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Case study on Ethiopia*

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Acronyms

ADLI	Agriculture Development Led Industrialization
AGOA	African Growth and Opportunity Act
ART	Anti-Retroviral Treatment
BPoA	Brussels Programme of Action
CSO	Civil Society Organizations
DTIS	Diagnostic Trade Integration Study (DTIS)
EBA	Everything But Arms
EEA	Ethiopian Economic Association
EEPRI	Ethiopian Economic and Policy Research Institute
ESDP	Education Sector Development Programme
FDI	Foreign Direct Investment
GDI	Gender-related Development Index
GDP	Gross Domestic Product
GNP	Gross National Product
HDR	Human Development Report
HIPC	Heavily Indebted Poor Countries
HSDP	Health Sector Development Programme
LDC	Least Developed Countries
MDG	Millennium Development Goal
MFI	Micro Finance Institution
NBE	National Bank of Ethiopia
NGO	Non-Government Organization
ODA	Official Development Assistance
PASDEP	A Plan for Accelerated and Sustained Development to End Poverty
SDPRSP	Sustainable Development and Poverty Reduction Strategy paper
SME	Small and Medium-size Enterprises
TVET	technical and vocational education training
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
WTO	World Trade Organization

Introduction

The Government of Ethiopia started the implementation of the Brussels Programme of Action for LDCs with full recognition of the high incidence of extreme poverty and the structural problems of the economy of the country. The Government has attempted to address the seven commitments of the Brussels Programme of Action by integrating and implementing them in the context of its Sustainable Development and Poverty Reduction Strategy Papers. According to the recent internationally defined estimates of UNCTAD and the World Bank, about 85.4 per cent of the Ethiopian population lives under absolute poverty (one US$ a day) and 94.7 per cent under extreme poverty (two US$ a day). According to the African Economic Outlook, Ethiopia is slipping back far behind the MDG goals set for 2015, except for access to improved and safe water, which has shown significant improvement over the years.[1] The structurally weak and vulnerable economy of the country, characterized by over dependence on traditional agriculture, a stagnant industrial sector, excessive commodity and market concentration for export earnings, low levels of human and institutional development, political instability, successive natural disasters such as drought and a lack of investible financial and technical resources, amongst others, are major factors responsible for the prevalence of the alarmingly high incidence of extreme poverty in the country.

Agriculture remains the dominant sector of the Ethiopian economy accounting on average for 43 per cent of the GDP for the period 2000/01 to 2004/05. In the same period, the share of the services sector exceeded agriculture, accounting for 46 per cent of GDP. The major sources of the increase in the share of the services sector were increased expenditure on administration and defence, education and finance. Other than public administration and defence and, considering 2000/01 as a reference year, the share of education, banking and insurance increased by 1.8 per cent and 1.3 per cent respectively, followed by domestic and other services, and transport and communications, whose shares increased by 0.9 per cent. However, such an increasing trend has not been observed in the industrial sector, as its share remained nearly constant, accounting for an average of 15 per cent for the period 2000/01 to 2003/04.

After the war with Eritrea politically ended in December 2000 (with tensions still existing due to the delay in border demarcation), the Ethiopian economy declined in 2002/03, particularly due to adverse weather conditions. The growth of real GDP averaged 1.7 per cent in 2001-2002 which translated into a 1.2 per cent and a 6.6 per cent decline in per capita income in 2001/02 and 2002/03 respectively Per capita income during the period 2000/01 to 2004/05, increased at an average annual rate of 1.8 per cent. If weather conditions continue to improve, per capita income is expected to grow at an annual average rate of 4 per cent during the next two years and, this will track the average economic growth rate target of the Programme of Action for 2001 - 2010. Consistent with the trend in per capita income, GDP has been fluctuating mainly as a result of the poor performance of agriculture since 2000/01. Up to now, the GDP exhibited an average annual growth rate of 6.8 per cent[2] which is 1 per cent below the target set for 2001-2010. It is also estimated to reach 6.8 per cent and 7 per cent respectively, in 2005/6 and 2006/07. The estimates indicate that the economy can be on track to achieve the planned average GDP

[1] OECD and ADB, 2005. African Economic Outlook, 2004/05, Paris.
[2] This estimate excludes the 2002/03 data where the GDP fell by about 4 per cent due to severe weather conditions that adversely affected the performance of the agriculture sector.

growth rate of 7.6 per cent by 2010, slightly higher than the 7 per cent growth target of the Programme of Action.

1. Assessment of national policy efforts and challenges to implement actions and commitments of the Programme of Action

Ethiopia has continued the weekly wholesale foreign exchange auctions to determine the foreign exchange rate and, this has enabled the country to manage the depreciation of the Birr at the current level. In 2004/05, the official exchange rate was Birr 8.66 per US$ and, the Birr depreciated by 3.6 per cent compared to the previous year. The exchange rate of the parallel market was 1 per cent higher than the official exchange rate in 2004/05. The Government has been able to maintain macroeconomic stability as inflation has stabilized at single digit levels. Currently, it stands at 6.8 per cent (as of June 2005). The inflation rate in the fourth quarter of 2004/05 was also 5.2 per cent, exhibiting a slight increase from 4.9 percent in the same period in the previous year.[3] Inflation since September 2005 is likely to continue, due to the increase in oil prices and, the gradual removal of the oil price subsidy.

After a sharp decline in 1997/98, gross domestic savings[4] are estimated to exhibit an average annual increase of 2.4 per cent of the GDP from 2000/01 to 2003/04. Gross national savings have also shown a gradual increase since the early 1990s. Although characterized by fluctuations, domestic savings have on average increased by 13 per cent of the GDP since 2000/01, compared to 11 per cent in the 1990s. Similar increasing trends are expected to prevail in the coming years. The overall Government revenue has been steadily increasing since 1990/1991. In 2004/05 it increased by 11.5 per cent over the previous year mainly as a result of increased foreign trade tax. Whereas the proportion of foreign trade tax was increased from 25 per cent in 2000/01 to 31 per cent in 2003/04, the proportion of non-tax revenue, steadily decreased from 24 per cent in 2000/01 to 15 per cent in 2003/04.

[3] NBE, 2005. Quarterly Bulletin, Fourth Quarter 2004/05, Addis Ababa.
[4] Domestic savings is calculated as the GDP minus private and public consumption expenditure. All macro data is acquired from Ministry of Finance and Economic Development.

Table 1

Summary of Government Revenue and Expenditure

	2001/02	2002/03	2003/04	2004/05	2005/06 Budget	2006/07 Forecast	2007/08 Forecast	2008/09 Forecast	2009/10 Forecast
Revenue-value	10,477	11,157	13,916	15,477	22,465	22,445	24,482	27,711	31,304
% to total	88.09	87.02	80.82	80.77	77.62	78.48	77.64	79.61	80.16
Tax Revenue-value	7,926	8,243	10,906	12,265	16,164	18,111	20,716	23,758	27,204
% to total	66.64	64.29	63.34	64	55.85	63.33	65.7	68.26	69.66
Non-tax revenue-value	2,551	2,914	3,010	3,212	6,301	4,334	3,766	3,953	4,100
% to total	21.45	22.73	17.48	16.76	21.77	15.15	11.94	11.36	10.5
Grant-value	1,417	1,664	3,302	3,686	6,477	6,153	7,050	7,096	7,747
% to total	11.91	12.98	19.18	19.23	22.38	21.52	22.36	20.39	19.84
Budget Support-value	305	467	2,255	2,331	3,506	2,861	3,389	3,690	3,951
% to total	2.56	3.64	13.1	12.16	12.11	10	10.75	10.6	10.12
Project-value	1,112	1,197	1,047	1,355	2,971	3,292	3,661	3,406	3,796
% to total	9.35	9.34	6.08	7.07	10.27	11.51	11.61	9.79	9.72
Total Revenue & Grants	**11,894**	**12,821**	**17,218**	**19,163**	**28,942**	**28,598**	**31,532**	**34,807**	**39,051**
Expenditure	**15,674**	**16,950**	**19,533**	**23,672**	**35,027**	**41,515**	**48,924**	**57,099**	**67,270**
Current	9,544	10,637	11,262	12,315	15,032	18,619	22,016	25,579	30,234
Capital	6,130	6,313	8,271	11,357	19,995	22,896	26,908	31,520	37,036
Budget Deficit	**-3,780**	**-4,129**	**-2,315**	**-4,509**	**-6,085**	**-12,917**	**-17,392**	**-22,292**	**-28,219**

Source: MoFED

Grants and budget support have been increasing since 2001/02 and, the same trend is expected to continue until 2010. However, the proportion of the budget support to total grants has declined from 13 per cent maximum in 2003/04, to 12 per cent in 2004/05 and, this is expected to decline further to an average of 10.5 per cent in the coming years. The budget deficit exhibited a decline in 2003/04. However, it increased significantly in 2004/05 by about 94.7 per cent. According to the estimate of the MoFED, it is anticipated that the budget deficit will continue to increase until 2001, while the overall composition of expenditures is also estimated to increase from 2004/05 to 2005/10, with a gradual increase in resource balance. Therefore, overall government expenditure has been steadily increasing since 1990/1991. In 2004/05 it increased by 20.5 per cent from the previous year largely due to the increase in capital expenditure. The increase in capital expenditure over the previous year accounted for about 37.3 per cent, mainly due to high spending on road construction, agriculture and education. Current expenditure grew by about 9 per cent in 2004/05 and accounted for about 64.7 per cent of the real GDP; (8.3 per cent more than the capital expenditure).

Table 2
Expenditure as percentage of GDP

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
GDP at Current Market Price	83,892	96,676	112,435	125,927	144,060	165,237	189,196
Consumption Expenditure	95.1	109.0	124.2	135.4	150.2	166.2	182.6
Gross capital formation	21.3	24.2	29.1	35.3	43.4	54.1	67.6

Source: MoFED

As in many other poor countries, the average domestic resources available for financing investment and public services in Ethiopia remain very low. For instance, in Ethiopia this was 23.7 per cent of the GNP for the period 2000/01 to 2003/04. Gross domestic savings averaged about 15.3 per cent of the GNP.

The Government needs to consider formulating new policies and/or amending the existing ones so that they will contribute to the overarching goal of poverty reduction. Such policies should also enhance the role of the private sector in general and, the trade sector in particular. For instance, apart from the land use certification system that started in the last few years, land is solely owned by the Government. Contrary to the views of the Government, various studies have indicated that the ban on private land ownership has a negative effect on privatization and, land reclamation, as well as on investment activities. In spite of some progress in recent years, the supply of land and the process of land acquisition does not encourage private investment (domestic and foreign).

The most disadvantaged and affected by the current land policy, are those with limited capital and access to credit. This is mainly due to the fact that in Ethiopia land cannot be used as collateral to access financial loans or credit, unless it is acquired through a land lease. In addition to reviewing the security of tenure to improve the economic and psychological value of land, the Government needs to review its financial policy. The current financial policy is found to be discouraging for domestic investment. For instance, domestic investors can only access investment financing or equity financing if they have a minimum of 30 per cent collateral of the desired loan amount, provided that the risk is adequately financed. For accessing the remaining 70 per cent loan, banks require risk financing, amounting from 100 per cent to 150 per cent of the loan. The financial sector provides loans with a very minimum risk, putting the burden of risk solely on investors. Therefore, the financial sector needs to develop risk sharing attitudes and practices. In the face of the low asset holding and/or capital base of the private sector and, where land does not have commercial value, the private sector may not be able to adequately contribute to the overall objective of poverty reduction through employment generation and increasing returns on investment.

In the past, Ethiopia did not have an industrial policy that was able to direct and attract investments to the sector. During the imperial era (pre-1974), the five-year development plans encouraged investment flows into the manufacturing sector. This contributed to strengthening input-output linkages and, to the promotion of an import substitution strategy. However, the development plans failed to transform the economy of the country in general and, its industrial and agricultural sectors in particular. This was followed by a socialist industrialization policy (1974-1991), that nationalized the privately owned manufacturing industries and restrained their growth and efficiency. It also eroded the entrepreneurial skills and motivation of the people to take individual initiatives in the sector. The current Government has also adopted an Agriculture Development Led Industrialization (ADLI) strategy as an overarching policy to generate industrialization through the development of agriculture. The central assumption of this strategy is that higher demands for manufactured goods through the growth in agriculture, would sufficiently generate higher investment and productively in the industrial sector. Since 1991, although there has been privatization of state controlled manufacturing industries, the Government continues to own some strategic industries (such as large scale engineering, metallurgy, communications, power and pharmaceutical industries), including land and urban housing. The experiences of the last 15 years show that the agriculture sector could not generate the expected demand for the industrial sector due to various reasons. Hence, there is an urgent need to design an industrial policy for the country.

Moreover, the financial sector has a sustained problem of liquidity as a result of the limitations of the policy for free and competitive market environments in most sectors. At the end of the fourth quarter of the 2004/2005 budget year, the total reserves at the National Bank reached 12.6 billion birr, of which 10.9 billion birr was an excess.[5] Although four interest rates for loans and deposits were set, the banks do not seem to be free from the excess liquidity problem. The persistent rise in the excess liquidity of the banking system has continued to pose a challenge to the effectiveness of monetary policy instruments. According to the NBE this hinders the development of a money market in Ethiopia.[6] Loans for large investments need to be available to private investors with attractive incentive packages such as long grace periods, subsidized loans, matching funds and loan guarantee schemes. The financial market is also not fully liberalized and, the Government needs to look into the possibility of establishing a stock exchange and a capital market, in addition to designing policies and strategies to encouraging domestic investment, particularly the latter, to avoid and/or channel excess liquidity into investment.

The 1998-2000 war with Eritrea and subsequent natural disasters, had a serious knock-on effect on the economy of the country. The financial cost of the war, alone, according to Government or official estimates, was about US$2.9 billion although conservative estimates put the financial cost as high as US$5 billion. These estimates do not take into account the loss of lives, property damage, real economic and opportunity costs and, the political cost of the war that reduced the region's prospects to attract investment, as well as the loss of revenue from tourism and other business activities. Lack of regional political stability and, the continued tension along the border between Ethiopia and Eritrea, could have a long-term adverse impact on the economies of the two countries. Urgent resolution of the dispute between the two countries should be given serious considerations at the national, regional and international levels.

1.1 Commitment I: Fostering a people centred policy framework

Ethiopia has been implementing its Sustainable Development and Poverty Reduction Programme (SDPRP) since 2001, as an on-going commitment of the Government and, as a framework for strategies and policy formulations. Ethiopia continues to implement the

[5] http//www.allAfrica.com, 2005
[6] Ibid-

programme by building on the strategy of Agricultural Development Led Industrialization (ADLI) and food security. This is accompanied by civil service and justice system reform, governance, decentralization and empowerment and, institutional capacity building initiatives.

The notable successes registered in the past few years in Ethiopia were the increases in coverage of water supply, construction of road networks, the expansion of telecommunications services and education (increase in the number of schools and children in schools, as well as the doubling of the university intake). Spending on sectors oriented towards poverty reduction objectives, increased from 50.3 per cent in 2003/04 to 56.8 per cent of total public spending in 2004/05. The administrative structures were decentralized to the woreda (District) level, although their weak institutional capacities, including lack of financial, technical, and trained human resources remain a challenge. There has been a large increase in public spending on education, health, and agriculture, with respective average increases of 26 per cent, 45 per cent and 66 per cent during the period 2000/01 to 2003/04, while maintaining prudent fiscal management. The National Food Security Programme has been designed and, the Government was able to maintain macroeconomic stability with low inflation and a stable exchange rate.

Other positive developments relate to the establishment of a major private sector in the "cut-flower" industry, and the doubling of the level of horticulture exports, as well as major changes in public service delivery (customs, licensing, access to land, courts etc.). Although quantitative increments have been observed in many of these areas, the qualitative aspects still await serious attention in future development interventions. The focus of SDPRP on expanding education, strengthening health and fighting against HIV/AIDS, capacity-building and decentralization and, the food security programmes, are believed to contribute to improving the development of institutional and human capacities.

As a continuation of the process of SDPRP, the design of a Plan for Accelerated Sustainable Development to End Poverty (PASDEP) by 2015 (a 10 year plan) has been completed. The planning process involved two rounds of consultations with civil society, non-governmental actors, and development partners. The consultations were based on the recent Household Income, Expenditure and Consumption Survey and, a number of background papers and studies prepared by various government ministries and independent Ethiopian experts. Several major studies recently conducted by Government ministries and independent Ethiopian experts, including the Millennium Development Goals Needs Assessment for Ethiopia (conducted by the Government in collaboration with partners), have also been effectively used in the process. The preparation of both the SDPRP and PASDEP involved a wide-range of stakeholders at regional and federal levels, while the draft report was distributed for review to development partners, non-government organizations (NGOs), civil society organizations (CSOs) and the private sector.

The Government of Ethiopia and the donor community have established various technical and advisory groups to discuss progress made and problems encountered in implementing development programmes. Joint review of planning and monitoring of the implementation of development programmes is becoming a common practice. Apart from political and democratic issue, which have been deteriorating since the last election, there has been a better exchange of information between Ethiopia and her development partners.

As part of its integrated rural development strategy the Government has also been making efforts to establish cooperatives, such as coffee farmers' cooperatives and grain farmers' cooperative unions in different parts of Ethiopia. This was in recognition of the important role of such cooperatives in the delivery of social services and, in building institutional capacities in rural areas. For instance, the rural development policies and strategy documents state that "cooperatives play a significant role in creating improved marketing systems and, in providing market information, as well as in promoting other agricultural development initiatives".[7] These newly formed and viable cooperatives and unions now represent about 4.2 million members. Although an apex body does not exist as yet, the cooperative's unions were not consulted during the recent process of PASDEP and, other relevant policy dialogue forums. The Government has been benevolently supporting the cooperatives sector and has been able to establish about 14,423 cooperatives and 101 cooperative unions. In 2005, there were only five coffee farmers' cooperative unions involved in exporting coffee, while the grain farmers' cooperatives unions participated in external trade (output marketing and input purchase). The establishment of a cooperatives' apex body and its involvement in the processes of policy dialogue on development related issues, including macroeconomic policies, is crucial for the socio-economic progress of the country. The Government needs to create and to improve the policy environment to make it more conducive to the further expansion and growth of cooperatives and their unions. It should also look for ways and means to further strengthen their capacities, so as to enhance their productive and marketing functions.

According to studies of the Ethiopian Economic Association (EEA) and the Ethiopian Economic Research Institute (EEPRI), efforts made for mainstreaming trade in national policies and strategies need to be considered from the development perspective, instead of focusing only on trade liberalization The emphasis of the PASDEP on commercialized agriculture, envisaged for enhancing exports, should be accompanied by integrated development interventions[8] that improve the productive capacities of producers.

1.2 Commitment II: Good governance at national and international levels

1.2.1 Justice, Law and Order

The Government of Ethiopia has made efforts to strengthen the justice system through the training of judges and prosecutors and, enhancing the institutional capacities of courts to manage legal cases. The dissemination of information on the legal and civil rights of women have been aired through the national radio in collaboration with NGOs. In terms of enforcement, the existing institutional capacities to provide efficient and effective legal services have not yet been realized, as most cases take a long period (months and years) prior to judiciary decisions. The delay in justice to the officials of the former regime who have been imprisoned for more than 15 years could be one classic example of delayed justice and the weak capacity in this field.

The Government established the National Electoral Board (NEB) that oversaw the preparation and the conduct of the last election. Ethiopia has had three multiparty elections since the 1990s. The most recent was held in May 2005. The preparation for the May

[7] FDRE, 2004. Rural Development Sector Millennium Development Goals Needs Assessment.
[8] This calls for a number of interventions aimed at creating a favourable policy environment for enhancing agricultural production, marketing, infrastructure, social services and, the inception of farmers institutions, such as cooperatives and their apexes, strengthening the services of financial institutions and, the private sector and others.

election was very effective in informing the general public about the procedures of the election and the exercise of the vote. The National Electoral Board used both electronic and print media to popularize the election and its processes. The dissemination of information on the election procedures and processes was later accompanied by live debate among the contesting parties. This helped them to promote their respective political agenda and criticism of the policy of the current regime. This in turn has contributed to effectively inform and educate the people about the democratic process, which raised the expectations of the general public on having a fair and free election.

The May 2005 election was also the first of its kind in terms of popular participation. The turnout, which was above 90 per cent, also confirmed the growing interest of the people in the election. The NBE effectively insured that appropriate procedures were put in place until the voting was completed. However, the opposition accused the Electoral Board of and, its apparent failure to appropriately complete the counting process. The opposition also accused the NEB of its inability to appropriately and transparently address issues raised after the voting. This resulted in the bitter disappointment of the opposition parties and their supporters. This in turn caused civil riots- riots that brought about allegations of serious violations of human rights, loss of life and property damages, as well as the disruption of socio-economic activities in the country. Since May 2005, the Government has attempted to control two major and several localized riots in various parts of the country. The existence of a slim chance for peaceful protest had further exacerbated the political tension between the Government and the opposition. Genuine efforts to promote open and constructive dialogue between the parties in dispute, as well as enhancing the effectiveness of justice, law and order, are indispensable to restore democracy and sustainable peace.

1.2.2 Human Rights

The Government of Ethiopia has been able to establish a Human Rights Commission and Ombudsmen's office, and also appointed a Commissioner and Ombudsmen. The attempts made to protect the human rights conditions prior to the last election were encouraging and provided an ample basis to build the confidence of citizens to participate in the democratic processes. However, international observers and human rights institutions have raised serious doubts and concerns on the commitment and promise of the Government to democracy and the rule of law following the election. The inability of the people to conduct peaceful protests after the election and, the ensuing measures taken by the Government against demonstrators, were heavily criticized by the opposition, international human rights institutions and, by some developed countries. Since then, the human rights conditions in Ethiopia were viewed by many as deteriorating and characterized by political instability, a number of civilian deaths and, the injury and imprisonment of several thousands of people. The Government accused the opposition of insurrection, incitement, treason and genocide, offences which could result if convicted, in capital punishment.

Civil societies working on human rights issues have been actively engaged in both educating and lobbying for respect for, and protection of human rights in Ethiopia. Their relationships with the Government have also been relatively smooth and, efforts were made to promote human rights concerns until the recent election. According to many observers of the current political situation in Ethiopia, the inability to distinguish between human rights concerns and opposition politics on the one hand, and lack of tolerance to accommodate and/or appreciate differences of opinions on the other, have tremendously affected the current human rights and governance situations.

Although the Government has been defending its actions as being within the laws of the country, the imprisonment and constant harassment of journalists and/or clamping down on private media, including preventing publication of their newspapers, have been widely reported[9]. These activities could have resulted in adverse effects or, a setback to the accountability, transparency and openness of governance, as well as on the democratic process as a whole. The recent imbalance observed and, the deterioration of the human rights condition resulting from election politics, have contributed to the forced migration of those who were involved in the political process, as well as those who were disappointed. Unless such trends are quickly reversed and the Government renews its commitment to bring back democracy and good governance, there is the likelihood of more "brain-drain" in the coming years.

The development partners played a crucial role in observing the democratic process, mediating and reducing the tension that was created due to the disputes among political parties. The persistent requests made by the donor community for Ethiopia to take action on the protection of human rights have been effective, as the Government responded to some of the requests. Development partners had an important role to play, particularly in resolving disputes between the opposition and the Government on the conduct and outcome of the May election. This proved to be an effective balancing force when tension ran high between the disputing parties, causing political instability and civil strife. It is worth noting the growing role of information technology in improving the protection of human rights. Ethiopians residing in the country, as well as abroad, have been using the internet and other print and electronic media to share their views on the socio-political developments in the country.

Furthermore, as a critical factor for the achievement of the goals of SDRPR and/or, for the future PASDEP, as well as for the attainment of the goals and targets of the MDGs and those of the PoA, Ethiopia needs to fully resolve the border demarcation dispute with Eritrea, enhance its governance and, resolve the deadlock created with the opposition parties. This will also assist in ensuring internal and external peace in the country.

1.2.3 Corruption

In an effort to fight corruption, the Government has set up an Ethics and Anti-corruption Commission. The Commission attempted to reform the Government procurement systems and is developing a Public Servants' Code of Conduct. However, the actions taken by the Commission on cases that have been widely reported have not been adequately made public, so as to enlighten the general population. Despite the above-mentioned efforts of the Government, Ethiopia scored 2.3 out of a score of 10 in the rating of the index for perception on corruption by Transparency International in 2005. The Government needs to do more to fight corruption to attain at least the average score..

9 CPJ 2006. special report: China, Cuba, two African nations are top Jailors of journalists: Ethiopian Crackdown fuels worldwide increases; US is 6th among nations; ICJ, 2006, ICJ calls for immediate and unconditional release of Lawyer, Trial observer sent to Ethiopia

1.2.4 Decentralization

Decentralization was implemented in order to improve the participation of local governments and their respective communities in the development process. The decentralization strategy clearly stipulates the mandates of the local governments to mobilize resources and use 40-60 per cent of such resources. These attempts have also been complemented by financial support from the Federal Government on a case by case basis. However, the capacities of the local governments to fully finance their expenditures have not been realized as yet and, will remain a challenge in the near future.

1.3 Commitment III: Building human and institutional capacities

According to the Human Development Report (HDR) 2005, of the United Nations Development Programme (UNDP), Ethiopia ranked 170th out of 177 countries and, the HDI showed a slight improvement from 0.29 per cent in 1985 to 0.37 per cent in 2003. Some social indicators also show progress, especially on health and education. However, the low ranking of HDI is expected to reflect the continued social subordination of Ethiopian women and the cultural and religious customs that favour men. The HDR for 2005 ranked Ethiopia 134 out of 140 countries in terms of the gender-related development index (GDI). Female-earned-income amounts to only 52 per cent of male-earned-income. The representation of women in the parliament (which has about 500 members) has increased from about 7 per cent prior to 2005 to about 20 per cent at present. Even though the Government launched a National Action Plan for Gender in 2004/05, it is necessary to involve the development partners and engage proactively in the coming years to address gender concerns at all levels and, in all sectors.

Through the Education Sector Development Programme (ESDP), Ethiopia aims to provide universal primary education by 2015. ESDP was implemented through decentralized management, cost sharing mechanisms (at secondary and tertiary levels) and, the involvement of the private sector. The overall achievement of the education policy has been significant, although quality remains a challenge for the sector. In 2003/04, the overall primary school enrolment was 68.4 per cent compared to about 61 per cent in 2001/02. Girls' enrolment increased from 41 per cent in 2001/02[10] to 59.1 per cent in 2003/04[11]. The gross enrolment of girls at high school level remains relatively low at 27 per cent, as there are a large number of dropouts.

Encouraging signs were observed in terms of the participation of girls in both secondary (47.5 per cent) and higher education (23 per cent) in 2004. However, the overall literacy rate of the population remains low, at about 36 per cent. The number of technical and vocational education training (TVET) institutions substantially increased (from about 20 in 1995 to 159 by 2004[12]) and, their intake had reached 102,649 in 2003/04[13]. In addition to improving the quality of education, some of the major challenges facing the sector are:

[10] EEA Electronic Database, 2002

[11] MoFED, Dec. 2005. Plan for Accelerated Sustainable Development to End Poverty, draft programme document, Addis Ababa

[12] EEA, 2005. Economic Focus, Bulletin of the Ethiopian Economic Association, Vol. 8 no. 2, May 2005, Addis Ababa

[13] MoFED, Dec. 2005. Plan for Accelerated Sustainable Development to End Poverty, draft programme document, Addis Ababa

diversifying the fields of specializations in TVET, increasing the supply of qualified teachers and, reducing the high teacher-student-ratio, that was about 64 students per teacher in primary schools in 2004.

The Health Sector Development Programme (HSDP) has also been implemented since 2002, with the second phase of HSDP completed in 2005. The Government has been able to implement various health sector reforms geared towards improving health management systems, strengthening the health products logistics systems, strengthening health extension packages and, preventing and controlling malaria, tuberculosis and HIV/AIDS. Government expenditure on health increased from 27 per cent in 2000 to 36 per cent in 2004/05. The budgets for health enabled the per capita daily consumption of health services to increase from about US$1.4 per person in 2001/02, to about US$6.0 per person[14] in 2004/05.

Some of the achievements in the health sector relate to an increased coverage of primary health care from 61.3 per cent in 2002/03 to 64 per cent in 2004/05 and, tuberculosis prevention and control from 20 per cent in 2001/02 to 76 per cent in 2004/05. Compared to 2001/02, the programme on immunization expanded from 27 per cent to 60 per cent and, the antenatal coverage from 29 per cent to 41 per cent. The contraceptive prevalence rate increased from 13 per cent to 23 per cent in the same reference period. HIV/AIDS has remained the focus of the health sector initiatives. The adult prevalence rate is 4.4 per cent (as of 2003). A high prevalence rate has been observed in urban areas where an average of 12-13 per cent has prevailed since the mid-1990s. The HIV/AIDS prevalence rate among pregnant women and in rural areas increased from 1.9 per cent in 2000 to 2.6 per cent in 2003. A policy on Anti-Retroviral Treatment (ART) was introduced but, only less than 10 per cent of the people in need of ART had received treatment as of June 2005. A programme to control mother-to-child transmission of HIV/AIDS and sexually-transmitted diseases, as well as to monitor blood safety, was launched in order to improve the tracking, measurement and prevention programmes for HIV/AIDS.

The Government has embarked on setting up a health extension system to improve the health service coverage. Although the overall achievement of access and utilization of the health service has improved, there is still a huge gap between the demand and supply of health care services. The sector is characterized by a shortage of medical supplies, high spending of the health budget for tertiary curative services, inadequately qualified and inefficient medical staff and, inefficient retention and employment systems. The sector also suffers from weak coordination and, the lack of a common implementation procedure among donors and the Government.

The planning of the subsequent HSDP-III was recently completed and, commitments towards achieving the health-related MDGs are expected to address the above issues. This programme envisages increasing health service coverage to 64 per cent by 2010 and, focuses on the expansion of primary health care, child survival and reproductive health services.

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[14] MoH, 2005. Health and Health Related Indicators

1.4 Commitment IV: Building Productive Capacities to make Globalization work for LDCs

1.4.1 The Transport Sector

The Government is implementing the SDPRP and PASDEP with full recognition of the need to improve infrastructure, mainly in the transportation, telecommunication and energy sectors. The government has been implementing the Road Sector Development Programme to strengthen the road, air and water transport networks since early 2000. The road network increased from 24,970 km in 1997 to 36,496 km in 2004, with an increase in the density of roads from 24.1 km to 33.2 km per 1000 square km for the same reference period. The air transport sector has also been constantly expanding its destinations and, currently has 63 destinations including 22 domestic destinations. In addition, Ethiopian Airlines and/or the Ethiopian Civil Aviation Authority have been able to serve 62 destinations with other partner airlines. In addition to the Addis Ababa Bole International Airport, Dire-Dawa airport is used for international destinations and, the Government is upgrading domestic airports at historical sites to provide better flight services for tourists.

Ethiopia owns 12 ships, out of which 10 are functional, through the ports of Djibouti, Assab and Massawa (prior to the border war with Eritrea). A parastatal institution, Ethiopian Shipping Lines, provides commercial maritime services to various European, North and East African, Middle Eastern and Far East ports. Currently, it has a capacity of 112,834 gross registered tons and, works with 36 local freight forwarding and shipping agencies. A rail transport link, that was established in 1917, has also been operational under the "Chemin De Fer Djibouti-Ethiopien" agreement signed in 1981. This railway has not been upgraded for a long time and, lost its competitiveness to provide efficient service in the land transport sector. This is confirmed by the fall of its freight tonnage from 336,000 tons in 1986, to 207 000 tons in 2002 and, a decline in the number of passengers by about 50 per cent during the same reference period.

For many years road transport has been the most competitive and dominant mode of transport in the country. However, about 70 per cent of the total population lives without access to all weather road networks, while only about 17 per cent of the rural population has access to all weather roads within a 2 km radius. In addition, about 6 per cent of the road network is appropriate and about 65 per cent of roads are in good and fair condition. In addition to their low quality, the density of the roads does not allow the effective and efficient functioning of road transport services, inhibiting the smooth and effective implementation of the various policies designed to promote and expand domestic trade.

The Government spent about 9.5 per cent of the GDP in 2003 for investment, maintenance and rehabilitation of road networks.[15] This constituted a large proportion of public spending on transport in general. Road sector taxation and charges, namely user and other charges related to the road sector, including taxation on fuel and lubricants, are used for road transport. In 2000/01 about 77.5 per cent of the maintenance financing requirements was met from user charges, while by the end of 2003/04, the contribution of user charges was expected to cover all maintenance needs.[16] Spending through taxation accounted for about 31 per cent in 2003. Due to larger needs for enhanced road networks and increased

[15] WB, 2004. WB SSATP indicators on Ethiopia

[16] ADF, 2004. Multinational-Kenya/Ethiopia Mombasa-Nairobi-Addis Ababa Road Corridor Development Project, Appraisal Report, Infrastructure Development , ONIN, Oct. 2004

local trade, the sector could not provide adequate service, as it has a huge financial deficit, to maintain, upgrade and improve road networks to adequately cover the whole country.

Ethiopia is a landlocked country and, has been using ports in neighbouring countries, namely Djibouti and Eritrea (prior to the 1998-2000 border conflict). Currently, it relies mainly on the port of Djibouti, which is connected to a good quality asphalt road. Although no major problems have been experienced, the need for enhancing the regional road network with Kenya and Sudan will enable Ethiopia to access additional ports for promoting external trade. It is essential to pursue the implementation of the planned multinational road corridor development projects.

1.4.2 Telecommunications, energy and water supply

The Ethiopian Telecommunication Authority has undertaken a major expansion programme in both urban and rural areas. As a result, it increased its coverage from 400,000 in 2002 to over one million in 2005. In terms of enhancing the linkages among the cities, towns and localities, it was able to connect 300 towns and 3,000 villages by 2005. Increased connexions of towns and villages has promoted information exchange, trade and business relationships among various regions and communities. This is believed to promote local market integration and attract domestic and foreign investment. The internet connexions have helped the dissemination of various information that enhances business,education, research, etc. The recent experience which the Government and all partners recognize, was the role of the internet in informing the rest of the world about political developments in the country and, particularly in the absence of private media, it has served as the most accessible source of information for the general public.

The electric power of the country heavily relies on hydroelectricity which accounts for about 98 per cent of the total electricity supply. Although the country has a potential for generating 160,000 GWh of hydropower electricity, the current generating capacity is about 2,000 GWh[17]. The major supply of electricity (97.8 per cent) is transmitted through the Inter-Connected system, while the remaining is supplied through the Self-Contained System[18]. For instance, according to the World Bank's African Development Indicators, (2001), electric power consumption per capita for Sub-Saharan African countries was 431.3 KWH, while for Ethiopia in the same year, it was 22.1KWH.[19] The current supply of electricity reaches only about 17 per cent of the population who are mainly living within, and in the vicinity of urban areas. In spite of its low coverage, the real growth rate of the electricity power supply, after a decline of electricity power generation in 2003/04, was about 7 per cent. The share of oil and electric power in the energy consumption of Ethiopia is only 5.5 per cent. The importance of electricity supply for the development efforts of the industrial and private sectors is vital.

Safe water supply has also increased since 2002 through the interventions made to rehabilitate and expand urban and rural water supplies. The Government improved safe water supplies in 83 towns and constructed about 160,000 wells during the period 2002/03-2004/05. The coverage of the overall supply of safe water increased from about 20 million

[17] OECD and ADB, 2004. African Economic Outlook, France.
[18] Inter-connected system is a transmission system established for the hydroelectric power supply while the self contained system is for diesel generated electric power supply.
[19] CBE, 2005. 4th Quarter Report. Addis Ababa

people in 2002 to 26.6 million people in 2005[20]. Although it has narrowed, the gap still remains high, as about 64 per cent of the population has no access to clean or safe water. Ethiopia is expected to provide 70 per cent of its population with safe and clean water by 2010 and, is far behind the target set in the BPOA on water and sanitation.

1.4.3 Domestic and External Trade

The Government managed to create a favourable environment for the development of the private sector through privatization and, by undertaking institutional, legal, land use and tax reforms. Although the process started in 1994, the privatization of the Government owned enterprises has not been completed. By 2005, about 221 enterprises had been privatized and 146 remain in the hands of the Government. The privatization of the remaining enterprises is expected to continue in the coming years.

The Government has also adopted various legal and regulatory reforms on taxation and tariffs. Although revenues from taxation have been increasing since 2000/01, there was a marked increase in 2003/04 (about 28 per cent) over 2002/03. This was mainly a result of increased efficiency in tax collection and high import taxes. This increase in public revenue assisted the Government to increase its public spending on relevant social sectors for attaining the SDPRP objectives.

With a view to supporting private sector development and, enhancing the effectiveness of trade reforms, since 1993 the Government has been attempting to eliminate quantitative restrictions and to adjust tariff rates. Accordingly, tariff ranges were narrowed from 0-80 in 1995 to 0-32 in 2002 and, tariff rates declined from 28.9 per cent to 17.5 per cent in the same reference period. Implicit import duties also declined from 23 per cent in 1990 to 12 per cent in 2002 and, duties on all exports other than coffee have been removed. In addition, efforts were made to reduce the period required to clear customs and, to shorten the period required to acquire business licences. Although they have not been fully operational due to administrative reasons, the Government has also adopted measures for its gradual but complete withdrawal from the present state monopoly of the coffee trade and, to eliminate mandatory contract approval by the National Bank of Ethiopia, including allowing exporters to retain 10 per cent of their export proceeds. The implementation of reengineering the business process has also started and it is expected to significantly reduce the bureaucratic chain and related administrative problems.

In an effort to enhance the role of the financial sector, the Government has allowed the opening of private banks, micro finance institutions (MFIs) and financial cooperatives. Although the three state-owned banks account for about 70 per cent of the market, the growth of private banks is encouraging. Some private banks have established up to about 30 branches[21]. Unlike the public banks that continue to require collateral and provide credit services to relatively large enterprises, the private banks have played an important role in the provision of credit to small and medium size enterprises as well as cooperatives involved in external trade For instance, the Bank of Abyssinia was the first bank to provide loans to cooperatives through a loan guarantee scheme. The establishment of the private banks, as well as the micro finance institutions, has greatly enabled emerging entrepreneurs

[20] MoFED, Dec. 2005. Plan for Accelerated Sustainable Development to End Poverty, draft programme document, Addis Ababa

[21] OECD & ADB, 2005. African Economic Outlook. France

to access credit to set-up their businesses. The Government has also been attempting to provide support to small and micro enterprises through easing entry (licensing) requirements and improving access to credit and land.

The Government has also started to involve, and to encourage, the participation of the private sector in the policy dialogue and, have set-up a Public-Private Consultative Forum with the Chambers of Commerce and other relevant sectors. According to a survey made by the National Bank of Ethiopia, industry, particularly the private sector, recognizes the negative impact of competition from imports, the lack of access to credit or loans from banks, remoteness from the international market, market access problems in importing countries and, a shortage of skilled labour, on the performance of the private sector. Efforts to address these problems have to be enhanced both at national and international levels.

The balance of payments of Ethiopia has been very responsive to the recent price shocks in the international markets. For instance, the increase in oil prices imposed a sudden shift from a surplus of US$226.5 million in 2003/04, to a deficit of US$101.7 million in 2004/05. Imports of petroleum and petroleum products more than doubled in 2004/05 compared 2001/02. Imports excluding fuel, aircraft and cereals account for an average of 74 per cent of the total value of imports. As the increase in oil prices affects prices of imports other than fuel and cereals, it severely affected the trade balance of the country. As a result, the trade deficit for the year 2004/05 increased by 41.7 per cent from the previous year. Ethiopia’s trade needs to be further reformed in order to reduce its trade deficit. In spite of the price increases in the world market and quarterly price revisions, domestic oil prices remain nearly stable. A 1 per cent increase in oil prices is expected to induce a 62 per cent increase in the price of non-food items, according to estimates of the National Bank of Ethiopia.

Although petroleum imports showed an increase of 18.3 per cent from the previous year and, 55 per cent on all oil products, compared to prices in 2004[22], machinery and equipment, chemical products, transport equipment, raw materials and minerals dominate the overall imports of the country. Significant increases in imports of raw materials (89 per cent) and capital goods (125 per cent) were observed in 2004/05, compared to the previous year. It is expected that the expansion in industrial production and, the international price rise for metal products such as iron sheet and steel, are expected to further increase the value of imports into Ethiopia. The import of cereals was relatively stable while that of aircraft has slightly increased since 2003/04. Ethiopia has made significant reductions in import tariff rates and disparities. The quota system, contingency restrictions and seasonal tariffs, which were applied on used clothes and security/safety sensitive items, have been abolished.

[22] NBE, 2005. National Bank of Ethiopia Quarterly Report

Table 3

External Trade

	2001/02	2002/03	2003/04	2004/05
Exports FOB	**452**	**483**	**600.4**	**817.9**
coffee	163	165	223.5	335.4
Other	289	317	376.9	482.5
Imports	**1696**	**1858**	**2586.9**	**3633.2**
Fuel	267.7	287.7	310.5	668.7
Cereals	155.2	189.2	206.1	159.9
Aircraft	11.4	17.3	126.1	138.8
Imports (excluding above)	1261.5	1362.2	1944.1	2665.8
Trade Balance	**-1243**	**-1374**	**-1986.5**	**-2815.3**

Source: NBE

Export earnings have continued to depend heavily on a handful of primary commodities, namely coffee, pulses and oil seeds. The recent addition of horticulture to the export items of the country and, the export of flowers,[23] generated export earnings of Birr 4 million in 2003/04. Exports of goods and services as a share of GDP increased from 13 per cent in 2001/02 to 14 per cent in 2004/05. Merchandise exports were estimated at 8.8 per cent of GDP in 2004/05. In 2003/04 and 2004/05, the total value of exports grew by 25 per cent and 36 per cent, respectively.

In spite of its huge potential, the tourism industry of Ethiopia is underdeveloped. Although the Government managed to construct new airports at the main tourist sites and, to restore major cultural and historical assets, the contribution of the sector to the economy continued to be marginal as compared to its potential. The structural problems, such as poor accommodation, sanitation and road networks, as well as inadequate policy attention, are among the factors that limit the growth and expansion of the tourism sector. A stereotyped image of Ethiopia in tourist sending countries, the absence of a well thought out and effective tourist targeting strategy and, a lack of awareness about tourist sites, are further constraints that need to be effectively addressed if the sector is to contribute its share to the socio-economic development of the country. Regional and national political stability are also among the crucial factors necessary for the development of the tourism sector.

1.5 Commitment VI: Reducing Vulnerability and Protecting the Environment

Essential parts of the SDPRP and PASDEP deal with reducing vulnerability and protecting the environment. In addition to the achievements discussed in the context of SDPRP, the Government has enacted policies and strategies for protecting the environment. The objectives of these policies and strategies are to improve and enhance the health and quality of life of the population and, to promote the sustainable social and economic development of the country. The Government established the Ethiopian Environmental

[23] There has been an investment of 2.6 billion Birr (over US$300 million) in the flower industry that created many new jobs for the rural poor, especially for women.

Protection Authority (EPA) as the entity responsible for environmental issues and, enacted environmental proclamations, implementation guidelines and standards at the federal level, regarding the operation of environment protection institutions. The Government has initiated sectoral environmental impact assessments (for agriculture, industry, mining, and roads), social impact assessments and, resettlement guidelines. EPA has conducted 20 industrial and environmental audits and, is currently establishing its administration at the regional level.

A number of Government institutions are dealing with environmental issues, including the generation and dissemination of information. The Ethiopian Environmental Authority has the overall responsibility to ensure the appropriate implementation of the environmental policy. It networks with other government and non-governmental institutions to promote environmental protection. The Ethiopian Meteorological Authority is responsible for the collation, analysis and dissemination of metrological data. The decentralized early warning system was established recently to collate information on impending and chronic food shortages, as well as other natural and man made disasters. The Bio-diversity Institute is another Government organization that ensures the protection of the country's natural genetic resources including flora and fauna. It is necessary to establish information systems and reporting and monitoring mechanisms to assess efforts made by the various development institutions to implement policies and strategies at local levels. This will assist in the designing of appropriate interventions and policy measures to further promote the protection of the country's environment.

The recently adopted land use certification system, piloted in four regions, has entitled about 4 million farmers with land-use rights. This was believed to contribute to the conservation and better use of land and related resources, as security of tenure will enhance landholders' interest to invest for the future. Apart from this, further efforts made by development partners include attempts to address environmental concerns within their respective development programmes. The on-going agricultural extension programmes have at least partially addressed some of the objectives of the environmental concerns contained in the policy, such as soil and biodiversity conservation and, water resource management.

2 Assessment of international economic factors and support measures by development partners

The continued dependence of the Ethiopian economy on foreign assistance has remained one of the major development challenges facing the country. The country received Official Development Assistance of US$84.3 million in 2004/05, including under the HIPC initiative, which is about 1.14 per cent of the GDP. In addition, the Government was receiving direct budgetary support that constituted about 10 per cent of the total Government budget, mainly from the World Bank and the EU, until 2004/05. For 2005/06, the World Bank and the EU suspended their support, due to the current political crisis following the disputed election of May 2005. The inability of the Government to resolve the deadlock with the opposition led donors to suspend direct budget support amounting to US$375 million. This is expected to tighten public spending, particularly for the implementation of new projects, as well as the completion of donor funded projects which have already started. However, the World Bank and the EU have declared that they will continue their support to the poverty reduction goals and objectives, particularly for the development of infrastructure, including information and communication technologies and, capacity building for public and private sector development.

Ethiopia has received US$271.2 million from the HIPC debt relief since 2001/02. A considerable increase (91.7 per cent) in HPIC debt relief was acquired in 2002/03. Ethiopia has been able to service its debt over the last few years. However, its sustainability is uncertain in the coming years unless internal politics revert to normal and, the suspended development support is continued. Ethiopia may encounter serious financial limitations to achieve the goals set in the BPOA as well as the MDG, unless it proves its commitment to sustainable peace and good governance.

Private transfers have been increasing at an average annual rate of 32.7 per cent since 2001/02 i.e. from US$349 million in 2001/02 to US$811 million in 2004/05. Compared to the previous years, private transfers increased by 58.8 per cent. As can be seen from the table below, private transfers from NGOs have nearly doubled. The gradual increase in remittances, reaching about 61.6 per cent of the flow of total resources into the country, has significantly contributed to the reduction of the current account deficit, as it is more than five times the FDI inflows to Ethiopia. According to the NBE, Ethiopians abroad are making better use of official channels for international money transfers, such as through Western Union and Money Gram, in cooperation with domestic commercial Banks. Although not adequately assessed and recorded, unofficial transfers/remittances are still believed to be widely used.

Table 4

Foreign Direct Investment and Private Transfers

Particulars	2002/03	2003/04	2004/05
Foreign Direct Investment	123.3	150	150
Private Transfers	495,524	671,260	810,773
Receipts	511,224	690,218	828,096
NGO's	346,736	456,821	457,385
Cash	300,766	403,910	444,024
Other	8	7	0
Food	45,961	52,904	13,360
Private individuals	164,488	233,397	370,711
Cash	140,602	211,007	350,754
In kind	23,886	22,390	19,957

Source: NBE

With relation to market access, Ethiopia has been benefiting from the Africa Growth and Opportunity Act (AGOA) of the United States and, from the Every Thing But Arms (EBA) initiative of the European Union. Since January 2005, the USAID funded AGOA project has been actively working to promote Ethiopian exports to the United States by linking exporters, importers and potential investors in the United States. The AGOA had enabled Ethiopia to increase its value of exports from US$700,000 in 2000 to US$5 million in 2005. According to the project office in Ethiopia, about 50 per cent of the private companies participated in trade fares organized under AGOA and had established contacts with private businesses. They also participated in trade shows and accessed training and other technical and capacity building support. Some private companies from the textile and garments industry (five) and flower-producing firms (three) established contact with United States based private firms through the AGOA support. The project has also been able to increase its contacts from six in 2005 to 20 private companies at the beginning of 2006. Nearly, 50 per cent of these companies and private enterprises are owned by women. In addition to enhancing the linkage with private business, the project office of AGOA is focusing on re-branding and strengthening business relationship with the Ethiopian Diaspora in the United States.

Although data on the utilization of the market access opportunities from the Everything But Arms (EBA) initiative of the EU is lacking, the overall utilization of EBA has not shown significant change, with the exception of the initiation of sugar exports in the past few years. Sugar will be exported under EBA only after 2008, together with bananas, beef and other products. With a view to enhancing market access from EBA, the Government is working on an ACP-EU Economic Partnership Agreement based on the Diagnostic Trade Integration Study (DTIS) and, the Action Matrix of the Integrated Framework (IF), which identifies lack of diversification, trade and non-trade barriers, low supply capacity and weak trade support institutions and services, as key problems undermining the utilization of market access opportunities granted to Ethiopia.

In an effort to increase foreign direct investment (FDI), in 1991 the Government raised the minimum capital requirement of US$20 million on joint ventures. The recently revised investment law further reduces the minimum capital requirement for foreign investors with 75 per cent export proceeds to US$100,000. The upper limit of US$20 million applies to ventures in engineering, metallurgical, pharmaceutical, chemical and fertilizer industries. According to the National Bank of Ethiopia (NBE), FDI grew slowly from US$123 million in 2003/04 to US$150 million in 2004/05. Currently, foreign direct investment averages about 28 per cent of the capital account and 60 per cent of net long-term capital inflows. However, the capacity of FDI to finance the deficit of the current account balance has been declining since 2003/04 and, the Government will have to improve the policy environment to enhance and promote the role of FDI in the future.

The annual report of the NBE indicates that the amount of capital of approved investment projects increased from US$2.47 million[24] (Birr 21 million) in 2003/04 to US$1.29 billion (Birr 11 billion) in 2004/05. Similar reports indicate that the number of approved investment projects in the first quarter of 2005/06 increased by 51 per cent, compared to the same period in 2004/05. There were 749 approved investment projects in 2004/05. About 99.9 per cent of them are owned by private investors, of which 82 per cent are by Ethiopian nationals, while the remaining 18 per cent are owned by foreign investors. The amount of capital of these investment projects also increased by 730 per cent in the same reference period. This was attributed mainly to increased public investments in infrastructure, such as electricity, telecommunications and roads. According to the World Investment Review of Ethiopia (UNCTAD, 2005), foreign direct investment flows to Ethiopia increased from US$255 million in 2002 to US$545 million in 2004. FDI inflows in 2003/04 and 2004/05 were slightly more than 6 per cent of gross capital formation (gross domestic expenditure less private and public consumption expenditure). Further efforts are needed to deepen and sustain such positive trends by designing and

[24] USD 1 is considered to be about Birr 8.5 in this case.

implementing new investment policies and strategies to attract and to benefit from investment. Ethiopia applied to join the World Trade Organization (WTO) in 2003 and, the working party was established. The Ministry of trade has also established a Department of WTO that is working on capacity building, training, and research on WTO rules and, provides other relevant technical support. The memorandum of the foreign trade regime of Ethiopia has been completed and is awaiting the decision/appraisal of the Council of Ministers. The accession of Ethiopia to the WTO might assist the Government in reforming existing institutions and policies and /or, creating new institutions, including enacting new policies that are more favourable to investment and enterprise development.

Conclusions and policy lessons

The Ethiopian government had been making efforts to attain good governance and democracy prior to the May 2005 election, which created ample opportunities for people to participate in the election process. The support of development partners in enhancing governance, particularly in building the democratic process, has been tremendous, although the results have been shadowed by post-election instabilities. There is a need to put the process of democratization back on track and, to reform polices, if the country is to move towards attaining the goal of poverty reduction.

The Ethiopian Government has registered notable successes in changing the overall access and availability of safe water supplies, in constructing road networks, expanding telecommunications services and education. Even though the economy continues to be highly dependent on external assistance and, vulnerable to external shocks, with the support of its international partners, the Government has managed to maintain macroeconomic stability. Through prudent fiscal management and macroeconomic stability, the Government has been able to increase spending on sectors oriented towards poverty reduction objectives such as education, health, and agriculture. The contribution of debt relief in enhancing public spending in these sectors was substantial.

In addition, the Government has set up decentralized administrative structures. Consultations at the grassroots level with the public, including the CSO, in the design and implementation of development policies and strategies, has shown a remarkable improvement. The consultative and monitoring process with development partners has been enhanced in planning national development programmes and projects. The Government has also managed to reorient and provide support for cooperatives and, recently provided basic infrastructure to flower growers and exporters. Although Ethiopia has only recently started to benefit from various preferential market access initiatives, encouraging signs are being observed in terms of developing linkages with international business promoters and investors.

Due to weak institutions to implement policies and strategies and, the structural problems of the economy of the country, Ethiopia will not be in a position to attain all the goals and targets of the MDGS and the PoA, although efforts are underway to meet some of the gaols and targets. For Ethiopia to meet the goals and targets of the MDGS and the PoA, as well as those contained in its SDRSP, by 2015, the following national and international measures and actions should be taken as urgently as possible.

At the national level:

- The Government needs to restore peace and security (internal and with neighbouring Eritrea), which have become major concerns for regional and national political stability. A deliberate and genuine commitment by the Government to continue to promote good governance, durable peace and stability, is indispensable to reduce the political instability that has continued in various parts of the country.

- In addition to smoothing the local political environment for effective economic activity, durable peace and stability needs to be in place for mobilizing the necessary resources for the implementation of the PASDEP and other development programmes. The Government and opposition parties need to quickly resolve their current political deadlock.

There is an urgent need to refine and adopt more liberal economic reforms, including legislation related to security of tenure, the privatization of Government controlled industries and enterprises, the distribution and transport sectors, power and communications, as well as the financial sectors.

- While increasing coverage of public and/or social services is vital to socio-economic progress, the provision of services with adequate quality is equally necessary to sustain the achievements in the poverty reduction programmes. To that effect, the Government, in collaboration with the private sector, needs to ensure the provision of quality services in education, health and other public services.

- In addition to the above, the Government needs to align policy directions, including mainstreaming trade and development, into national policies and strategies as a necessary step to eradicate poverty. This requires focusing on building productive capacities, availing private business development services, improving overall competitiveness of the economy and, ensuring good governance, democracy and the rule of law.

- Although agriculture remains the major preoccupation of the current policies, the Government needs to give adequate attention to other sectors such as industry and tourism.

- To mobilize adequate finance from local sources, the Government needs to promote the private sector by facilitating access to, and putting in place, the necessary infrastructure, such as water, electricity and road networks, which are essential for enhancing the returns from trade. It is also crucial to explore sectors that have the potential for more returns on investment such as tourism.

- Improving access to loans and credit and, narrowing the digital divide, is critical for the expansion and growth of the private sector and, for taking advantage of trade opportunities in external markets. This requires the provision of market based incentives and, improving industry standards in other areas that warrant the emphasis of the Government and its partners.

- Enhancing and/or setting up information systems to track changes in the external trade sector is necessary for Ethiopia to assess its position and, available opportunities for enhanced trade, as a key to attaining the goals and targets of the MDGs, the BPOA and the SDPRP.

At the international level:

- Development partners should continue to improve the quality and quantity of development assistance to Ethiopia. There is a need for increased aid to develop supply capacities. In commodity-dependent economies such as that of Ethiopia, international assistance is needed to help diversification and, increase local capacities for value-added processing. International development partners should meet the targets for ODA of from 0.15 per cent to 0.2 per cent of GNI to the LDCs as agreed at the Brussels Conference.

- Ethiopia has not fully benefited from the preferential market access schemes of developed and other developing countries. Such trade preferences still have an important role to play and, should be strengthened through such measures as improvements in rules of origin, to reflect existing production structures. Improvement in supply capacities is at the heart of the problem of making trade work more effectively for poverty reduction.

- Ethiopia has been benefiting from debt relief measures both from bilateral and multilateral creditors, including through the HIPCs. Despite various initiatives to eliminate the debt burden of the country, external debt remains a major problem. Further comprehensive debt reduction is essential for poverty reduction and, for achieving the goals and targets of the BPOA, MDGS and, the goals contained in national polices and strategies.

- Donor support for the development of infrastructure, especially transit-transport facilitation and, improved road networks for land locked countries such as Ethiopia, is critical.

- Technical assistance in the area of trade capacity-building needs to be further strengthened. Support to develop the ICT infrastructure and, to improve access to information, marketing skills and the building of market- linkages is critical in improving the productive capacities of the country.

- Development cooperation aimed at providing long-term support in terms of resource mobilization is critical for enhancing the impact of trade on poverty reduction.

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