is focusing on multifaceted programmes of transition to irrigation, through comprehensive water management programmes and increased use of essential inputs**. It has embarked on the programme of constructing micro dams and has put in place the programme of terracing and afforestation to control and contain environmental degradation and effects of climate change. And has also piloted a high speed wind farm in Assab, which is a model with a great potential for scaling up.

1.4 **For the past eight years, the GoSE has also invested a lot of resources in human capital development.** For instance, the country has managed to triple the enrolment rate in primary education from a very low base. The Government has also expanded access to tertiary education by opening seven new colleges and has established a hands-on management school in the country to increase the efficiency of the Civil Service and managers of Public Enterprises. The capacity of the Civil Service and the Office of the Auditor General has also been strengthened. Overall, the Government's policies are geared towards self-reliance, driven by the need to find own solutions to the challenges currently being faced by the country and it is within this context that the Bank continues to lend its support.

[1] The **Automated System for Customs Data** is a computerized system designed by UNCTAD to administer a country's customs.

1.5 **The coming into force of the ADF XI cycle has therefore presented the Bank with an excellent opportunity to prepare a new results based interim strategy for Eritrea.** Two previous attempts to present to the Board the 2006-2007 CSP and the 2007 CSP update failed because of the objections raised by the Government on the contents of these documents.[2] The last CSP to be approved by the Board in 2004 was the 2002-2004 Country Strategy Paper (CSP).[3] The focus of that CSP was on human resource development and was valid until 2006. The Education Sector Development Programme (ESDP) was the only project that was approved in 2004 following the approval of the last CSP for Eritrea and its objective was to contribute to increased access to quality education at basic and secondary level. The freeze on private construction between 2006 and 2008, delayed the execution of the construction component, although implementation is expected to accelerate now with the lifting of the freeze. Normally in Eritrea, once agreement is reached with the Government on the elaboration of the project, implementation tends to move fast.

1.6 **The new Interim Country Strategy Paper (ICSP) therefore reflects the continuation of the Bank's strategic response to the country's human resource development challenges and a natural progression to the tertiary level.** This is a priority for the GoSE since investment in education is seen as critical for achieving sustainable growth and poverty reduction. This is also in line with the Bank's own Medium Term Strategy 2008-2012, which has also identified 'Higher education, technology and vocational training' as one of its pillars. Therefore, the 2009-2011 ICSP strategy is anchored on one pillar, the **Promotion of Human Resources Developmen**t and will revolve around interventions that will help the GoSE address some of the challenges currently being faced in the tertiary education sector. The ICSP will cover the period of 24 months from its approval date. As for the GoSE's plans under ADF XII, the focus is likely to switch to agriculture given the importance of this sector in growth and poverty reduction.

1.7 **The Boards of Directors are, therefore, invited to consider and approve the proposed strategic response to the country's skilled manpower shortages as elaborated in the 2009-2011 ICSP.** It is recommended that the total ADF-XI grant allocation of UA 13.7 million be utilized to finance activities geared at ensuring sustained human resource development in Eritrea.

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[2] The draft ICSP was sent to the GoSE mid-September 2008 and it was finally in mid-May when detailed comments from the GoSE were received. In June 2009, the Government officially informed the Bank of the change in priority focus for ADF XI resources from financing the undersea fibre optic cable to financing activities in the higher education sector. The Bank mission was then launched during the first week of July 2009, where detailed discussions were held on the contents of the draft and agreement on both the nature of intervention as well as the contents of the draft ICSP. A mission to discuss the final draft would be launched upon the completion of the document.

[3] Reference ADB/BD/WP/2003/152-ADF/BD/WP/2003/191

ERITREA INTERIM COUNTRY STRATEGY PAPER 2009-2011

I. Introduction

1.1 **This results based 2009-2011 Interim Country Strategy Paper (ICSP) presents the Bank's strategic and selective response to development challenges currently facing Eritrea in the higher education sub-sector.** Specifically, the Bank Group's interim strategy seeks to assist the country address human resource challenges through activities that will contribute to the country's efforts to build the optimal level of human capital stock required to achieve sustainable growth. This is in response to the specific request from the Government of the State of Eritrea (GoSE) to the Bank for support in the area of higher education, which is also a priority area for both the GoSE and the Bank. For GoSE, this falls within the priority area on 'human capital development.' The other two GoSE priority areas include, 'food security and development of cash crops' and 'physical and social infrastructure.' The Government has been recruiting foreign teachers in order to temporarily address the problem of shortages of teachers for tertiary education and is now working towards strengthening its own internal capacity as it strives to achieve economic self-sufficiency. As for the Bank, support to higher education is one of the four priority areas identified in its Medium Term Strategy 2008-2012 (MTS). The decision to support this sector is also based on the Bank's own comparative advantage, its country knowledge and the existing policy framework. Therefore, the proposed interventions in tertiary education will be financed by the grant allocation UA13.7 million from ADF XI. In anticipation of the upcoming ADF-XII, the GoSE has already indicated that agriculture would be priority number one.

1.2 **The coming into force of the new ADF cycle has presented the Bank with an excellent opportunity to start afresh with a new results based interim strategy.** The ICSP will cover the period of 24 months from its approval date. The decision to prepare an interim strategy instead of a full CSP is based on the fact that the country's draft 5 Year National Development Plan is yet to be finalized. This ICSP will therefore facilitate the transition to a full CSP. It should be noted that since 2006 the relationship between the Bank and Eritrea has not been based on a valid CSP. Previous attempts to present the 2006-2007 CSP and the 2007 CSP update to the Board, in 2006 and 2007, respectively, did not bear results because of the objections that were raised by the GoSE on the contents of the CSP[4] and the last minute withdrawal of the Integrated Rural Development Project (IRDP), which was to accompany the 2007 CSP update. As a result, the country was not able to utilize its ADF X allocation of UA 14.3 million. Extra efforts have been made to ensure the acceptability of the ICSP to the Government.

1.3 **The last strategy to be approved by the Board, the 2002-2004 Country Strategy Paper (CSP)**,[5] approved on February 25, 2004, was based on the Interim Poverty Reduction Strategy (I-PRSP) of 2004. Consistent with the I-PRSP, the medium-term assistance strategy focused on human resource development, in particular support to basic education and was valid until 2006. In considering the Bank Group's strategy, the Board commended the authorities for beginning to refocus their efforts from post-conflict reconstruction to long-term development and poverty eradication, but expressed concern over high defence spending, lack of transparency in fiscal management, weak business environment as well as the strained relations with members of the international community. Although progress has been made to address some of these issues, as will be illustrated in subsequent sections, there is still room for further improvements. With the approval of the 2002-2004 CSP, Eritrea received UA18.63 million through the Education Sector Development Program (ESDP), approved in November 2004. The project is now progressing well, after delays in the construction of schools, caused by the construction freeze (2006-2008), and is scheduled to be completed in 2011.

II. Country Context and Prospects

2.1 Political, Economic and Social Context

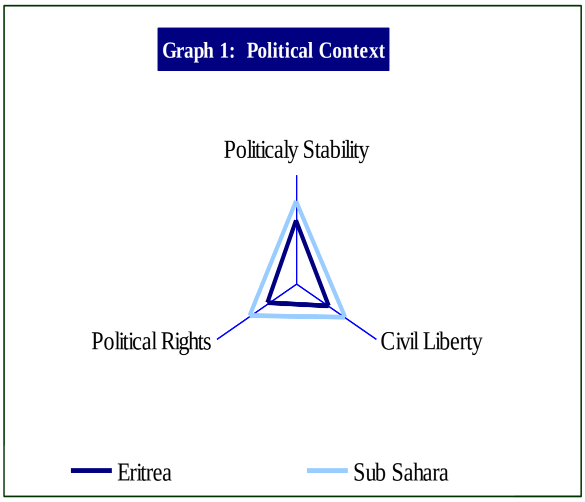
[4] Government was of the view that the document had not presented the country context correctly and that it contained factual errors and misconceptions.

[5] Reference ADB/BD/WP/2003/152-ADF/BD/WP/2003/191. It should be noted that the 2002-2006 CSP was not results focused, as it was prepared before the new results-based CSP format was approved.

Political Context

2.1.1 **The country's political landscape continues to be affected by border issues.** Thirty years of liberation struggle against Ethiopia and the 1998–2000 border conflict continue to influence and impact Government policies and institutions. As far as Eritrea is concerned, the border conflict was resolved in 2007 with the virtual demarcation by the Eritrea-Ethiopia Boundary Commission (EEBC). This was the remaining action that was needed following the issuance of its verdict in 2002, which was only accepted by Eritrea. Meanwhile, border tensions escalated between Eritrea and Djibouti following the brief skirmish along their border in June 2008. From the Government's perspective, the Djibouti issue is not a major one and believes that it can be resolved amicably and bilaterally.

2.1.2 **On domestic politics, the country continues to operate within a centralized one party political system, with the People's Front for Democracy and Justice (PFDJ) led Government**. While the national Constitution, ratified by a constitutional assembly in May 1997, enshrines the principle of political pluralism, the political parties' legislation is yet to be adopted by the GoSE. There have been no national elections since Eritrea became independent in 1993, but local elections continue to be held regularly (on bi-annual basis), involving community judges, local administrators etc. According to the assessment of the country's political situation by various governance surveys reflected in graph 1, the country appears to perform well below the SSA average in the three indicators assessed. However, this conclusion has been strongly disputed by the authorities. From their perspective, these do not reflect the reality on the ground since the country enjoys strong political stability and civil liberties.



Sources: AfDB Statistics Department, African Economic Outlook, 2008 and the WB, Governance Indicators

Economic Context

2.1.3 **The Eritrean economy remains largely managed with the Government active in most sectors.** Despite on-going efforts to promote more private sector participation in the economy, performance remains sub-optimal. The economy continues to suffer from the effects of the border conflict, the country's vulnerability to external shocks (i.e. recurrent droughts, fluctuation in world commodity prices) and the persistent foreign exchange shortages, which are fueling macroeconomic imbalances and hampering growth. Over the past five years Eritrea has registered a lackluster growth with real GDP growth averaging at 1% mainly due to poor agricultural performance from recurrent droughts and the overall low capacity utilization. This can be contrasted to the post independence period where the country registered robust growth in the region of 7%, in real terms.

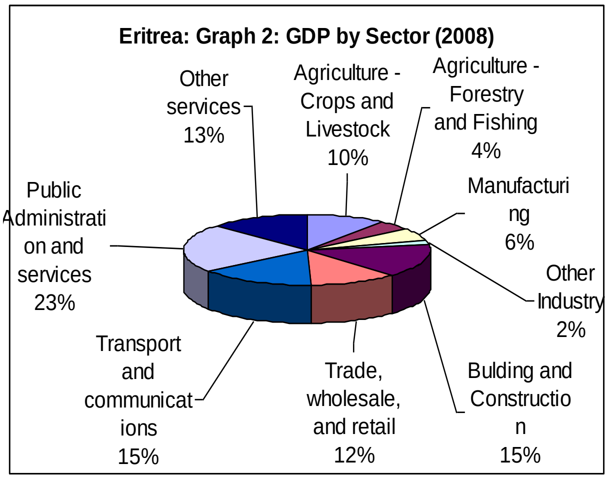
Economic Performance and Macroeconomic Management

2.1.4 **Despite the fact the economy is agriculture based, with about 70% of the population relying on this sector for income and employment,** the sector's contribution to GDP has been moderate largely due to recurrent drought, rudimental farming methods, and effects of war. The severe drought witnessed in 2008 resulted in a decline in cereal production to about 100,000 tons, which is well below the average national requirement of 650,000 tons per annum. As such, the sector's contribution to GDP fell sharply to 14.9% in 2008 from 24.3% in 2007 (see table 1 and graph 2). Other exogenous shocks that badly shook the economy that year included the sharp rise in food and fuel prices, whose combined effect resulted in a severe contraction in real GDP by 10% in real terms, from a positive growth of 1.4% in 2007.

Table 1: Sectoral Contributions

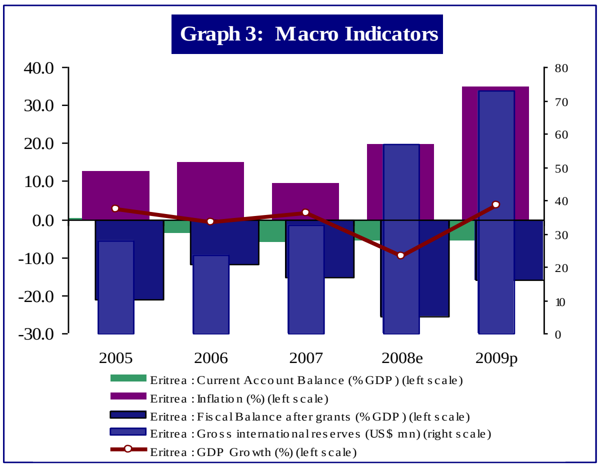
	2006	2007	2008 est.	2009 proj.	2010 proj.	2011 proj.
	(percent of GDP at current factor cost)					
Agriculture	24.6	24.3	14.9	20.5	21.0	21.0
Industry	19.9	20.7	23.1	21.7	21.7	22.2
Distribution Services	23.9	23.4	26.7	23.9	23.9	24.1
Other Services	31.7	31.5	35.4	33.8	33.5	32.8

Source: Eritrean Authorities



Source: AfDB Statistics Department, 2009

2.1.5 **Although the country's financial system is underdeveloped and not well integrated into the world financial system,**[6] it is likely to experience some relief from the fall in fuel and food import prices as well as some reductions in remittance inflows. It should be noted however that remittances have been on a downward trend even before the advent of the global financial crisis. For 2009, the IMF projects an improvement in real GDP growth of 3.6%, driven by the recovery in the agricultural production. With the expected commencement of production of cement from the new Cement factory in mid-2010 as well as the commence of production of gold from the Bisha mine expected in late 2010, growth prospects are more promising in the subsequent years.



Source: Economic Indicators: AEO, ADB Statistics Department, April 2009

2.1.6 **Major cuts in defense spending, salary freezes and the scaling down of capital projects and externally financed programmes are measures being applied by the GoSE to bring down the deficit in the fiscal balance.** Although the deficit still remains in double digits, the GoSE managed to bring it down significantly from 45% of GDP in 2000 to 15.3 % of GDP in 2007,[7] before widening again in 2008 to 25.4% of GDP (see graph 3).[8] Total revenue[9] is estimated to have shrunk to 18.2% of GDP in 2008 from 23% of GDP in 2006, reflecting a narrower tax base and reduction in economic activity. Whereas, expenditure is estimated to have shot up sharply to 39% of GDP in 2008 from 31% of GDP in 2006, largely due to the increased spending on food and fuel.[10]

2.1.7 **Meanwhile, credit to the economy (public and private sector) as a percentage of**

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[6] The financial system is dominated by local financial institutions.

7 Both revenues and expenditure have been on a downward trend in the recent past. Large military spending cuts saw a drop in the share of defense spending in GDP terms from 16.4% in 2005 to an estimated 10.0% of GDP in 2007.

8 Overall balance includes grants; primary balance is -27.7% of GDP and primary domestic balance is -16.9% estimated for 2008.

[9] Revenue excluding grants

[10] Domestically financed

broad money remains rather low, estimated at an average of about 16.7% in 2008 and 2009, compared to an average ratio of 78.9% of credit to the Government. Broad money is estimated at 15.9% in 2008, from 12.5% in 2007, reflecting some increase in narrow money as well as in deposits. Deposits continue to remain resilient despite the negative real interest rates. Reflecting both the sharp rise in food and fuel prices and a weakening fiscal position, inflation rose sharply to 19.9% in 2008, from 9.3% in 2007. For 2009, inflation is projected to accelerate sharply to 34.7%, reflecting significant monetary financing of the fiscal deficit.

2.1.8 **Government's financing needs continue to be a key driver of the country's monetary policy.[11]** Huge defense and social spending, immediately after the war, contributed to structural fiscal deficits. And since there has been little foreign financing, the deficit continues to be largely financed domestically through issuance of Treasury Bills (TBs) as well as borrowing from the central bank.[12] With TB rates set at artificially low levels (at 2.5% over the past five years and currently at 3%) and sharply rising inflation, the economy has operated in an environment of high negative real interest rates, adding to lower real GDP growth.

2.1.9 **To address some of the fiscal structural constraints, the GoSE has undertaken numerous measures recently to improve fiscal discipline**—including tight expenditure controls and the scaling down of defense outlays—as well as improve fiscal management and transparency. There have been some improvements in treasury operations, control measures are now in to control cash flows and balances and the budget has been aligned to the *Government Financial Statistics* (GFS) 2001 coding. Payroll has been computerized and customs and tax administration have been strengthened and revenue mobilization increased. Moreover, debt management capacity has also been enhanced. These notwithstanding, further fiscal adjustments and transparency will go a long way towards reducing the external imbalances and restoring fiscal sustainability.

2.1.10 **Significant reduction in transfers (private and official) since 2005 have been offset by reduction in imports.[13]** As a result, the deficit in the external current account has narrowed slightly from 6.1% of GDP in 2007 to 5.5% in 2008.[14] However, the persistent external deficit and the fixed peg exchange rate regime continue to exert pressures on the foreign reserves, which are now uncomfortably low, equivalent to just one month of imports of goods and services.[15] External imbalances, largely triggered by foreign exchange shortages, the fixed peg and high global market prices[16] are currently being managed by trade and foreign exchange restrictions. Specifically, import restrictions (prioritization of imports i.e. edible oil and food and payment of external obligations) have been introduced. The Government also introduced selective price controls on few food items (i.e. edible oil, sugar, cereals) to make food affordable and available to families based on need. Since there is little that is being exported, donor inflows and the inflows from the diaspora[17] now remain the country's main source of foreign financing.

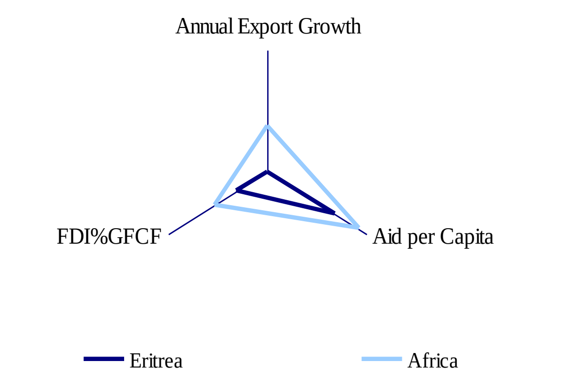
2.1.11 **Trade has been one of Eritrea's main economic activities, but its contribution to real GDP shrank with the cessation of trading activities with Ethiopia[18] at the ports of Massawa and Assab, and the introduction of trade restrictions.** The country has a narrow export base and relies heavily on imports. Foreign Direct Investment (FDI) inflows have also been quite low, but recently received a boost from FDIs to the mining sector.[19] Eritrea's mining industry remains small but is now poised to become a main growth driver and foreign exchange earner for the country. Its mineral resources include substantial reserves of barite, feldspar, kaolin, gold, potash, copper, zinc etc. It

[11] IMF Article IV Consultation Report, April 2008.
[12] Net external financing is estimated at 7.3 of GDP compared with domestic financing of 20.1% of GDP in 2008

[13] Exports and imports have been trending downwards since 2005, from 6.2% of GDP and 54.9% of GDP to 4.4% of GDP and 26.1% of GDP in 2008, respectively.
[14] IMF World Economic Outlook, April, 2009
[15] The exchange rate regime is a fixed peg, with Nakfa pegged to the US$ and since 2005 the rate is fixed at 1US$= Nakfa15.
[16] Prices for fuel, food and construction materials
[17] Private remittances accounted for about 26% of GDP in 2007.
[18] Ethiopia used to be Eritrea's main trading partner.
[19] The ratio of FDI as a percentage of gross fixed capital formation grew from -3.7% in 2004 to 1.4% in 2006 (UNCTAD, World Investment Report 2007).

is expected that with the commencement of production activities at the Bisha mine could contribute an additional one or two percent to the real GDP. Graphs 4 and 5, highlights key growth drivers and the trend in FDI.

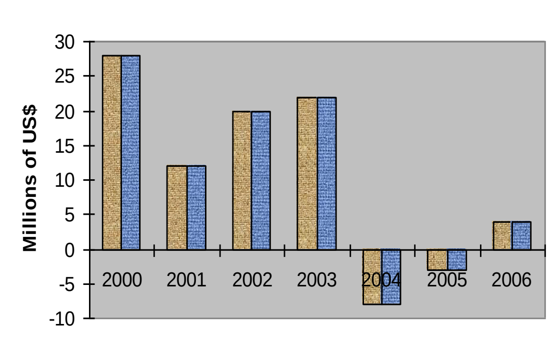
Graph 4: Key Growth Drivers, 2008



Source: AfDB Statistics Department

2.1.12 **The country's debt remains highly unsustainable, with the domestic debt at 114% of GDP and external debt at 62% of GDP as of end December 2008**. According the IMF, Eritrea has a high risk of debt distress, with most of its debt indicators above the HIPC threshold. The debt relief option under HIPC/MDRI is available, but its eligibility also requires having in place an IMF Staff Monitored Programme (SMP).[20] More external grant resources would be needed to ease pressures on domestic financing and hence domestic debt.

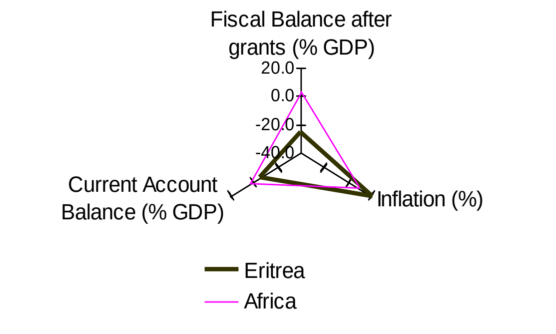
Graph 5 : FDI inflows to Eritrea



Source: UNCTAD World Investment Report 2008

[20] Eritrea has not yet indicated its readiness for the SMP.

Chart 6: Macroeconomic Management (2008)



Source: IMF Article IV Consultation Report and AfDB Statistics Department

Governance

2.1.13 **Transparency of public finance management remains limited in Eritrea, despite efforts being made to address it.** Since the national budget is not publicly available, the task of assessing the quality of public finance management remains difficult.[21] This notwithstanding, the moves towards decentralized governance are in place and now the Zobas have budgetary autonomy and authority to chart out and implement development policies and programmes specific to their regions.

Table 2: Governance Indicators for Eritrea, 2008	
Mo Ibrahim Index of African Governance	46.5 ranked 41st out of 48
Ease of Doing Business	171st out of 178
Corruption Perception Index	126th out of 180

Sources: www.moibrahimfoundation.org, www.transparency.org, www.doingbusiness.org,

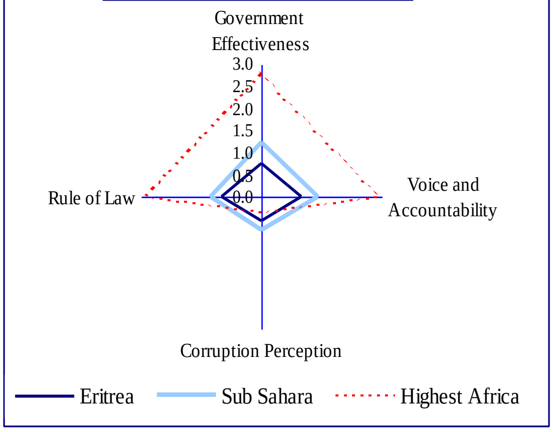
2.1.14 **Information from various global governance surveys point out to a down trend in the country's governance indicators** (see Graph 7 and table 2).[22]For instance, the Governance Matters 2009 reported some improvements in the country's governance indicators on political stability and control of corruption, but deterioration in the voice and accountability, rule of law, government

[21] Budget performance is available ex-post through the Article IV Consultation Reports.

[22] There are fundamental questions on the methodology used, validity and interpretation issues raised by the GoSE, which highlights some of the weaknesses associated with some of these global surveys.

effectiveness and the regulatory quality.[23] According to this survey, Eritrea fell below the 50 percentile rank in 2008. Moreover, the Transparency International Report ranks Eritrea 126th out of 180 countries surveyed, in the Corruption Perception Index (CPI) of 2008, above Ethiopia, Uganda, Kenya and Sudan. This being said, the GoSE has strongly expressed its reservation on the conclusions of these surveys and questioning their validity. From their perspective, there have been significant improvements in governance i.e. government effectiveness, the rule of law etc.

Graph 7: Governance (Score 0-3)

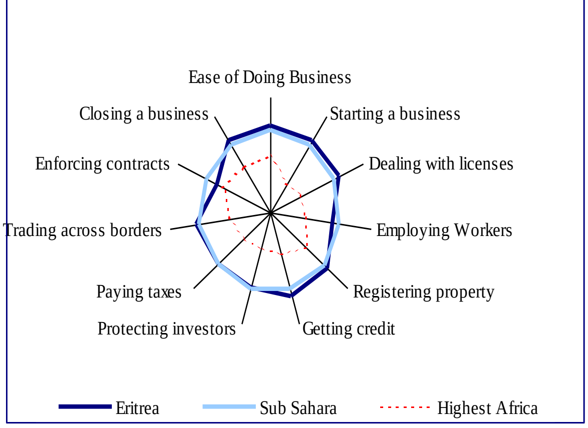


Source: AfDB Statistics Department using data from the WDI, WB, 2009

Business Environment and Competitiveness

2.1.15 **Investment climate continues to be affected by macroeconomic imbalances, inadequate infrastructure, and regional insecurity** *(see graph 6 and Annex II-B).* Moreover, the private sector remains small and underdeveloped operating in very difficult environment, with its activities undermined by foreign exchange shortages, payments system controls and imports restrictions. In addition, inadequate telecommunication services, shortages of skilled workforce and the underdeveloped state of the financial sector continue to affect the cost of doing business and the associated investment risks *(see box 1, graph 8 and* graph 9*).*[24] With prevailing high negative real interest rates, financial intermediation activities continue to be repressed with the implication that the country has been effectively dissaving. The GoSE has made some efforts to improve the business environment by increasing focus on infrastructure and on strengthening its human capital stock. The Government's development policy is firmly anchored on the need to promote trade and investment. Moreover, the GoSE has recently established an economic free trade zone (FTZ)[25] in Massawa and has issued several licenses for new mining ventures.

Graph 8 : Ease of Doing Business (Rank)



Source: AfDB Statistics Dept using data from Doing Business Databases, WB, 2008

2.1.16 **Eritrea still remains uncompetitive in the regional and global arena because of weaknesses in supply side responses, the fixed peg, and the overall business environment.** Moreover, the years of war have destroyed the country's basic economic and social infrastructures and have brought about the loss of skilled workforce.[26] Increasing domestic demands in the area of investment and trade are also exerting increasing pressure on the existing institutions. To date, however, efforts have been made to improve the road networks, rehabilitate the airports, sea ports and power plants as well as the telecommunication infrastructure. Moreover, efforts have been made to expand access to electricity and other social services (water, roads, schools, hospitals) in the rural areas. The Government has also exerted efforts to develop the human resources through higher education to push its economy on higher growth trajectory. This notwithstanding, there is still room for

[23] Kauffmann D., A. Kraay, and M. Mastruzzi 2009: Governance Matters VII: Governance Indicators for 1996-2008

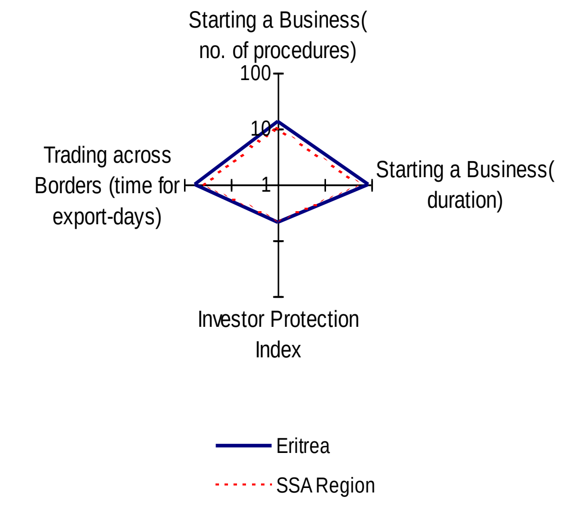
[24] Access to capital is said to be the greatest obstacle to business development in Eritrea

[25] A one-stop shop for investors.

[26] Eritrea is facing a shortage of manpower in both productive and non-productive sectors, partly affected by high national conscription.

improvement, especially in the country's business and institutional environment as well as the legal framework (see graph 9 below).[27]

Graph 9: Business Environment



Source: WB: Doing Business Databases, 2009

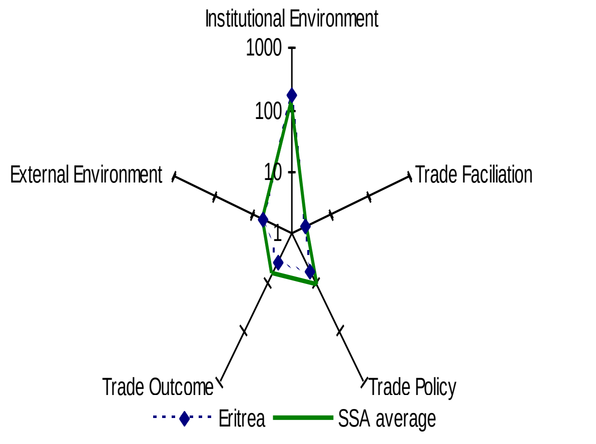
Box 1: Business Environment Assessment

Eritrea fared worse than its regional neighbours in the Doing Business and Country Credit Ratings in 2008, being ranked last globally (178) in the *Dealing with Licenses* indicator and the *Closing a Business* indicator in the 2009 Doing Business report. But doing better in Control of Corruption Index. Eritrea was also ranked in the bottom five globally in the *Starting a Business* indicator, with its overall rank of 171st (out of 178) in Doing Business. According to the 2009 Doing Business, Eritrea has been commended for undertaking positive reforms in the area of 'trading across borders.' In the 2007 Logistics Perception Index, Eritrea was also lagging behind the Sub-Saharan Africa (SSA) and low income group averages, ranked 124th (out of 150), with huge shipment delays as its main weakness (ranked 149th on the timeliness indicator).

Regional Integration and Trade[28]

2.1.17 **Eritrea actively participates in regional integration initiatives** and is a member of the COMESA, CEN-SAD, NEPAD, and is also a signatory to the 2001 trade agreement between COMESA and the United States.[29] Before suspending its membership in early 2007, Eritrea was also a member of the Inter-Governmental Authority on Development (IGAD). Despite being a beneficiary of the Generalized System of Preferences (GSP) with a number of industrialized countries, Eritrea has not been able to fully utilize the US and EU preferences, with a modest utilization rate of 54.7% due partly to low capacity utilization. Progress has, however, been made in the area of customs processing and clearance, with the time to clear goods cut down significantly at both the airport and Massawa port. The ASYCUDA system is also in the process of being rolled out. The country's trading activities with COMESA member states have increased significantly in recent years. However, the country's regional trade options and integration continue to be limited by complex regional relations. From the surveys on regional integration, Eritrea is not fairing well in most of the integration indicators compared with SSA average, with the exception of the regional indicator on 'external environment' (see graph 10).[30]

Graph 10: Regional Integration



Source: World Trade Index, World Bank 2007

Social Context

Poverty, Social Inclusion and Gender/Equity

2.1.18 **Eritrea is one of the poorest countries in the world.** GDP per capita is US$ 284 and it has a Human Development Index (HDI) ranking of 165th out of 182 countries surveyed in 2007.[31] Compared with SSA, Eritrea

[27] Eritrea is not among countries surveyed in the 2009 World Economic Forum's Global Competitiveness Index

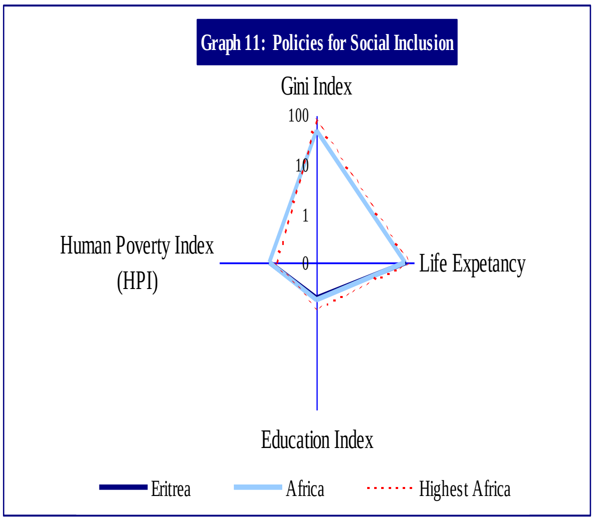
[28] 2008 Eritrea : Trade Brief, World Bank (WTI)

[29] Not a member of WTO and GATT.

[30] The GoSE has raised some fundamental questions on the methodology used, validity and interpretation issues, which highlights some of the weaknesses of these global surveys. Thus, their objections to the conclusions.

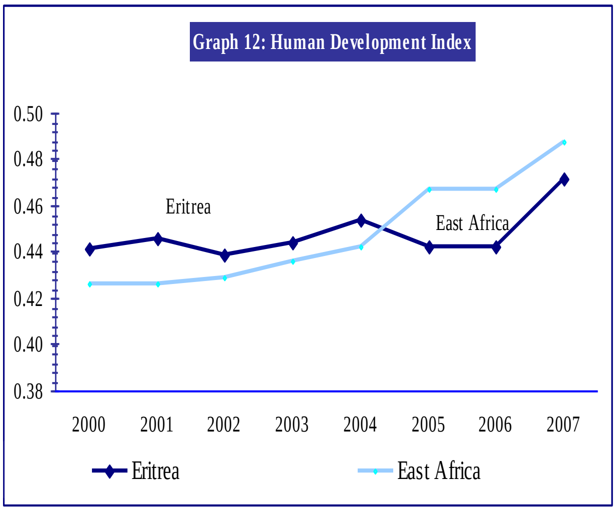
[31] 2009 Human Development Index, UNDP

is performing better on the life expectancy index (see graph 11), but lagging behind in HDI when compared with other East African countries (see graph 12). The country has an estimated population of about 4.8 million (2007), 70% of which living in rural areas. According to the 2009 Human Development Report, the country's population living below the national poverty line is estimated at an average of 53% between 2000 and 2006. Poverty has however not led to social exclusion per se as basic social services like health and education are available to all. War has also affected the family structures, with a large number of rural households being Female Headed Households (FHH).[32] Unemployment also remains high; most of it is disguised unemployment.



Source: AfDB Statistics Department using data from the UNDP Databases, 2008

2.1.19 **Eritrea happens to be one of the only three sub-Saharan countries that are on track to meet "Millennium Development Goal 4" child survival targets; and one of the seven countries to have managed to reduce child mortality by more than half.**[33] Based on the 2003 Demographic and Health Survey (DHS), health indicators reflect some improvement. Between 1995 and 2002 infant mortality rate decreased from 72 to 48 deaths per 1,000 and under-five mortality rate dropped from 136 to 93 deaths per 1,000.[34] In addition, the country has been able to reduce overall malaria morbidity by more than 86% and mortality due to malaria by more than 82%, making it one of the few countries in Sub-Saharan Africa to have met the Abuja "Roll Back Malaria" targets.



Source: DDP, ADB Statistics Department, 2009; UNAIDS; United Nations Population Division, 2008.

2.1.20 **Net enrolment rate in primary education has tripled from a very low base, but the education system is still facing many challenges.** Adult literacy rate remains low at 38.6% in 2006 vis-à-vis 43.3% for Africa and so is the gross primary school enrolment rate at 62.2% compared with 99.6% for Africa *(see annex IIa)*. **Gender equality** is also a concern in schools with 41% girls' enrolment in the middle and secondary school and 26% at higher education sub-sector in 2008/09. According to the 2009 Country Gender Profile (CGP),[35] there are increasing gaps between boys and girls enrolment particularly at higher levels of education in favour of boys. However, girls enrolment in the technical and vocational education has been growing and has now reached the GoSE's established quota of 30%.

2.1.21 **Eritrea has gone a long way towards achieving gender equity, given the importance of gender in poverty reduction efforts.** The GoSE is committed to promoting gender equality, as enshrined in the Constitution, and is making

[32] About 47% of the households.
[33] 2008 State of the World's children, UNICEF
[34] Lack of updated social sector data makes the task of evaluating progress difficult. The process to conduct a new DHS survey started in 2009 is expected to be completed in mid-2010..

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[35] The Country Gender Profile prepared by the Bank was completed in early 2009.

efforts to ensure women's empowerment.[36] According to the 2009 Human Development Report, 22% of seats in parliament in Eritrea were held by women and 18% of the Ministers are women. Despite all the challenges, Eritrea is on track with MDG 3 on gender equality.

Environment and Climate Change

2.1.22 **The GoSE accords environmental issues among the top priorities since the war and recurrent drought have caused immense damage to the environment.** As a result, the GoSE places environmental issues among the top priorities Eritrea is also extremely vulnerable to adverse effects of climate change mainly because of its least adaptive capacities and geographical location in the arid and semi-arid region of the Sahelian Africa.[37] To control and contain soil erosion and environmental degradation, terracing and afforestation programs as well as land reclamation and re-distribution policies were introduced and continue to be implemented. The GoSE has also constructed micro-dams in different parts of the country and has undertaken nationwide soil and water conservation activities, among others, as its response to the effects of climate change. In addition, there are on-going initiatives to set up high speed wind farms, with one already established in Assab. The Assab pilot is a model that needs to be replicated and possibly scaled up as a way to diversify energy sources in the country.

2.2 Strategic Options

2.2.1 Country Strategic Framework

2.2.1.1 **The country's policy, built on the strategy of self-reliance, aims to attain rapid, widely shared, sectorally and regionally balanced economic growth with macroeconomic stability and sustainable poverty reduction.** This objective is embedded in a number of the Government's policy and strategy documents listed in box 2, whose operationalization was affected by the 'no war no peace' situation that prevailed prior to the virtual demarcation by EEBC in 2007. While notable progress has been made in the infrastructure and social sectors, the poverty reduction and economic growth targets that were set in the 2004 Interim Poverty Reduction Strategy (IPRSP),[38] are a long way from being achieved.

Box 2: National Development Policies and Strategies

- The National Economic Policy Framework and Program (1998)
- Transitional Economic Growth and Poverty Reduction Strategy (2001)
- The Interim Poverty Reduction Strategy Paper (IPRSP) 2004
- The Food Security Strategy (FSS 2004)
- Education Sector Development Programme 2004-2015
- 2003 National Education Policy
- The National Water Supply Emergency Action Plan
- The 2003-2009 National Gender Action Plan (NGAP)
- National Health Policy
- Agricultural Development Programme 2009-2010

2.2.1.2 The Government is in the process of articulating a five year National Development Plan, which is expected to focus on the three priority areas already identified by the Government, that is (i) food security and development of cash crops, (ii) physical and social infrastructure and (iii) human capital development in the short to medium terms.[39] This plan will be reinforced, among others, by the existing policies and strategies in box 2 including the 2003 National Education Policy. The expected focus of the NDP is the appropriate one since these are critical areas that need to be addressed if the country is to move out of the vicious cycle of food insecurity and poverty. It is, however, not possible to assess the robustness of the Government's plans, its goals and targets in addressing macroeconomic imbalances, unemployment and private sector development, because of lack of relevant strategy documents.

2.2.2 Challenges and Weaknesses

[36] 2009 Country Gender Profile

[37] The main environmental challenges include continued deforestation, desertification, soil erosion, overgrazing, and significant land loss as a result of the presence of land mines.

[38] IPRSP was anchored on four pillars, namely (i) re-invigorating economic growth; (ii) creating income earning opportunities for the poor; (iii) enhancing access to and utilization of essential services for human development; and (iv) promoting political, economic and social participation of the population by putting in place the enabling environment.

[39] The process of preparing a five year Medium Term Development Plan (MTDP) is underway.

2.2.2.1 The Government is committed to alleviating poverty by creating food security, building up its infrastructure and boosting the stock of its human capital, but is facing multiple challenges.

- ***Low agricultural productivity and food insecurity:*** Given the country's vulnerability to recurrent droughts and reliance on rain-fed agriculture, Eritrea continues to face food insecurity. Even in good years Eritrea is not able to meet more than 70% of its national food requirements

- ***Restoring macroeconomic stability:*** Macroeconomic and structural imbalances continue to weaken the overall business environment as well as impact the country's competitiveness (see section 2.1). The main challenges that need to be urgently addressed include the persistently high fiscal deficit, unsustainable public debt, an overvalued exchange rate, and rising inflation..

- ***Shortages of skilled workforce:*** Shortage of appropriate human capital hinders Eritrea's development efforts. The country is facing serious shortages of skilled workforce, especially teachers for upper-schools and higher education institutions, and is currently relying on foreign teachers to fill the gaps, which is not sustainable.

- ***Shortage of foreign currency to boost business environment:*** Shortage of foreign exchange and lack of supplies (i.e. fuel, spare parts, construction materials etc) are crippling the economy, forcing it to operate at low capacity. Specifically, private households and business are facing difficulties in accessing foreign currency to meet their import needs. The fixed peg also continues to make the country uncompetitive, discouraging export and investment activities.

2.2.3 Strengths and Opportunities

2.2.3.1 Eritrea is a country with numerous potentials, which if exploited, could transform its growth dynamics.

- ***Strategic location****:* the country is easily accessible from Europe and the Middle and Far East and strategically located with its 1000 km coast along the Red Sea. Although transit trade with Ethiopia has ceased, the two ports, the Massawa and Assab, still have potential of becoming the country's foreign exchange earner, serving landlocked countries in the region. To facilitate this, efforts are currently being made to attract services investment to the port and shipment sectors as well as to the FTZ. The completion of the free-port in Massawa is expected to also give a boost to the export services, especially transport and logistics services.
- ***Transformation of Agriculture:*** Although this sector has been affected by years of war, recurrent drought and effects of climate change, it can be transformed into a modern high technology and high valued export products sector. The scope is also high for raising agricultural productivity through increased reliance on irrigation and improved farming methods and promotion of the livestock sector exports activities especially for the Middle East markets. Moreover, opportunities also lie in the production of high valued crops and vegetables for exports to Europe and Middle East.

- ***Fisheries****:* The country has a potential of catching up to 80,000 tons of fish annually, but currently is only able to catch up to 60,000 tons. Eritrea has started to export fish and sea cucumbers from the Red Sea on a small scale to markets in Europe and Asia. To facilitate the export of high valued perishable seafood, a new airport has also been constructed in Massawa and the Massawa port has been rehabilitated and is also being developed so as to be able to service the needs of the neighbouring countries as well and more investments in fishing equipments would be needed.

- ***Mining potential****:* Exploration activities conducted in various parts of the country during the last seven years confirm that Eritrea is one of the Volcanogenic Massive Sulfide (VMS) countries in the world. Eritrea has a large reserve of gold and also substantial reserves of potash, zinc, copper, silver, marble, barite, feldspar, kaolin and rock salt. The recent licensing of a number of mining concessions is expected to make the mining sector one of the main drivers of growth. For instance, the Bisha mining site is expected to yield 1.06 million ounces of gold, 10 million ounces of silver, 747 million pound of copper and more than 1 billion pounds of zinc over a 3-year life once production starts in 2011.[40]

- ***Tourism:*** The country's location at the Horn of Africa with its natural resources and rich historical sites and a close proximity to the European and Middle and Far Eastern market makes it an attractive tourist spot as well as strategic trade point. This sector has the potential of being a good source of foreign exchange earnings if well developed, but border issues would also need to be resolved.

- ***Off-shore oil and gas***: Although the country's full potential has not be exploited fully, it is reported that the country has a potential of producing up to 200,000 barrels/day.

2.3 Recent Developments in Aid Coordination/Harmonization and AfDB Positioning in the Country

2.3.1 **The GoSE is driving forward its development agenda and it is clear about the direction it wants to go.** In terms of donor coordination, the GoSE currently prefers to deal with development partners bilaterally rather than as a group, adopting a more focused approach in their cooperation with development partners.[41] In doing this, the Government seeks to ensure that there is minimal duplication of efforts and clear division of labour and a more balanced distribution of limited external resources to critical sectors of the economy. The Eritrean Development Partners' Forum (EDPF) established in 2007,[42] meets quarterly to share information on different development issues in and review implementation of individual interventions and is supported by Technical working groups. The GoSE does not participate in these meetings in view of its preference to hold bilateral meetings for programmatic issues. However, the Authorities have made it clear that the door for dialogue with the development partner group on broader policy and other regional issues was open.

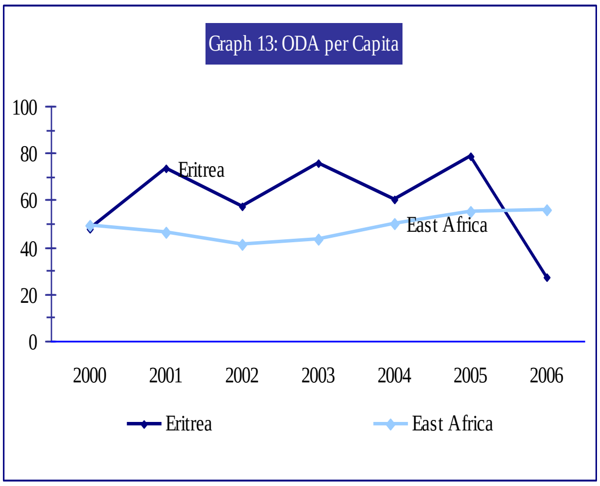
[40] Almost 1 million troy oz of gold are expected over the first two years of production at Bisha.

[41] The major development partners in Eritrea include the World Bank, AfDB, the European Union (EU), the UN System (UNDP, UNICEF, FAO, UNFPA, UNHCR, WHO, IFAD), Norway, United States, Italy, China. Active international NGOs include the Lutheran World Federation, Oxfam, among others.

[42] Currently co-chaired by the UN System and the EU.

Box 3: Development Partners' Activities	
Organization/Institution	**Current Programme and areas of Focus**
World Bank	**Operational Framework: FY** 2009-2010 Interim Strategy Note **Focus:** infrastructure (energy, port and telecommunication) and human capital development (health and education) **Funding:** US$ 70.73 million (IDA 15 2009/11
EU	**Operational Framework:** 2009-2013: Country Strategy Paper (under preparation) - Programme under 10th EDF **Focus:** food security/rural development- livestock production, marketing and pricing (€70 million), road infrastructure and regional connections (€30 million) and capacity building (€22) **Funding:** €122 million for six years
IFAD	**Operational Framework: Four year Plan** **Focus:** recovery and rural development --food security (crop and livestock production and irrigation components) **Funding:** Estimated allocation per year of US$ 15-16 million
UN System:	**Operational Framework:** 2007-2011 UNDAF **Focus:** social sectors (health, education, social protection) and agriculture (food security- fisheries, seed production, irrigation systems, water conservation) , IDPs and emergency reconstruction **Funding**: estimated at about US$34 million per annum
Norway	**Operational Framework:** 2009-2010 Strategy (under preparation) **Focus:** Development programme (capacity building, health and education) and political dialogue **Funding:** US$10 million per annum
IMF	**Operational Framework:** No Fund programme in place. **Dialogue:** 2009 Article IV Consultation Report.
Chinese	**Focus:** telecommunication, industry, education and agriculture (food security) **i)** Telecommunication project US$ 20 (2006) ii) Cement factory US$40 (2007)

2.3.2 On the programming side, development partners have successfully been collaborating among themselves in a number of areas through joint programming as well as co-financing. The Bank's co-financing of the Education Sector Development Programme with the World Bank and EU is such one example where the project is also being managed by one Project Management Unit (PMU). The Integrated Rural Development Programme (IRDP) was another initiative that would have brought together many donors, including the Bank, but was abandoned due to change in policy focus by the GoSE in early 2007. The preferred mode of financing by the GoSE is still direct project financing. In terms of the flow of Official Development Assistance (ODA),[43] graph 13 depicts declining trend, especially since 2005.[44] There has also been an outflow of international NGOs since the Government introduced new policies to govern their operations.[45]



Source: AfDB Statistics Department using data from the OECD Databases, 2008

Bank Group Portfolio

2.3.3 **The Bank Group operations in Eritrea have been geared towards assisting the country address challenges in the area of reconstruction and poverty reduction.** In terms of sectoral distribution, agricultural sector projects received the largest share (40%) of net commitments of UA76.3 million (equivalent to US$120 million) since 1992, followed by multi-sectoral projects (27%) and social sector projects

[43] Calculated on the basis of data on ODA and population from OECD-DAC (Organization for Economic Co-operation and Development, Development Assistance Committee) 2007. Correspondence on official development assistance disbursed.

[44] UNDP, Flows of aid, private capital and Overseas Development Assistance, Human Development Report Statistics.

[45] Now there are less than 10 International NGOs operating in the country.

(24%). Currently, there is only one on-going project, the Support to the Education Sector Development Programme- ESDP (UA18.6 million), whose implementation has been slowed by lack of progress in the implementation of the construction works due to the suspension of private construction activities between 2006 and 2008. As such, the disbursement remains rather low for the ESDP at UA 8.2 million, equivalent to 44% disbursement rate. Total disbursement as at end September 2009 was UA65.8 million, which is about 86.2% of the cumulative net commitments. Following the removal of restrictions over the construction industry and increased community base construction activities, the implementation of the project is expected to accelerate.

2.3.4 **The Bank is also providing support to the agricultural sector through the grant allocation of UA 2 million from the African Food Crisis Response, approved in February 2009.** Eritrea was one of the countries that was badly affected by the high food and fuel prices and as such became one of the beneficiaries of the Bank's Food Crisis Response. These resources are currently being used to purchase the much needed farm inputs including (i) seeds and pesticides with the objective of improving productivity of food crops and (ii) poultry farming inputs with the objective of increasing productivity of poultry farming. The procurement process has reached an advanced stage, with some of the items already being put into use in the current rainy season.

2.3.5 **Overall, the Bank portfolio in Eritrea has performed satisfactorily with the implementation progress (IP) and Development Objective (DO) ratings averaging at 2.1 and 2.4, respectively, despite implementation delays.**[46] These delays were clearly evident in the *Emergency Reconstruction Programme, a* multi-sector and multi-donor project, which instead of being completed within the original timeframe of three years; it was closed six years later due among others to the complex management of such projects. This notwithstanding, the ERP was successfully completed with encouraging results. Although the agricultural sector projects performed relatively well, they also took an average of nine years to complete (instead of six). The other remaining projects took an average of five years to complete. In terms of the global portfolio performance, as reflected in table 3, the Bank's portfolio in Eritrea performed better on the 'implementation and impact' criteria than in 'harmonization and alignment', when Bank-wide comparison is made. Similarly, when compared with the World Bank, the Bank did not fair well in the harmonization and alignment criteria, but performance was mixed on the implementation and impact.

Table 3: Portfolio Performance Indicators

Performance Indicators		2008	Bankwide	World Bank – Eritrea
Implementation and Impact	Project Cycle from Approval to Effectiveness (months)	13	11.7	
	Age (years)	5	15	5
	Disbursement Rate (%)	85	19	62.22
	Average Project Size (US$ M)	30	20.6	39.8
	Project-At-Risk PAR (%)	0	40	50
	Number of PIUs (% of total Portfolio)	100 (1 PIUs)	17.4	100 (6 PIUs)
Harmonization and Alignment	% Support relying on RMCs PFM and Proc. Syst	0	44 (2007)	0
	% Aid provided as Programme Based Approach	0	30 (2007)	1
	Number of co-financed projects	1	18.1	2
	Leader of Donor Working Groups in the Field	0	n/a	1
	Joint ESW and % of total ESW	0	44 (2007)	0

Sources: AfDB and World Bank

2.3.6 **Although no formal portfolio review has been undertaken in Eritrea**, common factors identified by both the Bank and Government in various Project Completion Reports as contributing to the slow implementation of projects were: (i) insufficient understanding of the Bank's procurement procedures; (ii) low threshold levels requiring Bank approval for small contracts; (iii) long delays on procurement and no objection request; (iv) frequent changes of Task Managers; (v) weak communication between the Bank, PIUs and GoSE; and (vi) short and inadequately staffed supervision missions. It should be noted that in Eritrea once agreements on the specifics of the project are reached usually the projects tend to

[46] Implementation ratings range from 0 (highly unsatisfactory) to 3 (highly satisfactory)

run smoothly-thus the better ratings (see annex I b). The Bank Group's Audit Report of May 2005 concluded that project management in Eritrea has improved in the areas of accounting, procurement and compliance with loan conditions. On the non-lending side, the Bank maintained dialogue with the GoSE on issues that were identified in the last CSP as well as on issues concerning project management and communication between the Bank and the GoSE with some success. The Bank was also able to prepare a Country Gender Profile, which was submitted to the Board during the first quarter of 2009.

2.3.7 Given the fact that there was no formal post CSP review for the previous CSP, the desk review of the operationalization of the previous CSP and the assessment of the failed attempts to prepare CSPs highlight the need to be more *flexible* to respond to the special needs of countries emerging out of conflict as well as the need to engage closely with the Government to gain country ownership and support. This also highlights the need for the field presence to ensure effective and continuous dialogue and efficient operationalization of Bank-financed projects and programmes. On the portfolio side, the Bank will also ensure that quality-at-entry for new interventions is high and that delays are minimized and problems resolved in a timely manner.

Box 4: Alignment of Eritrean Development Agenda and Bank Group's Proposed Strategy

Opportunities and Challenges	Government Development Priorities	Bank Group's Response
Opportunities • Transformation of Agriculture • Existing potential in off-shore fishing • Mining potential • Potential for tourism • Unexploited off-shore oil **Challenges** • State of regional instability • Weak business environment • Low agricultural productivity and food insecurity • Restoring macroeconomic stability • Rehabilitating and rebuilding infrastructure • Shortages of skilled manpower	**Overall development objective**: To attain rapid, widely shared, sectorally and regionally balanced economic growth with macroeconomic stability and sustainable poverty reduction. **Key Priority Areas** • Food security and development of cash crops • Physical and social infrastructure • Human capital development	**To support the country's effort to reduce poverty and promote sustainable growth through interventions that will seek to increase the stock of human capital through improved quality of higher education sub-sector.** **Pillar 1: Promotion of Human resource development.** • **Portfolio Overview by sector** (see below) • **Proposed New Interventions** (see below)
Short/Medium Term Objectives		
Long Term objectives	Poverty reduction and attainment of the MDGs.	

Portfolio Overview by sector

Sectors	UA millions	Status of on-going projects	Overall IP/DO rating
Agric sector	29.5	1	2.2/2.6
Multisector	20.8	None	2.3/3.0
Social sector	20.5	1	1.9/2.0
Transport	5.4	Cancelled	none
TOTAL	76.26		2.1/2.4

Proposed New Interventions

Sectors	ADF window (UA million)	Programmed
Education	13.7	2010

III. Bank Group Strategy for Eritrea

3.1 Rationale for Bank Group Intervention

3.1.1 **The rationale behind the proposed Bank Group's interventions in higher education is the need to help the GoSE improve the quality of its human capital critical for growth and poverty reduction.** Specifically, the Bank's strategy has been designed to respond to the shortages of skilled workforce through interventions in the higher education sub-sector. The Bank's planned intervention intends to support the GoSE's efforts to achieve self-sufficiency in human resource by producing the optimum level of skills needed to enable the country to maximize its growth potential as well as accelerate the process of reducing poverty. The proposed support for the development of the higher education sub-sector is also in line with the Bank's own priorities articulated in its Medium-Term Strategy, identifying higher education, technology and vocational training as one its priority area of support.

3.1.2 **Therefore, the strategy is going to be supported by one pillar: *Promotion of Human Resource Development*.** This presents the continuation of the Bank's support in the education sector, but at the next step, the tertiary level. As already indicated in section 2.2.2, the institutes of higher education are facing serious shortages of qualified teachers and only able to absorb a fraction of student graduating from high school. The development of this strategy has been guided by the Government's development priorities; the Bank's own comparative advantages and existing policy framework. Specifically, the strategy is supported by the existing national policy framework guiding the sector, that is, the 2003 National Education Policy and the Education Sector Development Programme 2004-2015. The planned intervention will be financed by the grant allocation of UA13.7 million from ADF XI. [47]

[47] The country's allocation under ADF-XI, which is grant, is the outcome of the Performance Based Allocation (PBA) exercise completed in early 2009 and is subject to change. The allocation was based on both the Country Policy and Institutional Assessment (CPIA) rating of 2.43 and the Governance Factor rating of 0.66.

3.2 Deliverables and Targets

It is envisaged that the new Bank programme will be supported by one new operation under ADF XI that is **Support to Higher Education Development** which is expected to contribute to the country's desire to be self-reliant in human resources.

Pillar: Promotion of Human Resource Development

3.2.1 **The GoSE considers education as being central to its economic development and therefore places the sector high on its development agenda**. After investing on health for over seventeen years, as part of the GoSE's programme of improving its human resources, the focus has now shifted to education. The education system is now focusing on access to the tertiary level since studies have shown that investment in higher education does lead to economic growth through improvements in labour productivity.[48] Specifically, the National Education Policy of 2003 highlights the government's commitment to the development of the sector as well as the critical role education plays in the country's socio-economic development. In the past eight years, the GoSE has pursued a decentralization strategy in the higher education system through the establishment of seven new institutions at various regions of the country; expansion of existing facilities; provision of distance learning to those who cannot access regular programs; and promotion of gender equity in the provision of tertiary education. It has also instituted a staff training program aimed at producing qualified staff to gradually replace the expatriate staff. As a result, transition to tertiary education has increased to about 23% in 2009, compared to 10-15% before the opening of these colleges.

3.2.2 **Lack of qualified teachers, insufficient absorption capacity of higher learning institutions and inadequate resources continue to act as impediments to the country's socio-economic transformation and the attainment of self-reliance in human resources**. Overcrowded classrooms at tertiary level and failure to produce sufficient marketable skills are the reflection of a mismatch between supply and demand as well as quality and relevance. Moreover, the shortage of qualified national staff remains a binding constraint and the government has been recruiting foreign teachers to augment the staff of the tertiary institutions. The pupil-classroom ratio at the Eritrea Institute of Technology (EIT) was reported to be at 1:90 in 2006, even with the double shift system (Rena, 2007). At present about 10,000 students are attending higher education institutions in the country and the total number of the faculty is 759. About 62% of the faculty staff are nationals and the remaining 38% are expatriate.

3.2.3 **The Bank's proposed intervention aims at contributing to efforts to improve the quality of higher education in Eritrea in a holistic manner**. Specifically, the proposed support in the higher education sub-sector will include provision of assistance in capacity building for teaching and research through staff development at the seven higher education institutions in the country, and the provision of technical assistance for these institutions in the areas where competencies are not currently available in the country; infrastructure development for teaching and research and support for the provision of teaching and learning resources at some of the institutions; assistance to faculty research activities and strengthening of the management capacities of the institutions. The project will also provide preferential treatment to female junior staff in the faculties for upgrading their skills. This will also complement the GoSE policy of preferential access to female secondary school graduates to higher education.

3.2.4 **At the moment, there are not many players in the tertiary sector**. China is currently involved in the extension work on the Teacher Training Institute (TTI) financed by the Bank, following the Government's decision to use the TTI as a College of Arts and Social Sciences. WHO has also been providing support to the College of Health Sciences. Meanwhile, the Government of India is supporting this sub-sector in the area of ICT (US$18 million), whereas, JICA is in the preliminary stages of identifying possible areas of support at the tertiary sector.

[48] Rena, Ravinder (2007) "Higher Education in Africa – A Case of Eritrea",

Table 4: Indicative Bank Programme for Eritrea for 2009-2011:

Project Title	Planned Board Date	Indicative Amount (in UA million)	Regions Covered
Human Resource development			
Support to Higher Education Development	2010	13.7 (ADF XI allocation)	nationwide
Total Programmed		**13.7 (UA m)**	

Source: AfDB database

Non-Lending Activities

3.2.5 **The Bank Group will also focus its engagement in the country on non-lending activities.** Economic and sector work (ESW) will enhance the Bank's advisory role and support the realization of the country's development agenda**.** The Bank will explore with the Government existing opportunities for analytical work with a view of coming up with an agreed plan of work. Possible sources of financing for the ESWs would also include bilateral and thematic Trust Funds.

3.2.6 **The monitoring of the ICSP will be through regular consultations with the Government.** The performance indicators selected in this ICSP will facilitate the monitoring of ICSP outputs and outcomes. The Bank's dialogue missions as well as the ICSP completion report will be used as tools to assess how far the Bank's interventions have contributed to the intended results.

3.3 Country Dialogue Issues

3.3.1 **Need to improve the accessibility and availability of data:** Given the data accessibility and availability problem—with no publication and dissemination of national statistics and data, the Bank will continue to engage the GoSE on the importance of having good timely data and the legal framework to facilitate its publication and dissemination for effective poverty reduction. The Bank will be ready to provide capacity building support if requested.

3.3.2 **Need to improve the business environment and governance for private sector growth.** Given the needs for further improvement in the current environment for private sector development and growth, the Bank will continue to dialogue with GoSE on the need to undertake reforms to address some of the barriers to private sector development, competition and foreign investment.

3.3.3 **Possible areas for Studies or Economic and Sector Work (ESWs):** The Bank will continue to engage in discussion with the GoSE on the importance of such analytical work for knowledge building and the deepening of policy analysis.

Box 5: ICSP Preparation Process

The ICSP has been prepared using a participatory approach, with full involvement of GoSE, and development partners. The preparation process started with the High Level Consultation Mission (HLC) in March 2008, which held consultations with officials from Government ministries and agencies, representatives from donor community in Eritrea and the private sector. This was then followed by the ICSP preparatory mission in June 2-6, 2008, where meetings were held with officials from the GoSE sectors specifically involved in the ICSP as well as those from international agencies, and organizations including the NGOs.

The draft ICSP was sent to the GoSE mid-September 2008, but due to concerns raised by the GoSE regarding the contents in the draft report, the process was put on hold. It was finally in mid-May 2009 when the Bank received detailed comments from the GoSE. In June 2009, the Government officially informed the Bank of the change in priority focus for ADF XI resources from financing the undersea fibre optic cable to financing activities in the higher education sector. The Bank mission was then launched during the first week of July 2009, where detailed discussions were held on the contents of the draft and agreement on both the nature of intervention as well as the contents of the draft ICSP. A dialogue mission was undertaken in mid-September 2009 and the document was discussed and eventually cleared. The clearance was through a formal letter to the Bank dated September 30, 2009.

3.4 Potential Risks and Mitigating Measures

3.4.1 **Macroeconomic risk:** Although temporary measures have been put in place to address the foreign exchange shortages and revenue shortfall, they do not address the underlying causes of scarcity for foreign exchange and structural deficits. Therefore, further fiscal adjustments will be required to restore fiscal and debt sustainability and reduce internal and external imbalances. The IMF had expressed willingness to work with the GoSE on fiscal adjustments and structural reform measures, but the GoSE is currently not ready to enter into a programme with the Fund.[49] So the Bank will continue to dialogue the GoSE on the need to

[49] 2008 Article IV Consultation report for Eritrea

address those structural issues to ensure effectiveness of its support.

3.4.2 **Weak Capacity for Project management:** To minimize this risk, the Bank will organize regular training events for project coordinators, staff, and other government officials involved in procurement and disbursement activities. This will ensure gradual building up of capacity for project management. This will be enhanced by the inbuilt capacity building activities anticipated in the new operations

3.4.3 **Risk of falling in chronic arrears with the AFDB:** The risk of the arrears situation becoming a chronic problem is high, with the country being in and out of sanctions and its related effect on disbursement activities. Recent improvements in debt management and the expected increase in foreign exchange from the Bisha mine should minimize this risk. The Bank will work closely work with the GoSE to find sustainable solution to this problem.

IV. Conclusion and Recommendations

Conclusion

4.1 **The country faces many challenges. Support from development partners, including the Bank would be critical to achieving he GoSE's socio-economic objectives.** The GoSE has been using its meagre resources to improve basic social services, service delivery, and invest in human and physical capital in the country. These efforts continue to be undermined by shortages of skilled manpower, foreign exchange shortages, recurrent drought and persistently high fiscal deficit. The proposed Bank's strategy for the period of 2009-2011 ICSP aims at contributing to the country's efforts to build the capacity of the higher education institutions needed to produce the required stock of human capital necessary for economic growth and poverty reduction. The proposed interventions would be anchored on the pillar on Promotion of Human Resource Development.

Recommendation

4.2 **The Boards of Directors are invited to consider and approve the proposed strategic response to the country's challenges in higher education elaborated in the 2009-2011 ICSP.** It is recommended that the total grant allocation under ADF-XI of UA 13.7 million be utilized to finance activities geared towards enhancing human resource development.

http://www.reliefweb.int/

Annex I (A) CSP Results-Based Framework					
Country Development Goals(PRSP/NDP)	**Issues hindering the achievement of Country Development Goals (= sector issues)**	**FINAL OUTCOMES (expected by the end of 2013)**	**INTERMEDIATE OUTPUTS (expected by the end of 2011)**	**FINAL OUTPUTS (expected by the end of the ICSP in 2013)**	**ADB Interventions expected to be ongoing during the ICSP period (new and ongoing)**
Pillar: Promoting Human Resource Development					
Higher Education Sector					
Human resource development through increased access and equity and improved quality of tertiary education	•Shortage of qualified national higher education staff •Inadequate teaching and learning resources •Inadequate infrastructure for teaching and research	• Increased number of students attending higher education institutions: Increase transition to higher education from the 23% in 2009 to 30% by 2013 •Improved quality of higher education and increase knowledge of students: Build adequate capacity for teaching and research at the higher education institutions by 2013.	• Increase the number of qualified national staff from 40% of staff to 60% • Upgrade infrastructure of 2 higher education institutions (50%) • Provide teaching and learning materials to 2 higher education institutions (50%)	• Increase the number of qualified national staff from 60% of staff to 80% • Upgrade infrastructure of 2 higher education institutions (100%) • Provide teaching and learning materials to 2 higher education institutions (100%)	**Project 1: Support to Higher Education Development (UA 13.7 UA) – New. ADF XI operation for 2010**
	•Low participation of females in higher education institutions	•Reduced inequities in the provision of higher education: Increase the proportion of female students in higher education institution from 26% in 2009 to 40% by 2013	• Maintain the policy of preferential access to higher educations in favour of female secondary school graduates	• Maintain the policy of preferential access to higher education in favour of female secondary school graduates	
	• High dependence on expatriate expertise in the staffing of higher education institutions	•Increased sustainability of the higher education system by 2013	• Increase proportion of higher education staff that are nationals from the 62% in 2009 to 70%	• Increase proportion of higher education staff that are nationals from the 62% in 2009 to 90%	

Basic and Secondary Education Sector					
Increase proportion of the population with basic literacy and higher levels of skills to achieve EFA and MDGs	•Shortages of class rooms •Low completion rate •Gender inequality •High illiteracy rates	Contribute to an increased access to quality education	537 classrooms for elementary, middle and secondary schools constructed and equipped; 2 secondary schools rehabilitated; 2 hostels for girls constructed; textbooks, sports and fine arts equipment supplied to the 19 primary and 15 middle schools; 20 secondary schools equipped with science laboratories and 20 with workshops and computer laboratories; 50 secondary schools provided with reference/library books; 400 primary school teachers trained; 450 secondary school teachers recruited; 90 Ministry of Education staff trained	537 classrooms for elementary, middle and secondary schools constructed and equipped; 2 secondary schools rehabilitated; 2 hostels for girls constructed; textbooks, sports and fine arts equipment supplied to the 19 primary and 15 middle schools; 20 secondary schools equipped with science laboratories and 20 with workshops and computer laboratories; 50 secondary schools provided with reference/library books; 400 primary school teachers trained; 450 secondary school teachers recruited; 90 Ministry of Education staff trained	**Project 3: Support to the Education Sector Development Programme – UA 18.63 million (on-going)**

Annex I (B) Performance Indicators per Sector

Identification	Implementation and Impact									Harmonization			
	Financial Performance			Risk			Rating *			Project Design			
Project Name	Amount Approved (UA m)	Amount Disbursed (UA m)	% Disbursed	Projects at Risk	Amount	Age (years)	Implementation Progress	Impact on Development	Overall Assessment	Average size	Relying on Gov PFM and Proc	PIU	Co-financed Projects
Agriculture and Rural Development	**30.02**	**29.5**	**100%**							**10**	**0**	**3**	**0**
Central Highlands Irrigated Horticulture Development	8.5	8.22	100%			8.2	2.36	2.75	2.56				
National Livestock Development	10.02	10.02	100%			8.1	2.08	2.5	2.29				
Fisheries Infrastructure Development	11.5	11.26	100%	33.3	11.5	7.1							
Multisector	**20.97**	**20.84**	**100%**							**10.5**	**0**	**1**	**1**
Emergency Reconstruction Programme	19.9	19.9	100%			6	2.23	3	2.62				
Economic and Financial Management Programme	1.07	0.94	100%			4.5	2.33	3	2.67				
Urban Development	**1.93**	**1.85**	**100%**							**1.93**	**0**	**0**	**0**
Asmara Infrastructure Development Study	1.93	1.85	100%			7	2	1.75	1.88				
Social	**18.63**	**8.20**	**44%**							**18.63**	**0**	**1**	**1**
Support to Education Sector Development	13.6	3.17	23.3%			**4.5**	1.75	2	1.88				
Support to Education Sector Development	5.03	5.03	100%			**4**	2	2	2				
Transport	**6.5**	**5.43**	**100%**							**5.53**	**0**	**1**	**0**
Barentu - Omhajer Road Study	0.97		0%				N/R	N/R	N/R				
Recovery and Rehabilitation Programme for Eritrea	5.53	5.43	**100%**			4.6							
Overall Assessment	**78.05**	**65.83**	**86.23%**	**33.30%**	**11.5**	**5.9**	**2.1**	**2.4**	**2.3**	**9.3**	**0**	**6**	**2**

Notes: *Portfolio Performance Ratings: 0 = Highly unsatisfactory; 1 = Unsatisfactory; 2 = Satisfactory; 3 = Highly satisfactory

Source: AfDB database

Annex I (C) Bank Group Operations Eritrea, 31 July 2009

Project Name	Window	Amount Approved (UA)	Date Approved	Date Signed	Date Effective	Last Disburs.	Amount Disbursed (UA)	Amount Cancelled (UA)	Net Commitment (UA)	% Disbursed	Status
Agriculture and Rural Development											
Central Highlands Irrigated Horticulture Development	ADF	8,500,000.00	12-Dec-96	29-May-97	29-Sep-98	20-Oct-04	8,217,881.75	282,118.25	8,217,881.75	100%	Completed
National Livestock Development	ADF	10,024,000.00	19-Nov-97	16-Feb-98	17-Sep-98	6-Sep-06	10,024,000.00	-	10,024,000.00	100%	Completed
Fisheries Infrastructure Development	ADF	11,500,000.00	19-Nov-97	16-Feb-98	24-Nov-98	19-Jul-06	11,261,557.90	-	11,261,557.90	100%	Completed
Sub-total		**30,024,000.00**					**29,503,439.65**	**282,118.25**	**29,503,439.65**	**100%**	
Multisector									-		
Emergency Reconstruction Programme	ADF	19,900,000.00	10-May-01	30-May-01	16-Aug-01	31-Dec-07	19,900,000.00		19,900,000.00	100%	Completed
Economic and Financial Management Programme	TAF	1,070,000.00	17-Jun-98	6-Apr-99	7-Apr-00	22-Jul-03	944,750.11	125,249.89	944,750.11	100%	Completed
Sub-total		**20,970,000.00**					**20,844,750.11**	**125,249.89**	**20,844,750.11**	100%	
Urban Development											
Asmara Infrastructure Development Study	TAF	1,930,000.00	14-Dec-00	5-Feb-01	2-Jun-03	30-Mar-07	1,853,741.06	76,258.94	1,853,741.06	100%	Completed
Social									-		
Support to Education Sector Development	ADF	13,600,000.00	10-Nov-04	2-Mar-05	30-Jun-05	31-Dec-09	3,170,000.00	-	13,600,000.00	23.3%	Ongoing
Support to Education Sector Development	TAF	5,030,000.00	10-Nov-04	2-Mar-05	30-Jun-05	31-Dec-09	5,030,000.00	-	5,030,000.00	100%	Ongoing
Sub-total		**18,630,000.00**					**8,200,000.00**	**-**	**18,630,000.00**	**44%**	
Transport									-		
Barentu - Omhajer Road Study	TAF	970,000.00	5-Nov-97	16-Feb-98			-	970,000.00	-		Cancelled
Recovery and Rehabilitation Programme for Eritrea	ADF	5,530,000.00	11-Sep-96	8-Nov-96	24-Nov-97	9-Mar-01	5,430,000.00	**100,000.00**	5,430,000.00	**100%**	Completed
Sub-total		**6,500,000.00**					**5,430,000.00**	**1,070,000.00**	**5,430,000.00**	**100%**	
GRAND TOTAL		**78,054,000.00**					**65,831,930.82**	**1,553,627.08**	**76,261,930.82**	**86.2%**	

Sources : ADB database

Annex II (A) Comparative Socio Economic Indicators

	Year	Eritrea	Africa	Develo-ping Countries	Developed Countries
Basic Indicators					
Area ('000 Km²)		118	30 323	80 976	54 658
Total Population (millions)	2008	5	985.7	5 523.4	1 226.3
Urban Population (% of Total)	2008	20.8	39.2	44	74.4
Population Density (per Km²)	2008	42.6	32.5	23	49.6
GNI per Capita (US $)	2007	230	1 226	2 405	38 579
Labor Force Participation - Total (%)	2005	49.6	42.3	45.6	54.6
Labor Force Participation - Female (%)	2005	47.5	41.1	39.7	44.9
Gender -Related Development Index Value	2006	0.428	0.482	0.694	0.911
Human Develop. Index (Rank among 174 countries)	2006	164	n.a.	n.a.	n.a.
Popul. Living Below $ 1 a Day (% of Population)*	2005	36	38.7	…	…
Demographic Indicators					
Population Growth Rate - Total (%)	2008	3.1	2.3	0.3	1.2
Population Growth Rate - Urban (%)	2008	5.3	3.3	2.5	0.5
Population < 15 years (%)	2008	43	40.9	16.6	27.4
Population >= 65 years (%)	2008	2.4	3.4	16.7	8
Dependency Ratio (%)	2008	83.3	79.5	47.7	53.9
Sex Ratio (per 100 female)	2008	96.5	99.3	94.3	101.5
Female Population 15-49 years (% of total population)	2008	24.8	24.2	24.3	25.8
Life Expectancy at Birth - Total (years)	2008	58.5	54.5	76.7	67.5
Life Expectancy at Birth - Female (years)	2008	60.6	55.6	67.5	80.3
Crude Birth Rate (per 1,000)	2008	38.5	35.7	11	20.1
Crude Death Rate (per 1,000)	2008	9	13	10.4	8.6
Infant Mortality Rate (per 1,000)	2008	54	83.9	7.1	48.5
Child Mortality Rate (per 1,000)	2008	74.9	137.4	8.8	72.3
Total Fertility Rate (per woman)	2008	4.9	4.6	1.6	2.5
Maternal Mortality Rate (per 100,000)	2005	450	683	450	9
Women Using Contraception (%)	2002-06	8	29.7	61	75
Health and Nutrition Indicators					
Physicians (per 100,000 people)	2004	4.9	39.6	78	287
Nurses (per 100,000 people)	2004	57.5	120.4	98	782
Births attended by Trained Health Personnel (%)	2002-06	28.3	51.2	59	99
Access to Safe Water (% of Population)	2006	60	64.3	84	100
Access to Health Services (% of Population)*	2004	…	61.7	80	100
Access to Sanitation (% of Population)	2006	5	37.6	53	100
Percent. of Adults (aged 15-49) Living with HIV/AIDS	2007	1.3	4.5	1.3	0.3
Incidence of Tuberculosis (per 100,000)	2006	94	315.8	275	19
Child Immunization Against Tuberculosis (%)	2007	90	83	89	99
Child Immunization Against Measles (%)	2007	80	83.1	81	93
Underweight Children (% of children under 5 years)	2003	73	25.2	27	0.1
Daily Calorie Supply per Capita	2004	1 465	2 436	2 675	3 285
Public Expenditure on Health (as % of GDP)	2005	1.7	2.4	1.8	6.3
Education Indicators					
Gross Enrolment Ratio (%)					
Primary School - Total	2006	62.2	99.6	106	101
Primary School - Female	2006	55.6	92.1	103	101
Secondary School - Total	2006	31.1	43.5	60	101.5
Secondary School - Female	2006	23.3	40.8	58	101
Primary School Female Teaching Staff (% of Total)	2006	42.7	47.5	51	82
Adult Illiteracy Rate - Total (%)	2003	...	38	21	1
Adult Illiteracy Rate - Male (%)	2003	...	29	15	1
Adult Illiteracy Rate - Female (%)	2003	...	47	27	1
Percentage of GDP Spent on Education	2006	5.3	4.5	3.9	5.9
Environmental Indicators					
Land Use (Arable Land as % of Total Land Area)	2005-08	4.9	6	9.9	11.6
Annual Rate of Deforestation (%)	2000-08	0.3	0.7	0.4	-0.2
Annual Rate of Reforestation (%)	2000-08	…	10.9	…	…
Per Capita CO2 Emissions (metric tons)	2005-08	0.1	1	1.9	12.3

Sources : ADB Statistics Department Databases; World Bank: World Development Indicators; UNAIDS; UNSD; WHO, UNICEF, WRI, UNDP; Country Reports
Note : n.a. : Not Applicable ; ... : Data Not Available;

Annex II (B) Table of Economic and Financial Indicators, 2005-2009

	2005	2006	2007	2008 est.	2009 proj.
	(Annual rate of change, percent, unless stated otherwise)				
National Income and Prices					
GDP at constant market prices	2.6	-1	1.4	-9.8	3.6
Nominal GDP at market prices	10.4	10.3	8.8	4.7	35.7
GDP deflator	7.6	11.4	7.3	16.1	31.0
Consumer Price Index, period average	12.5	15.1	9.3	19.9	34.7
Consumer Price Index, end of period	18.5	9.0	12.6	30.2	30.2
Nominal GDP at market prices (million Nakfa)	16,880	18,622	20,264	21,220	28,801
External Trade					
Export of goods and services, f.o.b	5.7	23.4	-9.0	-19.6	-23.6
Imports of goods and services f.o.b	-9.0	-23	-18.3	-4.9	-0.8
Real Effective Exchange rate (annual ave) 1/	26.7	11.7	0.2	8.4	…
Nominal Effective Exchange Rate (annual average) 1/	15.2	-1.5	-5.9	-2.2	…
Money and Credit					
Net foreign assets 2/	-5.3	-1.9	-1.6	3.0	2.3
Net Domestic assets 2/	16.0	7.6	13.7	12.9	9.3
Credit to the government 2/	11.5	7.4	11.1	14.4	9.3
Credit to the economy 2/	3.5	0.5	-2.8	1.1	1.6
Broad Money	10.7	5.7	12.1	15.9	11.7
Interest Rates (savings deposits, %)	4	4	4	4.0	…
	(Percent of GDP)				
Central Government Operations					
Total revenue and grants	35.3	27.1	25.3	21.0	15.7
of which: grants	9.3	4.1	3.1	2.8	2.6
Expenditure and net lending	56.5	39.1	39.6	46.4	31.6
of which: externally financed expenditures 3/	16.7	8.4	5.9	7.7	5.0
Overall fiscal balance (incl. grants)	-21.2	-12.0	-15.3	-25.4	-15.9
Financing	21.2	12.0	15.3	25.4	15.9
Domestic 4/	16.6	8.1	10.7	18.1	10.3
External	4.6	3.9	4.6	7.3	5.7
Primary domestic balance	-10.7	-4.5	-9.3	-16.9	-9.7
	(Percent of GDP, unless state otherwise)				
Balance of Payments					
Current account (incl. official transfers)	0.3	-3.3	-6.1	-5.5	-5.6
Overall balance of payments	-8.7	-1.8	-2.0	3.0	2.3
Gross international reserves (US$ millions)	27.7	23.6	32.4	56.7	73.1
(months of imports of goods and services)	0.7	0.7	1.1	1.9	2.2
	(Percent of GDP, unless state otherwise)				
Public Debt 5/					
Central government domestic debt	93.7	93.8	99.2	114.8	94.5
External public debt	63.9	59.3	58.0	61.9	51.2
NPV of external public debt/export (%) 6/	657.0	570.3	668.1	721.2	991.7
Debt service/exports (%) 6/	30.2	25.1	34.9	36.4	51.1
Savings-Investment balance	0.3	-3.6	-6.1	-5.5	-5.6
Private	21.5	8.4	9.2	19.9	10.3
Public	-21.2	-12.0	-15.3	-25.4	-15.9

Sources: Eritrean Authorities, and IMF Staff estimates and projections

1/ Positive = appreciation. 2/ Change, % of beginning of period Broad Money. 3/Includes both current and capital expenditures. 4/includes errors and omissions. 5/Public and publicly guaranteed debt, including projected new debt. 6/ Based on three-year average of exports of goods and services.

Annex II (C) Table of Government Financial Operations- Eritrea

	2005	2006	2007	2008 est.	2009 proj.
		(In millions of Nakfa)			
Total revenue and grants	5,957	5,043	4,921	4,457	4,512
Revenue	4,380	4,275	4,293	3,853	3,775
Tax Revenue	2,709	2,723	2,405	2,459	2,374
Direct taxes	1,586	1,647	1,512	1,719	1,580
Indirect domestic taxes	572	571	487	395	435
Import Duties and taxes	550	504	406	345	360
Nontax revenue	1,671	1,552	1,888	1,393	1,401
Grants	1,577	768	628	604	737
Total expenditure and net lending	9,537	7,274	8,029	9,844	9,097
Current expenditure	6,799	5,419	5,900	6,905	6,824
Wages, salaries and allowances	2,041	2,074	2,234	2,275	2,430
Materials and services	2,117	1,969	2,316	2,531	2,398
Subsidies and transfers	851	592	706	1,311	931
Interest	528	601	644	788	1,065
Domestic	395	503	571	648	853
External	133	98	73	140	212
Externally financed special programs	1,261	182	0.0	0.0	0.0
Capital expenditure	3,016	2,262	2,224	2,331	2,134
Central treasury	1,453	888	1,012	704	681
Externally financed	1,563	1,374	1,203	1,627	1,453
Net lending	(278)	(408)	(95)	608	139
Overall balance	(3,580)	(2,231)	(3,109)	(5,387)	(4,584)
Overall balance, excluding grants	(5,157)	(2,999)	(3,736)	(5,991)	(5,321)
Financing	3,580	2,231	3,109	5,387	4,584
Domestic (net)	2,499	1,643	2,635	4,273	2,857
External (net)	769	727	935	1,549	1,629
of which: accumulation of external arrears (net)	29	(68)	43	119	53
Errors and omissions	311	(139)	(462)	(434)	99
Memorandum items:					
Primary balance	(3,052)	(1,630)	(2,465)	(4,599)	(3,520)
Primary domestic balance	(1,805)	(842)	(1,890)	(3,577)	(2,804)
		(percentage of GDP)			
Total revenue and grants	35.3	27.1	24.3	21.0	15.7
Revenue	25.9	23	21.2	18.2	13.1
Grants	9.3	4.1	3.1	2.8	2.6
Expenditure and net lending	56.5	39.1	39.6	46.4	31.6
of which: Current expenditure	40.3	29.1	29.1	32.5	23.7
of which: Capital expenditure	17.9	12.1	11	11	7.4
Overall balance	-21.2	-12	-15.3	-25.4	-15.9
Financing	21.2	12	15.3	25.4	15.9
Domestic (net)	14.8	8.8	13	20.1	9.9
External (net)	4.6	3.9	4.6	7.3	5.7
Errors and Omissions	1.8	-0.7	-2.3	-2.0	0.3

Sources: Ministry of Finance, and IMF staff estimates and projections

Annex III Millennium Development Goals Indicators for Eritrea

	1990	1995	2000	2007
Goal 1: Eradicate extreme poverty and hunger				
Employment to population ratio, 15+, total (%)	..	65	65	65
Employment to population ratio, ages 15-24, total (%)	..	59	57	53
GDP per person employed (annual % growth)	..	0	-18	-2
Income share held by lowest 20%	..	..	..	..
Malnutrition prevalence, weight for age (% of children under 5)	..	..	..	..
Poverty gap at $1.25 a day (PPP) (%)	..	..	..	..
Poverty headcount ratio at $1.25 a day (PPP) (% of population)	..	..	..	..
Prevalence of undernourishment (% of population)	..	..	..	68
Vulnerable employment, total (% of total employment)	..	..	..	..
Goal 2: Achieve universal primary education				
Literacy rate, youth female (% of females ages 15-24)	..	..	..	..
Literacy rate, youth male (% of males ages 15-24)	..	..	..	..
Persistence to last grade of primary, total (% of cohort)	..	..	61	60
Primary completion rate, total (% of relevant age group)	..	23	36	46
Total enrollment, primary (% net)	..	..	38	42
Goal 3: Promote gender equality and empower women				
Proportion of seats held by women in national parliaments (%)	..	..	15	22
Ratio of female to male enrollments in tertiary education	..	..	17	..
Ratio of female to male primary enrollment	94	80	82	83
Ratio of female to male secondary enrollment	..	..	69	70
Share of women employed in the nonagricultural sector (% of total nonagricultural employment)	..	..	..	..
Goal 4: Reduce child mortality				
Immunization, measles (% of children ages 12-23 months)	..	58	86	95
Mortality rate, infant (per 1,000 live births)	88	74	61	46
Mortality rate, under-5 (per 1,000)	147	122	97	70
Goal 5: Improve maternal health				
Adolescent fertility rate (births per 1,000 women ages 15-19)	..	..	92	72
Births attended by skilled health staff (% of total)	..	21	..	..
Contraceptive prevalence (% of women ages 15-49)	..	8	..	..
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	..	450
Pregnant women receiving prenatal care (%)	..	49	..	..
Unmet need for contraception (% of married women ages 15-49)	..	28	..	..
Goal 6: Combat HIV/AIDS, malaria, and other diseases				
Children with fever receiving antimalarial drugs (% of children under age 5 with fever)	..	..	..	..
Condom use, population ages 15-24, female (% of females ages 15-24)	..	1	..	..
Condom use, population ages 15-24, male (% of males ages 15-24)	..	36	..	..
Incidence of tuberculosis (per 100,000 people)	72	78	85	95
Prevalence of HIV, female (% ages 15-24)	..	..	..	0.9
Prevalence of HIV, male (% ages 15-24)	..	..	..	0
Prevalence of HIV, total (% of population ages 15-49)	0.1	0.9	1.2	1.3
Tuberculosis cases detected under DOTS (%)	..	..	43	35
Goal 7: Ensure environmental sustainability				
CO_2 emissions (kg per PPP $ of GDP)	..	0.1	0.3	0.3
CO_2 emissions (metric tons per capita)	..	0.1	0.2	0.2
Forest area (% of land area)	..	16	16	15
Improved sanitation facilities (% of population with access)	3	3	4	5
Improved water source (% of population with access)	43	46	54	60
Marine protected areas, (% of surface area)	..	..	..	..
Nationally protected areas (% of total land area)	..	..	..	5
Goal 8: Develop a global partnership for development				
Aid per capita (current US$)	..	46	48	32

Debt service (PPG and IMF only, % of exports, excluding workers' remittances)	..	0	3	..
Internet users (per 100 people)	0	0	0.1	2.5
Mobile cellular subscriptions (per 100 people)	0	0	0	2
Telephone lines (per 100 people)	..	1	1	1
Other				
Fertility rate, total (births per woman)	6.2	6	5.7	5
GNI per capita, Atlas method (current US$)	..	190	170	270
GNI, Atlas method (current US$) (billions)	..	0.6	0.6	1.3
Gross capital formation (% of GDP)	..	22.5	23.8	10.6
Life expectancy at birth, total (years)	49	52	54	58
Literacy rate, adult total (% of people ages 15 and above)	..	..	..	..
Population, total (millions)	3.2	3.2	3.7	4.8
Trade (% of GDP)	..	105.3	96.9	40.7
Source				

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