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THE CORPORATE COUNCIL ON AFRICA

The Corporate Council on Africa

Critical Issues

A Guide for U.S. Businesses: Ethiopia

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The Corporate Council on Africa

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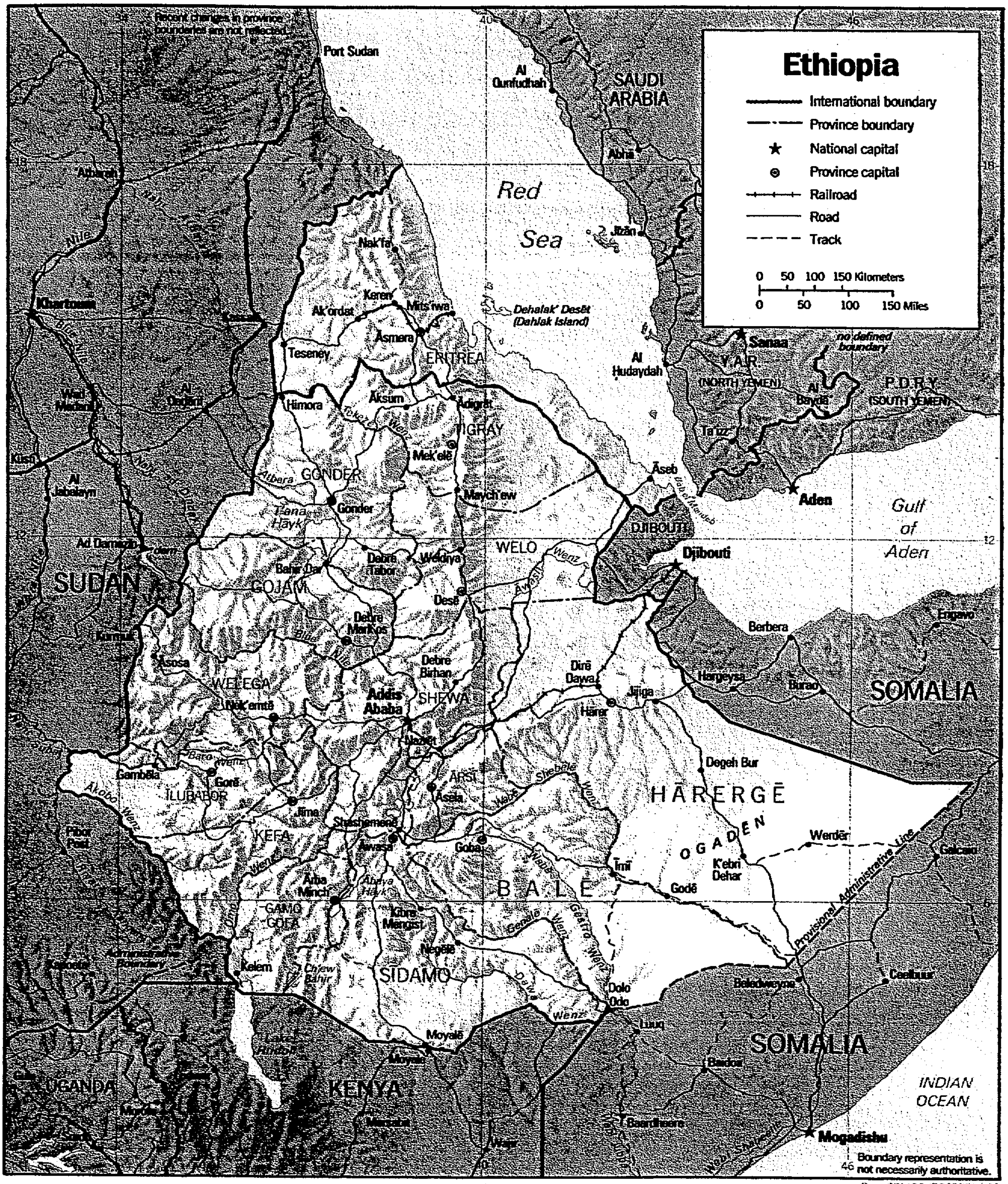
Ethiopia
International boundary
Province boundary
National capital
Province capital
Railroad
Road
Track
0 50 100 150 Kilometers
0 50 100 150 Miles
Recent changes in province boundaries are not reflected.
Red Sea
Gulf of Aden
INDIAN OCEAN
SUDAN
SAUDI ARABIA
DJIBOUTI
SOMALIA
KENYA
UGANDA
Y.A.R. (NORTH YEMEN)
P.D.R.Y. (SOUTH YEMEN)
no defined boundary
ERITREA
TIGRAY
GONDER
WELO
GOJAM
WELEGA
SHEWA
ILUBABOR
KEFA
ARSI
BALE
HARERGE
GAMO GOFA
SIDAMO
OGADEN
Provisional Administrative Line
Port Sudan
Al Qunfudhah
Abha
Jizan
Nak'fa
Keren
Mits'iwa
Ak'ordat
Asmera
Teseney
Dehalak' Desēt (Dahlak Island)
Sanaa
Al Hudaydah
Al Bayda
Ta'izz
Aden
Āseb
Himora
Āksum
Ādigrat
Mek'elē
Maych'ew
Gonder
Tana Hayk
Bahir Dar
Debre Tabor
Weldiya
Desē
Djibouti
Berbera
Hargeysa
Burao
Debre Markos
Debre Birhan
Addis Ababa
Dirē Dawa
Jijiga
Harer
Āsosa
Nek'emtē
Nazrēt
Gambēla
Gorē
Jīma
Āsela
Shashemenē
Awasa
Goba
Degeh Bur
Werder
K'ebri Dehar
Imī
Godē
Arba Minch
Abaya Hayk'
Kibre Mengist
Negēlē
Kelem
Chew Bahir
Moyalē
Dolo Odo
Luuq
Khartoum
Wad Medani
Al Qadarif
Kusti
Al Jabalayn
Ad Damazin
Kurmuk
Atbarah
Pibor Post
Lake Rudolf
Baardheere
Baidoa
Beledweyne
Galcaio
Ceelbuur
Erigavo
Mogadishu
Boundary representation is not necessarily authoritative.

C

ETHIOPIA **BASIC INDICATORS**

Geography	
Area	1,127,127 sq. km.
Comparative Size	Slightly twice the size of Texas
Land Boundaries	5,311 km - Djibouti, Eritrea, Kenya, Somalia, Sudan
Coastline	None - landlocked
Climate	Tropical monsoon with wide topographic variation
Natural Resources	Gold, platinum, copper, potash
People	
Population	55.9 million (1995 est.)
Growth Rate	3.09% (1995 est.)
Language	Amharic (official), English, Oromigna, Tigrigna, Arabic
Literacy	24%
Government	
Type	Federal Democratic Republic
Prime Minister - Head of State	Meles Zenawi
President	Negasso Gidada
Legislative Branch/Judicial Branch	Bicameral/Federal Supreme Court
Political Parties	EPRDF ruling coalition; a number of smaller parties
Economy	
National Product	GDP purchasing power equivalent $20.3 billion
National Product Real Growth Rate	3% (1994 est.)
GDP per capita	$130 (1993 est.)
Consumer Price Index	10% Fiscal Year 93/94
Unemployment Rate	30%
Budget (FY 93/94)	Revenues - $1.2 billion Expenditures - $1.7 billion
Exports (1993 est.)	$219.8 million (f.o.b.)
Imports (1993 est.)	$1.04 billion (c.i.f.)
External Debt (1993 est.)	$3.9 billion
Currency	1 Birr (Br) = 100 Centim
Exchange Rate (Br per US$)	6.35 (3/96), 5.95 (1994), 5.0 (fixed rate 1992-93)

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Introduction

Ethiopia is strategically located in the heart of the Horn of Africa forming a bridge between the Middle East and the rest of Africa. Somalia lies to the southeast, Sudan to the west, Eritrea to the north, Djibouti to the northeast and Kenya to the south. The country covers approximately 1,127,127 square kilometers and is about twice the size of Texas. With Eritrea gaining independence in 1993, Ethiopia relies on its neighbors, Djibouti and Eritrea for access to the Red sea. The climate is mainly temperate because of the high plateau terrain, with an average annual temperature of 55° F, abundant rainfall in some years and low humidity. The lower country and valley gorges are very hot and subject to recurrent drought.

Ethiopia is a veritable melting pot of ancient Middle Eastern and African cultures as evidenced by the religious, ethnic and language composition of its Semitic, Cushitic, Omotic and Nilotic peoples. About seventy to eighty different national languages are spoken. Amharigna, Oromiffa and Tigrigna are used by about two-thirds of the population with Amharigna as the official language of the Federal Government. English is the medium of instruction in the secondary schools, colleges and universities, and is widely used in business.

As host to the Organization of African Unity (OAU) and the United Nations Economic Commission for Africa (ECA), the capital city of Addis Ababa is a veritable focal point of international diplomacy, commerce and development. Additional centers for trade and industry in Ethiopia are: Awassa, Dire Dawa, Gondar, Dessie, Nazareth, Jimma, Harar, Bahir Dar, Mekele, Debre Markos and Nekemte. All of these towns are connected to Addis Ababa by asphalt and gravel roads.

The country is emerging at a rapid rate from a devastating period of totalitarian marxist rule under Lt. Colonel Mengistu Haile Mariam and almost two decades of civil war which ended in April 1991. The recent estimate of GDP per capita as reported by the World Bank stands at US$130 which places Ethiopia amongst the poorest countries in Africa. Nevertheless, Ethiopia's access to regional markets in Africa and the Middle East, coupled with its own substantial population of 55.9 million, vividly illustrate the country's economic potential.

Ethiopia's vast agricultural, mineral, tourism and energy resources are virtually untapped as a result of the civil war and an economically stagnant period which ended when the transitional government came to power in 1991. The Ethiopian People's Revolutionary Democratic Front (EPRDF) was part of the Transitional Government of Ethiopia (TGE) from May 1991 to August 1995. The EPRDF is a coalition party comprised of the Tigray People's Liberation Front (TPLF), the Oromo People's Democratic Organization (OPDO) and Democratic Forces of Southern Peoples (DFSF). There are about 60 smaller parties which participate in the political process of the country both at the federal and regional levels.

The present constitution establishes a parliamentary system and adheres to the basic principles of human rights of the UN Convention. The country is divided into nine federal states which are vested with power for self-administration. The new EPRDF government under the leadership of Prime Minister Meles Zenawi, has embarked on a program of economic liberalization featuring deregulation of prices and markets as well as promotion of the private sector.

Despite the many hurdles to overcome, progress is visible. Several factors have contributed to a rising flow of private sector investment in Ethiopia. Among the most salient are: the end of the civil war in 1991; peaceful democratic elections in 1995; a drive toward privatization of former state-owned enterprises; the enactment in 1992 of a liberal investment code which provides incentives for both foreign and domestic private sector investment; emphasis on diversification of the economy to capitalize under-utilized comparative advantages in the mining and tourism sectors.

Economic performance, measured by growth in GDP, has steadily improved from an annual average of 1.2 percent during the pre-reform period to 6.2 percent per annum during FY93-95. Real interest rates, which were negative throughout the 1980's, became positive during the reform period and have averaged around 1 percent per annum in the past few years. Real GDP is expected to grow about 6 percent for FY96-98. However, efforts to improve the country's social welfare could be hampered by the high population growth rate which stands at 3.1 percent per year.

Hence, good progress has been made in stabilization, particularly in lowering the rate of inflation. The economy has responded favorably to the change in policy direction, and to the injection of resources provided by the donor community.

Although urban unemployment and underemployment are high, it is somewhat offset by the parallel economy which has expanded massively since decontrols on trade have been implemented. Nevertheless, over 200,000 largely unskilled young men have entered the labor market following military demobilization who will have to be absorbed. In 1993, the Addis Ababa-based UN Economic Commission for Africa estimated that 30 percent of the Ethiopian workforce was unemployed. The government has established social safety nets to reintegrate displaced people and demobilized soldiers into their communities and provide training and employment for the disabled and orphans. Resources have been shifted substantially toward providing basic social and economic services and away from military uses.

The Economic Reform Program (ERP) 1992 - Present

At the core of economic recovery is the Economic Reform Program (ERP) which was launched with World Bank structural adjustment support in 1992. The program mandated devaluation, tariff and transport reforms, as well as the deregulation of agricultural marketing. Western donors strongly backed the program. Despite devaluation, inflation has remained remarkably low. Although poor rains curbed growth in 1993/4, and disagreements persist over issues such as land tenure and privatization, both donors and the government remain confident that reforms designed to promote a private, market-based economy are on track.

In 1992, the World Bank led a multi-donor Emergency Recovery and Reconstruction Project (ERRP) involving a consortium of nine donors, to help re-start economic activity and rebuild essential social and physical infrastructure. In addition, given the critical role of agriculture, the Government launched a long-term strategy based on Agricultural-Development-Led Industrialization (ADLI). Specifically, agricultural production is to be increased by improving productivity of small-holder farms, and by encouraging large-scale private commercial farms especially in the lowlands. Components of the Economic Reform Program include:

Price control deregulation. All retail prices, except petroleum, fertilizers and pharmaceuticals have been decontrolled.

Privatization. Results of the first round of sales of state-owned enterprises (SOEs) began in earnest in early 1995. A total of 16 companies, mostly hotels, restaurants and food processing plants, notably flour mills, have been sold. They are the first of 144 SOEs listed for privatization. Later that year, the Ethiopian Privatization Agency (EPA) raised $53 million from the second round of sales which included the Coca-Cola and Pepsi-Cola bottling plants. The Pepsi-Cola plants in Addis Ababa and the northern towns of Gondar and Tessi, were sold to an Ethiopian/Saudi businessman. The Coca Cola plant in Addis Ababa was also sold to SOFCAM, an Ethiopian company.

Fiscal policy. The primary fiscal deficit after grants was reduced from an average of 8.5 percent of GDP per annum during the pre-reform period to 4.2 percent during FY93-95.

Financial sector reform. The financial sector is no longer restricted to government control. Both the banking and insurance sectors are open to participation by the domestic private sector. The National Bank of Ethiopia acts exclusively as a Central Bank, whereas commercial operations have been spun off to several private banks. Five private insurance companies have been operating since early 1995.

Foreign exchange. As part of the ERP, Ethiopia adopted a market-based exchange rate system. Fortnightly foreign exchange auctions that have been held since May 1993 have steadily narrowed the gap between the parallel rate and the auction rate.

The Bilateral Political Environment

The groundwork laid by the transition government combined with recent successful elections in Ethiopia have helped to cement good relations with international donors and foreign commercial partners. Saudi Arabia is Ethiopia's largest source of foreign investment followed by Kuwait and South Korea. Ethiopia is the 6th largest U.S. export market in sub-Saharan Africa.

Although relations with neighboring Sudan have deteriorated due to alleged Sudanese involvement in the attack on Egyptian president, Hosni Mubarak, in Addis Ababa on June 26, 1995, this does not threaten long-term stability. In addition to being host to the OAU and ECA, Ethiopia is a member of several regional and international organizations for political and economic cooperation such as The Common Market for Eastern and Southern Africa (COMESA), the OAU, UN and World Bank and IMF.

Economic Prospects

In addition to internal political and economic pressures several external factors will influence Ethiopia's economic performance over the next decade:

- ability of the government to keep liberal reforms on track, address social and labor issues, and maintain support from the international donor and financial community.

- ability to attract foreign direct investment and accelerate private sector development.

- steady economic growth and political stability in the Horn of Africa.

In the foreseeable future, Ethiopia will remain heavily reliant on its traditional primary exports such as coffee, hides and skins, and earnings from services such as Ethiopian Airlines. However, with an influx of foreign investment and progress in privatization and continued macro-economic stability, the mining, tourism, energy and light manufacturing sectors hold considerable promise as sources of growth.

Moreover, prospects of developing export-oriented and labor-intensive manufacturing should not be underestimated. There is potential for diversification in leather products, textiles, light manufacturing goods and gold, as well as agricultural exports such as pulses and oilseeds. Ethiopia's competitive edge lies in its access to regional markets in east and southern Africa, the Middle East and in its own 55.9 million strong population.

Private Enterprise

Despite recent successes in privatization and increased foreign investment, Ethiopia will continue to be aid-dependent for years. Ethiopia's small but emerging private sector comprises three groups:

1. **Multinational sector.** The multinational corporations operating in Ethiopia are dominated by European, Asian, and Saudi Arabian firms. However, U.S. companies also have a considerable presence and are poised to expand.

2. **Indigenous business sector.** More than 16 newly privatized, small and medium-sized companies as well as thousands of small shops owned and operated by Ethiopians, are revitalizing this sector.

3. **Informal sector.** This group comprises small subsistence farmers, local handicraft traders, small commercial business and service providers. The importance of the informal sector in the Ethiopian economy should not be underestimated but reliable data to measure its vitality and impact is not yet available.

The Case for Doing Business with Ethiopia

The business climate in Ethiopia is encouraging. The Government is working to create an enabling environment for private sector investment by: tightening fiscal policy thereby reducing internal imbalances and inflation, adopting a market-based exchange rate system, reforming its public expenditures, embarking on a privatization program, and inducing foreign direct investment through a number of tax and monetary incentives. Those who have invested time and money in Ethiopia report the following reasons for optimism:

Strengthening political stability. After almost two decades of military rule and civil conflict, Ethiopia is at peace with itself and with newly independent Eritrea. The freely-elected Government is in the process of strengthening federal institutions such as the judiciary and the armed forces while devolving considerable administrative and budgetary responsibilities to the nine regions.

Pent up demand. The combination of war, central planning and disinvestment over the last two decades has severely hampered Ethiopia's industrial base. The demand is great for imports of everything from consumer goods to fuel. Trade opportunities exist in construction; agricultural, telecommunications and industrial equipment; computers; pharmaceuticals and agricultural commodities.

Government support. In addition to the Corporate Council on Africa, U.S. businesses can receive support from the Department of Commerce offices in the U.S. as well as in Ethiopia through the U.S. Embassy. Investors and importers can also contact the Investment Office of Ethiopia (IOE) in Addis Ababa. In addition, direct contact with senior government officials facilitates understanding and long-term business relationships.

Expanded co-financing and financial support. Even though exporters to Ethiopia will not find U.S. EXIMBANK open for financing most trade activities, IFC, MIGA and OPIC can insure and guarantee investments in the country.

Business Opportunities

The thrust of Ethiopia's economic recovery program is toward a more market-driven, competitive environment. The large internal and regional consumer market coupled with Ethiopia's need for capital and technical expertise to exploit its resources and rebuild its vital infrastructure, exemplify the range of business opportunities for U.S. enterprises. The areas with greatest potential include:

- **Infrastructure building and maintenance.** U.S. contractors are encouraged to collaborate with Ethiopian firms in the construction and rehabilitation of the airport and road network. In addition, air, rail and marine transport services, as well as numerous irrigation projects will require sought-after U.S. machinery and technical expertise.

- **Computers and telecommunications equipment.** Demand for computers and peripherals, as well as supply and installation of telecommunications equipment provide excellent opportunities for U.S. companies.

- **Consumer goods and manufacturing equipment.** The consumer goods market is robust with almost 17 percent of all imports conducted by Government tender. With a population of 55 million consumers pre-disposed to American products, opportunities abound for U.S. suppliers. Industrial machinery and parts are also in demand as Ethiopia upgrades its light manufacturing sector.

- **Pharmaceuticals, veterinary drugs and supplies.** The local production of pharmaceuticals and drugs is practically non-existent in Ethiopia. Large-scale manufacturing of pharmaceuticals is envisioned to be of strategic importance. Full private participation in small and medium-scale enterprises for the manufacturing of pharmaceuticals is encouraged. In addition, given the salient role that livestock plays in the economy, there is a constant need for veterinary drugs and supplies.

- **Mining, oil and gas exploration.** Incentives in this priority sector are particularly attractive for investors. Significant opportunities lie in gold, tantalum, soda ash, potash, nickel and platinum as well as oil and natural gas exploration and development.

- **Tourism.** The Government is actively seeking investment in hotel and resort projects. Ethiopia's natural and historic treasures are as yet unknown to much of the outside world. The ancient castles, monasteries, diverse landscape, exotic wildlife and birdlife have the potential to attract tourists from all over. However, due to proximity and convenient flight connections, travelers from the Middle East and Europe are a natural target market.

- **Agriculture and agro-processing.** Agriculture is the backbone of the Ethiopian economy. To bolster productivity in this sector, a variety of inputs and services that

U.S. companies are well-suited to supply will be needed. Fertilizers, agricultural chemicals, pesticides and equipment are in demand. Production of cash crops such as coffee, tea, tobacco and cotton is a priority. Fish farming as well as the processing of horticultural products, poultry and livestock constitute key areas for cooperation with American firms.

Investors can also take advantage of Ethiopia's preferential access to international markets. Participation in the Lomé Convention gives access to the markets of the EU, while adherence to the Common Market for Eastern and Southern Africa (COMESA) provides a gateway to over 22 countries in the region.

U.S. Enterprise in Ethiopia

U.S. investment is beginning to increase with significant interest in mining, energy and tourism development. A construction project for a sugar refinery in the Finchaa Valley about 285 kilometers northwest of Addis Ababa was recently awarded to the U.S. firm F.C. Schaffer-Servtech. It is one of the largest contracts of its kind ever to be awarded to a U.S. company. In addition, a number of American firms have established branch offices in Addis Ababa such as Mobil Oil, AT&T, Coca Cola, Pepsi-Cola, Hunt Oil and many others listed in Appendix B.

The Regulation of Foreign Investment

The Ethiopian Government is wooing foreign investors with a liberal foreign investment code enacted in 1992. The equivalent of a one-stop-shop for investors, the Investment Office of Ethiopia (IOE), was established to facilitate the bureaucratic process of project registration and approval. Some incentives embodied in the legislation are:

- Remittance of funds in foreign exchange to transfer profits, dividends and royalties.
- Exemptions from payment of import customs duties.
- Exemptions from payment of export customs duties (except coffee).
- Deductions for research and development activities.
- Exemption from payment of taxes on remittance of capital.
- Export retention scheme.

Joint Ventures

Legislation permits 100 percent ownership, however, the Government prefers joint-ventures that enable Ethiopians to participate in the ownership and management of businesses. The private sector is organized in Addis Ababa through the Ethiopian Chamber of Commerce and a number of other industrial and sector-specific associations. A U.S. company seeking a joint venture partner should avail itself of all resources including the Economic Commercial Officer at the U.S. Embassy, the Investment Office of Ethiopia, the banks and business associations. In addition, there is a sizeable well-organized and qualified expatriate community in the U.S. which might be a source of potential partners. The Corporate Council on Africa in Washington D.C. liaises with the Ethiopian Community in the U.S. and can assist potential commercial partners with match-making upon request. More detailed information about business opportunities by economic sub-sector is included in Chapter 3. Constraints on foreign investment are addressed in Chapter 6.

The Policy Environment

The improved policy environment has started to have a visible beneficial impact on the living conditions of Ethiopians as well as provide incentives to the private sector. Real GDP grew by more than 6.2 percent per annum during FY93-95 compared to 1.2 percent during the pre-reform period. The underlying conditions for economic growth have begun to show signs of improvement. It is estimated that the investment to GDP ratio increased from a low of 11 percent prior to reforms to more than 16 percent in FY95. A key force in driving the investment ratio is the expansion of private sector activities. The share of private investment in total investment increased from 17 percent in the pre-reform period to about 25 percent during the reform period. In addition, the issuing of proclamation No. 7/1992 for the establishment of regional/national self governments with extensive political and economic powers, created a conducive environment for the revitalization of the economy.

Monetary Policy and Financial Sector Reform

Staying the course in stabilization and deepening structural reforms will require continuous effort by the Government. Positive real interest rates have been achieved and will need to be maintained. Average annual inflation for FY93-95 was reduced to 8 percent.

Trade Liberalization

The trade regime continues to be liberalized. In late 1992, the Ethiopian Government announced a complete overhaul of tariffs on foreign trade. These included substantial cuts in customs tariffs and in the sales tax on imported goods, bringing them into line with rates applicable to domestic goods.

Exchange Rate Policy

Ethiopia adopted a market-based exchange rate system which saw the domestic currency depreciate from Birr 2.07 to one US$ during the 1980's to an average of Birr 6.2 to one US$ in FY95. As a result, the balance of payments has improved and the level of foreign exchange reserves increased. To close the gap between the official and parallel exchange rates, the Ethiopian Government introduced a system of biweekly foreign exchange auctions in May 1993.

Deregulation

Deregulation of state participation in the economy over the last five years has been significant. However, privatization of state-owned enterprises (SOEs) has only just begun. Export taxes for all commodities but coffee have been eliminated, and import duties have been substantially reduced. The state has abolished the parastatal monopoly in coffee marketing. Domestic private participation in freight forwarding and clearing has been allowed and banking and insurance activities are now open to the domestic private sector.

Investment Promotion

The Ethiopian Government promulgated a new Investment Code in May 1992 and created the Investment Office of Ethiopia (IOE). The Code which is considered to be more liberal than the previous one, opens all but large-scale energy projects, transport and financial services to foreign investors. Subject to a minimum investment of $500,000, investors are allowed up to 100 percent foreign equity holdings. This amount may be lowered to $125,000 in special circumstances that entail priority investments or the transfer and development of suitable technology and know-how. Additional incentives include tax breaks of up to three years for new investment and reinvested profits, as well as tax-free importation of up to 15 percent of productive capital for any new projects. All foreign investments in Ethiopia require the approval of the IOE in the form of an "Investment Certificate". The Investment Code requires that the IOE approve investment proposals within 10 days of official receipt of the forms. IOE offices have been established in all 9 regions.

Liberalization of Price and Distribution Controls

Significant steps forward have been taken toward liberalizing the Ethiopian economy. All retail prices, except petroleum, fertilizer and pharmaceuticals have been de-controlled. Export taxes, except coffee, have been eliminated, and license fees have been substantially reduced for coffee exporters. In 1993, maximum import duties were reduced from 230 percent to 60 percent, and while still high, they are much less onerous than before. The Corporate Council on Africa (CCA) will continue to monitor the Ethiopian Government's trend to liberalize the economy.

Agricultural Prices and Marketing

The monopoly of most marketing boards has been abolished, enabling farmers to sell their crops to the highest bidder. Parts of the market for agricultural inputs were liberalized, and coffee marketing has been opened to competition.

Labor Market Regulations

The Government sets the minimum wages for public sector employees. Labor unions may belong to the Confederation of Ethiopian Trade Unions (CETU) established in 1993.

Balance of Payments

Ethiopia's balance of payments has been affected by weather conditions, terms of trade, the civil war, change of government, and emergency relief and rehabilitation efforts provided by the international community. Developments in 1991/92 reflected the initial recovery and reconstruction following the new government in May 1991. In 1992/93, the balance of payments was influenced by stabilization and structural policies that consisted of a major devaluation, greater availability of and access to foreign exchange by the private sector, and liberalization of the foreign trade and domestic marketing systems.

Prospects for the Reform Program

Several factors influence the success of Ethiopia's reform efforts:

- **Extent of political commitment**

The Government has stated its intention to continue to support structural reforms. These reforms cover wide-ranging areas including restructuring and privatizing public enterprises, developing competitive and diversified financial markets, further reducing the variance and the level of import tariffs, improving export incentives and rendering the policy environment conducive to private sector development.

- **Consolidation of regional administration**

The concept of decentralization was introduced three years ago by the Transitional Government. Under the federal system, progressive devolution of power to the regions is taking place.

- **Adequate financing**

Despite its thrust to attract foreign investment, Ethiopia will continue to depend on the international donor community for concessional financing. Nonetheless, Ethiopia has demonstrated its seriousness in improving its external debt situation and credit-worthiness by obtaining favorable debt from the Paris Club in December 1992, and reducing its debt service ratio from 82 percent in FY92 to 30 percent in FY95. Private sector-led development and structural reforms are slated to continue.

- **Privatization and deregulation**

The Government is reviewing the legal and regulatory framework to remove impediments to private sector activities. The recently established Privatization Agency is developing a plan and timetable for public enterprises to be divested and defining the modalities of privatization (sales, leases or management contracts). To date, Ethiopia's privatizations have not included divestiture of the public telephone service which cannot meet demand and is a serious impediment to increased foreign investment.

Chapter 1

Political Background

1.1 History, Government and Politics

Ethiopia is the only African country which was not colonized by European colonial forces. It was only briefly occupied by the Italians between 1936 - 1941. The first recorded account of the region was about 4,800 years ago during the time of the Egyptian pharaohs. Despite the overwhelmingly Christian nature of the ancient Axumite Empire, Islam penetrated Ethiopia in the 7th century during the life of the prophet Mohammed. Nonetheless, the Ethiopian Orthodox Church, an ancient branch of Christianity, prevailed as the dominant religion. Between 1889 and 1913, the Christian Emperor, Menelik II reigned. Emperor Menelik was succeeded by Haile Selassie who became regent in 1916, King in 1928 and Emperor in 1930. Selassie ruled Ethiopia for over 50 years, interrupted only by the brief Italian occupation between 1936 - 1941. He was finally deposed by the armed forces in 1974 in the wake of serious famine, economic turmoil, and increasing demands for democratic reform. A captive of the military regime, Haile Selassie was presumably executed in 1975.

Since civilian groups lacked the cohesion to mobilize support, the Provisional Military Administrative Council (PMAC, Dergue in Amharic) filled the power vacuum and began 17 years of military rule. In 1974, Ethiopia was declared a socialist state. Land, financial institutions and large industrial companies were nationalized and peasant co-operatives were introduced. However, internal power struggles racked the PMAC resulting in purges among the leadership that propelled Colonel Mengistu Haile Mariam to power in 1977. During 1977 and 1978, in an attempt to end political opposition to the regime, the government imprisoned or killed tens of thousands of its opponents, primarily intellectuals. This period came to be known as the "red terror," and it tragically deprived Ethiopia of a generation of educated cadres.

In May 1991, the Ethiopian Peoples Revolutionary Democratic Front (EPRDF), a coalition of political groups dominated by the Tigray People's Liberation Front (TPLF), toppled the Marxist-Leninist regime of President Mengistu Haile-Mariam, who fled into exile in Zimbabwe. The Transitional Government of Ethiopia (TGE), founded by the EPRDF, carried out a democratization program which provided Ethiopians with greater political freedoms than at any previous time in the nation's history. EPRDF Chairman Meles Zenawi was unanimously elected President during the Transitional Government. In 1994, a constituent Assembly drafted a democratic Constitution which was adopted in December that same year.

Then, in May and June of 1995, Ethiopia held national and regional elections deemed generally free and fair by the international community. The four-year old Transitional Government (TGE) handed over power to the elected government of the Federal Democratic Republic of Ethiopia (FDRE) in August 1995. However, since most opposition groups chose to boycott the elections despite their freedom to participate, the EPRDF won a landslide victory. A corresponding shift of executive authority occurred from the Presidency to the Prime Minister. Former President Meles Zenawi was elevated to the post of Prime Minister. There are 17 cabinet members.

The Ethiopian model of democracy is based on proportional representation with two houses of parliament: a 547-member Council of People's Representatives directly elected by districts and the Federal Council whose members represent the interests of the nine regional states in the federation.

1.2 Regionalization Policy and Party Politics

A policy of decentralization is the pivotal feature of Ethiopia's overall institutional reform program. A new federal system which devolves power to nine ethnically-defined regional governments, was introduced in 1992. The regions have become the core units of the new political system. This is a major departure from the highly centralist regimes that ruled Ethiopia for generations. It is designed to respond to the aspirations of various ethnic groups for a larger degree of control over their own affairs. The move toward regionalization was championed by the TPLF, the dominant political party within the EPRDF coalition. The Amhara National Democratic Movement (ANDM), the Oromo People's Democratic Organization (OPDO) and the Democratic Front of Southern People's (DFSP), comprise the remaining components of the ruling EPRDF.

Nonetheless, not all political parties were initially in favor of the regionalization program. The Oromo Liberation Front (OLF), which shared power with the EPRDF in the transitional government, withdrew in 1992 as a result of disagreements over the first regional elections. The policy has engendered animosity among some elites who previously held centralized power in Ethiopia.

Despite imbalances (states have disparate economies, populations and territories), the regions are consolidating their administrative roles. This is the third fiscal year in which the regions have managed their own budgets. The Government is closely monitoring the regionalization process to ensure equity.

1.3 Human Rights

The U.S. Department of State's recently released human rights report on Ethiopia registered concern over continued human rights abuses particularly with regard to the security forces. However, the report also acknowledged significant improvements such as progress toward enhancing the quality and performance of independent national and regional police forces.

Another area singled out for criticism was the judicial system which remains weak, understaffed and at times subject to political influence. The Government is cognizant of these deficiencies and is taking concrete steps to restructure the courts and reform the police forces. Moreover, President Gidada recently announced the formation of a Human Rights Commission.

1.4 Corruption

The amount of corruption in Ethiopia is almost negligible. It may occur from time to time at the mid to lower levels of the civil service. However, rarely does it appear within the higher echelons of the bureaucracy. As testimony to the Government's commitment to rooting out corruption, officials have been known to lose their jobs if found guilty of succumbing to bribery. This official stance against corruption, coupled with the absence of a colonial legacy and the fact that indigenous Ethiopians own and manage the majority of businesses (as opposed to expatriates from other countries) thus reducing the rationale for bribes, may explain the absence of a corruption factor.

1.5 Freedom of Expression

While the Constitution and 1992 Press Law provide for the right to free speech and press, the Government sometimes restricts these freedoms in practice. Radio, the most influential medium in reaching rural populations, is controlled by the Government as is the sole television station. However, in August 1995, following the Ministry of Information's merger with the Ministry of Culture, the Government announced that the official press would be "autonomous" from the new Ministry. Moreover, the Government has established a task force to work on a national information policy. Plans for creation of a training center for journalists underscore the Government's willingness to fortify and institutionalize freedom of speech and press. Currently, about 1 percent of Ethiopians have regular access to any newspaper or magazine. Citizens outside Addis Ababa have even less access to print media.

1.6 Bilateral Relations

U.S.- Ethiopian relations were established in 1903, and remained constant throughout the period prior to the Italian occupation. After World War II, bilateral ties were fortified via a number of military, economic and cultural agreements, including a sizeable Peace Corps program. However, after Ethiopia's revolution in 1974, relations deteriorated significantly. With the downfall of the Mengistu regime in 1991 and the advent of the transitional Government, legislative restrictions were lifted, signalling a dramatic improvement in U.S.- Ethiopian relations. During FY 95, the United States provided about $111 million in aid to Ethiopia, of which $69 million was emergency assistance to deal with an ongoing food shortfall. After South Africa, Ethiopia is the largest recipient of U.S. economic assistance in sub-Saharan Africa.

Development efforts emphasize support for democratic institution building, promotion of a market economy, agricultural improvement, health care and basic education. The Peace Corps which formerly had one of its largest programs in Ethiopia, recently returned to the country.

The new government further bolstered its bilateral relationship with the U.S. when Prime Minister Meles made an official visit to Washington in October 1995 which coincided with the 50th anniversary celebration of the United Nations. The Prime Minister met with President Clinton, Secretary of State Warren Christopher, the Secretary of Defense and Assistant Secretary of State for African Affairs, George Moose. The willingness of so many high ranking officials to hold talks with the Ethiopian delegation illustrates the importance the U.S. Administration now accords the country. Ethiopia is the sixth largest U.S. export market in sub-Saharan Africa after South Africa, Nigeria, Angola, Ghana, and Cote d'Ivoire.

Chapter 2

Economic Performance and Outlook

2.1 Historical Performance

The Ethiopian economy has been chronically weak since 1974. Despite moderate growth in 1979-81, the civil war disrupted large areas of the country and military expenditure expanded rapidly. By 1991, it was absorbing 15 percent of GDP, over half of government expenditures and generating an estimated US$ 4-8 billion debt to the former Soviet Union. Central planning, collectivization, and widespread nationalization hindered output. Yet, more than policy errors, the dependency on rain-fed agriculture still remains the economy's main structural weakness. Ethiopia's main foreign exchange earner, coffee, was hit by falling prices from 1979-82, in 1987 and from the collapse of the International Coffee Organization (ICO) quota system in July 1989 until mid-1994. The economy has been characterized by low agricultural productivity, a small industrial base, and all sectors have been constrained by shortages of skilled manpower and deteriorated infrastructure.

Despite the experience of three catastrophic famines in little more than a decade, development aid flows were generally weak until 1991. Much aid was blocked in 1975 over the issue of compensation, following nationalization by the incoming military administration. An economic reform package was issued in 1990, just prior to the EPRDF defeat of the Mengistu regime. However, the effort was too little too late.

Nearly two decades of instability marked by civil war, recurrent droughts, high population growth rates and central planning left Ethiopia with high rates of poverty and a weak economy. The recent estimate of GDP per capita of $130 places Ethiopia amongst the poorest countries in Africa. Two crushing famines, one in the mid-1980's and another in the early 1990's, sapped the country's agricultural production capacity, accelerated food imports and intensified the reliance on external food aid.

To redress this dire economic situation, the Government's main economic objectives since 1991 have been to reduce macroeconomic imbalances, eliminate structural distortion, improve human capital and reduce poverty. Most economic indicators suggest that the country has begun to make progress.

The World Bank-led multi-donor Emergency Recovery and Reconstruction Project (ERRP) totalling US$650 million was launched in 1992. This program has helped reconstruct the country's war-torn infrastructure and jump-start the economy. The first Structural Adjustment Credit (US$250 million in 1993), has helped bridge the balance of payments financing gap and supported the Government's stabilization and initial structural reforms.

2.2 Structure of the Economy

The Gross Domestic Product in 1994 was broken down in the following way:

Agriculture	57.3%
Industry	10.2%
Manufacturing	3.3%
Services	32.5%

2.3 Fixed Investment

The civil war and centrally planned economy precluded significant investment during the 1980's. With the advent of peace and a democratically elected government, Ethiopia is bound to reap the benefits of economic restructuring, privatization, diversification emphasizing value-added exports, untapped mineral wealth, and tourism potential.

2.4 Economic Prospects 1996 - 2000

Several factors are likely to determine Ethiopia's economic performance over the next five years:

- Increased foreign investment and private sector development.
- Maintenance of an appropriate macroeconomic framework.
- Improvements in agricultural efficiency and growth.
- Climactic conditions----adequate rainfall.
- Continued donor financing.

Under the scenario of continuing reforms, real GDP is expected to grow about 6 percent for FY96-98. In addition to a reduced inflation rate, the country's foreign currency reserves have grown from US$475 million to US$736 million last year. The gap between official (auction) exchange rate and the parallel market rate has narrowed considerably, the former being 6.3birr and the latter 7.4birr to the dollar. Foreign exchange receipts have reportedly increased by 78 percent due to a boost in coffee sales. Nonetheless, increased public and private sector savings, foreign currency earnings and foreign investment are crucial to maintain and accelerate the rate of economic growth.

Chapter 3

A Sectoral Analysis of the Economy

3.1 Agriculture

With the majority of the population living in rural areas, agriculture is the backbone of the Ethiopian economy. The agriculture sector accounts for over half of GDP, 85 percent of export earnings (predominantly from coffee) and employs 85 percent of its workforce. The vast majority of agricultural land is farmed by individual peasant households. Out of 85m ha of arable land, less than 16m ha are under cultivation. Agriculture growth stagnated in the 1970's - 1980's as a result of periodic drought, pest infestations, land loss due to environmental degradation, poor infrastructure and marketing facilities and a legacy of disrupted agricultural production caused by civil conflict and inappropriate policies.

Recently, the agricultural sector has responded positively to sweeping reforms which include abolition of monopolistic marketing boards and freedom to hire farm labor. In addition, Ethiopia has adopted several measures to strengthen and expand the use of fertilizer and seeds by the farmers. Privatization of state farms, a legacy of the Dergue regime, is slated over the long-term.

Given the critical role of agriculture in the economy, the Government's long-term development strategy is based on Agricultural-Development-Led Industrialization (ADLI). The ADLI strategy unveiled in 1993, aims to use agriculture as a stimulus to improve land utilization and productivity, generate employment and income, and as the spring-board for growth in other sectors such as industry and services.

Increased agricultural production, employment and income are expected to provide a growing market for industrial production which would bolster exports, another major government priority. However, the success of ADLI will depend in part on how the sensitive issue of land tenure is handled. To achieve sustainable growth and attract foreign investment in the agricultural sector, it will be imperative to clarify usership rights, sustain private initiatives, develop rural credit, improve rural roads and encourage linkages with research and agriculture-based manufacturing.

3.1.1 Land Tenure

According to article 40 of the Ethiopian constitution, the Government is opposed to private land tenure. Nevertheless, the Government permits long-term leasing to private investors. Implementation of new land leasing policy has started, with urban land auctions conducted in January 1995. Lease-holders have a right of use over urban land for a period ranging from 50 - 99 years. Such rights can be transferred, renewed, or mortgaged together with on-built facilities. Developments made on the land are fully owned by the lessee, and as such, he/she is entitled to sell on-built facilities and developments made on the property. With respect to rural land, the lease period and rate per hectare are determined by negotiations between the lessor and the lessee.

Regulation of the commercial use of land is beginning to fall under regional jurisdiction. Region 4 (Oromo State) recently passed a new land law in August 1995. Local press reports recounted that the regional administration will give preference in land allocation to projects which fall within the region's development objectives and provide employment opportunities.

3.1.2 Coffee

Some of the finest and rarest coffees in the world are grown in the highlands of Ethiopia. In fact, the word coffee is thought to have derived from the region of Kaffa in Ethiopia.
Ethiopia is Africa's third largest producer of coffee after Uganda and the Ivory coast. Coffee is Ethiopia's most important export commodity. For fifteen years up to 1994, coffee accounted for an average of 55 percent of the nation's total value of exports. This proportion has increased recently to about 65 percent of total export earnings in the 1994-95 coffee year (October - September). During 1994, a total of 79,920 metric tons of coffee was exported, generating an income of birr 969 million, which is a 15 percent increase in quantity and a 51 percent increase in value over 1993 export figures. The parastatal monopoly in coffee marketing has been abolished. Hence, the private sector may participate in coffee trading, marketing and exports.

3.1.3 Livestock, Hides and Skins

Ethiopia's 75 million head of livestock is estimated to be the largest in Africa. It is difficult to calculate the sector's value since a significant part of meat and dairy production is for subsistence purposes. In certain regions, particularly in the highlands, livestock is utilized only to support farming. Ethiopia's livestock continues to suffer from unpredictable weather conditions, diseases and the lack of a coherent plan for development of the sector. Drought in 1994 is believed to have hit livestock herds hard.

Although hides/skins and leather are Ethiopia's second largest export commodity (about 21 percent of export earnings), the sector's enormous potential remains largely untapped. Currently relatively few skins are processed locally; however, the reform program is intended to increase both the quality and quantity of production. Processed hides and skins along with finished leather goods are seen as the most promising sector for export expansion.

3.1.4 Cereals

Ethiopia's primary food and cereals are: barley, maize, sorghum, an indigenous grain called teff, and a number of pulses. Output of cereals and pulses has barely increased over the past decade. Only in 1992/93 did the total harvest top the previous high of 7.6m tons, reached a decade earlier. Given that Ethiopia needs to produce an extra 320,000 tons per year to keep pace with population growth, the stagnating trend in food production will have to be reversed. Land degradation, which is one of the most severe environmental problems in Ethiopia today, has a direct impact on grain yields. Nutrient loss and soil erosion result in reduced agricultural output to the tune of 600,000 tons of grain per year, equivalent to 90 percent of Ethiopia's structural food deficit in 1993. Nonetheless, the Government hopes that market-based policy incentives, coupled with an improvement in the supply of seeds and fertilizers, will stabilize and increase production.

3.2 Mining and Energy

The development of Ethiopia's mineral wealth is one of the Government's leading economic objectives. The most significant opportunities lie in industrial minerals and precious metals such as gold, tantalum, soda ash, potash, nickel, platinum, iron ore, coal, marble, silica, limestone, diatomite and bentonite as well as oil and natural gas. Accounting for less than 1 percent of GDP, current mining activity does not reflect its true potential. Mining operations are expected to be an important economic catalyst for the Government's export-oriented development strategy. The goal is to get the minerals sector up to 10 percent of GDP within 10 years.

Until recently, the mining sector has been exclusively reserved for the Government. In 1993 however, the Ministry of Mines opened the industry to competition and investment by the domestic and foreign private sectors. Mining income tax was cut from 45 percent to 35 percent and "free carried interest", the government's free equity stake, was reduced from a ceiling of 10 percent to a flat two percent.

Ethiopia is estimated to have total untapped gold reserves of 500 MT. The largest and most developed area is the Lega Dembi mine in the Adola Greenstone Region. For example, Lega Dembi currently produces slightly below three tons of gold per annum and published estimates of its proven deposits range from 60 to 200 tons. Other promising regions are: Arero Greenstone Region, Agere Maryam Region, Moyale Greenstone Region and the Western Greenstone Region. By March 1996, the Government had signed exploration agreements for gold and precious base metals with six foreign companies, five from Canada and one from the U.S. Recently, St. Genevieve Resources, a Montreal-based mining company, signed a precious and base metals exploration agreement with the Government of Ethiopia. The agreement grants to St. Genevieve all rights to the Serkole concession in the Benishangul-Gumuz Region which extends over 524.9 km. The property has significant primary gold deposits.

In the oil and gas sector, two international oil companies, Hunt Oil and International Petroleum Ltd. (IPL), have concessions in southeastern Ogaden and western Gambella regions respectively.

The recently approved Calub Energy Project, financed by the World Bank, aims to exploit natural gas reserves in the Calub region. These reserves are estimated to be 2.7 trillion cubic feet.

Electricity generation and transmission to rural areas has been identified as another high priority area for foreign investment. Large-scale projects permit joint-ventures with the Government; small-medium scale projects are fully open to private investors. Presently, hydro-electric power is Ethiopia's primary source of energy. Potential is estimated at 56,000 kwh per year, of which only 1,200 kwh per year are currently exploited. The Ethiopian Electric Light and Power Authority (EELPA) has begun to award contracts for work on the northern extension to the national grid. The work is being financed with loans from the African Development Bank (ADB).

The Minister of Mines and Energy recently suggested that discoveries of new geothermal sources could supplement hydro-electric power as a principal source of energy.

Some incentives for mining and petroleum and gas include exemption from import duties and taxes for import of capital goods and equipment required for mining, exemption from export duties, and accelerated depreciation on mining investments for four consecutive years among others.

3.3 Manufacturing

Ethiopian industry is comprised of light manufacturing products such as construction materials, metal and chemical products as well as basic consumer goods such as food, beverages, leather, clothing and textiles. Currently, food processing, textiles and beverages dominate the industry which is largely based on primary inputs from the agricultural sector. About 150 public enterprises are involved in bakery products, textiles, footwear and furniture production and account for more than 95 percent of the manufacturing sector's value. Private sector firms engage in similar activities, although on a much smaller scale.

Production is concentrated in and around Addis Ababa and Dire Dawa. Until its separation from Ethiopia, Eritrea encompassed the majority of the manufacturing industry. Manufacturing caters largely to the home market, although some products such as sugar, semi-processed hides, skins and other leather work and oilseed products, are exported.

During 1989-91, manufacturing was adversely affected by the civil war which induced shortages of raw materials, foreign exchange and fuel. As a result, manufacturing contributed to only 2.2 percent of GDP. However, since 1994, the sector has steadily rebounded due to investment incentives such as liberalization of foreign exchange. In 1994/95 the average capacity utilization of public enterprises rose to almost 70 percent from rates as low as 20 percent at the end of 1992/93. In 19949/5, the sector's share of GDP increased to 4.5 percent.

3.3.1 Outlook for Manufacturing

In the short term, sustainability of the manufacturing recovery is likely to be influenced by how well the private sector responds to market incentives as well as by the capacity of public enterprises to adapt to the more competitive market environment. According to the new policy, state-owned enterprises elect their management boards, assume autonomy in pricing and production decisions and are no longer supervised by the Ministry of Trade and Industry.

The main factor contributing to the past poor performance in the sector was excessive regulation, including severe restrictions on domestic and foreign private investment and a policy environment biased against exports. However, good initial progress has been made in encouraging private sector development. The wave of privatization is expected to boost production significantly. With approximately 60 million consumers, demand for manufactured goods in Ethiopia is sure to grow.

3.3.2 Incentives

The Government is making concerted efforts to promote private sector growth by dismantling barriers to investment and private sector participation:

- Right to remit profits, dividends or royalties in foreign exchange.
- Exemption from import duties and taxes for imports of capital goods and equipment up to 15 percent of the value of the capital invested.
- Exemption from export duties for most Ethiopian products destined for export (other than coffee).
- Income tax holidays between 3-5 years.

3.4 Tourism

The revival of the tourism industry has been a priority of the new Government. Many of Ethiopia's principal tourist attractions, such as Lalibela, Gondar and Axum have remained unknown to the outside world due to the civil war that raged until 1991. While the National Tourist Commission has been restructured, private tour agencies and hotels are expected to lead the revival. New private small and medium-sized hotels have sprung up, particularly around Addis, since 1991. A new Sheraton Hotel is scheduled to be completed in 1996, the first luxury hotel in the capital to be constructed in 25 years. The Ethiopian Tourist Commission (ETC) projects that 136,000 tourists will visit the country in 1995/96 increasing receipts to more than $50 million. This compares with earnings of $37 million from 117,000 visitors in 1994/95. In 1995, the ETC announced that over 600 companies working in tourism-related fields had now been licensed, and that 67 investors had been authorized to build hotels worth $86 million in various parts of the country.

3.5 Health Care

The low health status of the population is indicated by the life expectancy of only 48 years, slightly below the average for the rest of Africa at 52 years. Household survey data shows that on average, close to 80 days out of a year are lost due to poor health and illness. The burden of disease disproportionately affects women and children. The mortality rate of 700 per 100,000 livebirths is extremely high. Only 45 percent of the population have some form of access to primary health care compared to 60 percent for Africa as a whole. Only 18 percent of the rural population have access to safe water supply; this is responsible for high morbidity from infectious water-borne diseases. Nevertheless, the share of Government expenditures devoted to the health sector has increased from 4 percent in FY89 to 11 percent in FY94. Most of the capital budget had been allocated to the rehabilitation of clinics which were damaged during the civil war.

The national policy instituted in 1993 emphasizes primary health care, increased reallocation towards the regions and strengthening the financial base for health provision. The Ministry of Health has embarked on a 10-year financing initiative which emphasizes self-reliance through mobilizing both government and private resources. The health care financing methods aim to improve government sector efficiency, generating new sources of revenue through increased allocations to health, expanded user fee program, revolving drug funds, private sector participation in the health sector, increased donor funding for health services and development of private health insurance.

The local production of pharmaceuticals and drugs in Ethiopia is practically non-existent, forcing the country to import virtually all pharmaceutical products. Large-scale manufacturing of pharmaceuticals is envisioned to be of strategic importance. To that end, full private sector participation in small and medium scale enterprises for the manufacturing of pharmaceuticals and drugs is also encouraged with or without government participation.

Growth potential in the sector includes provision of medical equipment and supplies, pharmaceutical raw materials, veterinary drugs and supplies for treatment of livestock, as well as anti-malarial agents, antibiotics, and medications for tropical diseases.

The investment and tax incentives that apply to manufacturing projects also apply to health care manufacturing and service projects.

3.6 Transport, Construction and Communications

Ethiopia's inadequate and underdeveloped surface transport infrastructure has inhibited economic development and export growth. Ethiopia's road density is one of the lowest in Africa. About 65 percent of the road network can be classified in poor condition, largely as a result of insufficient maintenance, the effects of war and heavy vehicle overloading. In recognition of the crucial role of the road sector, the government has set out a Road Sector Development Program (RSDP) to speed up improvement and expansion of the road network. The RSDP has two phases, each of 5 years duration, to be executed from July 1997 - June 2007 with a combined budget of US$3.9 billion. As a result, there will be many opportunities for foreign investors to collaborate with local construction firms in the areas of road maintenance and construction.

International contractors are invited to take part in the large-scale construction and rehabilitation of the Federal Highway Network, composed of 8,180 kms of trunk roads in eleven corridors and major link roads of 8,043 kms interconnecting the radially oriented highway system. The government will also be soliciting assistance with bridge rehabilitation and replacement as well as appropriate equipment to implement the RSDP.

In the telecommunications sector, the Government is contemplating partial privatization of the Ethiopian Telecommunications Authority (ETA). In addition, it will establish a regulatory body to allow private sector participation in the trading of selected telecommunications equipment. It is widely expected that cellular telephone service will commence in Ethiopia with private sector participation in the near future. With a population of 55.9 million and current telephone density of only .45 percent, the potential for a lucrative market in the cellular, as well as long-distance sectors, is tremendous.

The ETA planned to build 32 new digital telephone exchanges (46 are already operational) and 400 remote stations using radio or satellite links, raise line capacity from 169,700 to 335,000, and increase the number of telephones to 374,000 between 1989-1993, however, the targets proved over-ambitious for that time frame. Information technology firms are beginning to take shape in Ethiopia's private sector, with the introduction of several firms in Addis Ababa that distribute equipment from noted U.S. and other manufacturers and service providers such as AT&T, IBM, and Siemens. The role of these firms will become increasingly important as reflected by their recent participation in a major bid to supply large quantities of computers and peripherals to the Commercial Bank of Ethiopia.

Chapter 4

The State's Role in the Economy

One of the Government's primary objectives since 1991 has been to encourage growth by replacing the previous centrally-planned economy with a market-based system and to reduce poverty. The new economic policy aims to limit the role of Government to selected economic services, encourage private investment, promote greater participation in the private sector, mobilize external resources and pursue appropriate macroeconomic and sectoral policies. It has relied on the World Bank and IMF to help carry out an economic rehabilitation program for the past five years.

The growth of the private sector has been slow, but a sense of economic vitality has followed the political transition which culminated in the national elections in 1995. Economic verve is evident not only in the proliferation of new businesses and wave of privatization, but also in the public discussions about economic policy. The Addis Ababa Chamber of Commerce recently critiqued the Government's economic policy saying that, despite the market-oriented reforms, the Government had not sufficiently diminished its role in the productive sector.

The state continues to have joint venture participation in a number of economic sectors and maintains a virtual monopoly in areas of national interest such as telecommunications; large-scale production and supply of electrical energy; large-scale air, rail, and marine transport services; and petroleum imports. The sectors that have benefitted most from deregulation and liberalization are the import/export sector, coffee trading and consumer goods distribution and marketing.

The Government's policy on land tenure is a point of contention with some potential domestic and foreign investors. The Government is opposed to private land ownership, asserting in article 40 of the Constitution that; "the right to ownership of rural and urban land, as well as natural resources, is exclusively vested in the state and in the people's of Ethiopia." The government claims that it can guarantee certain farmer's rights such as full control over output, leasing the land and passing it on to family members upon death. The pros and cons of this policy will likely be the subject of continued dialogue between the Government and prospective investors in the foreseeable future.

The state continues to dominate in most of the transport area with 100 percent ownership of Ethiopian Airlines (EAL). EAL is a major source of foreign exchange for the country. Likewise, Ethiopian Shipping Line (ESL) is a well-managed operation which almost consistently yields profits. The state continues to exert considerable influence and control in mining and petroleum exploration. In the manufacturing sector, many of the state-owned enterprises are in the process of re-structuring or are being divested.

Chapter 5

The Business Climate

5.1 Privatization and the Emerging Private Sector

The Government of Ethiopia has made substantial progress in accelerating economic growth and reconstruction. Faith in the reform program's main tenets has been strengthened by the fact that major changes, like devaluation and regionalization, have been implemented without the severe repercussions many had feared. One of the important aspects of the economic rehabilitation program is the implementation of policies which empower the Ethiopian private sector and attract foreign investments in value added activities.

In May 1992, the Government issued a detailed Proclamation on Investment and established an Investment Office of Ethiopia (IOE) which is accountable to the Board of Investment. The objective of the new investment code is to develop, promote and encourage private investment in general and in the productive sector in particular. The code also seeks to encourage foreign investors to play a key role in rehabilitating and restructuring Ethiopia as well as creating wider employment opportunities.

Three major groupings operate in the private sector:

- foreign investors dominated by Saudi Arabia, South Korea, Kuwait and Italy.
- businesses owned and managed by Ethiopians.
- a numerically huge informal sector: subsistence farmers, small-businesses and informal traders.

Reforms that have been implemented to stimulate private sector development include:

- restructuring and privatization of state-owned enterprises.
- reduction of inflation through budgetary and monetary controls.
- foreign exchange rate adjustments.
- issuance of a new labor law.
- approval of the Investment Code of 1992 streamlining investment approval procedures and providing fiscal incentives.

- reductions in corporate taxes and duties on imports.
- deregulation of domestic prices.
- opening financial services to foreign investors.
- abolishing all export taxes (except coffee) and subsidies.
- credit facilities for small and medium enterprises.
- membership in MIGA, OPIC, ICSID and other international institutions to offer added protection to investors.

Privatization has expanded the role of the private sector in all commercial activities allowing the Government to concentrate on provision of basic social services such as health and education. The Government expects to:

- reduce subsidies of inefficient operations.
- improve enterprise efficiency and productivity to compete globally.
- introduce new technology and management expertise.
- create conditions for higher levels of local and foreign private investment

The Government of Ethiopia is committed to ensuring that private capital plays a significant role in the economy. To this end, it has eliminated discriminatory tax, credit and foreign trade treatment of the private sector, simplified administrative procedures and established a clear and consistent set of rules regulating business activities. In addition to the Investment Office of Ethiopia, a Privatization Agency has also been established to formulate and implement a phased privatization program. In 1995, the Government began to sell most state-owned retail shops as well as most government-owned hotels and restaurants. Enterprises valued at over $3 million, such as soft drink bottling plants and major hotel chains, are being offered for lease, management contract or joint venture with the Ethiopian Government holding a minimum share of 25 percent.

The Government has also developed programs to facilitate the commercialization of those enterprises remaining in the public sector. For state-owned enterprises, the focus will be on improvement of performance, physical rehabilitation and financial restructuring and retrenchment, where warranted. Privatization of state farms will be undertaken along with the remaining public enterprises in due course.

For small to medium sized enterprises, sales have been made mainly via general public tender. For the larger state-owned enterprises under the Privatization Agency's mandate, the sale by total or partial privatization has been through one or more of the following modalities:

- public tender
- public auction
- private investment through the issue of new shares to inject capital
- transfer or sale of shares to managers and employees

The Privatization Agency published the following results of the first round of sales of SOEs which was launched in February 1995: a total of 16 companies mostly hotels, restaurants, food processing plants such as flour mills, were sold at combined price of $12 million. They are the first of 144 SOEs listed for privatization. Half are to be directly sold to employees with credits provided by the Government. Only a limited number of risk-taking individuals and businesses took the opportunity during this first phase.

The second round of privatization yielded the following:

- Coca Cola Bottling plants in Addis bought for $10.8 million.

- Three Pepsi-Cola Bottling plants in Addis, Gondar and Dessi sold for $16.6 million.

- A shopping and business complex in Addis sold for $10.8 million.

- Hotel, restaurant and bakery sold for total of $16 million.

- The Legadembi Gold Mine in Sidamo province is currently in the process of being privatized.

5.2 Investment Performance

According to the Investment Office of Ethiopia (IOE), as of June 1995, the IOE had licensed 1,400 investors (both domestic and foreign) with a total value of about US$2 billion. Foreign investors have introduced capital estimated at US$65 million. Although an accurate breakdown is not available, currently American direct investment in Ethiopia is estimated at about US$8 million. The liberal approach to commercial enterprise is attracting significant amounts of foreign investment from the Middle East, Europe, and Asia, as well as from the large Ethiopian expatriate community in the United States.

5.3 Business Outlook

The character and attractiveness of business opportunities in Ethiopia will be substantially influenced by the speed and effectiveness of liberalization, deregulation and privatization of the economy; successful reduction of the public deficit and inflation; continued stability and economic growth in the region and sustained world-wide demand for Ethiopian commodities.

Ethiopia's main attractions are likely to be in the field of resource-intensive investments such as agriculture and mining. However, Ethiopia's potential for tourism based on its rich cultural heritage, as well as exotic wildlife and bird species, should not be underestimated. In addition, strategically located at the crossroads of Africa and the Middle East, Ethiopia is poised to serve not only its own substantial consumer market of over 55 million people, but that of the Gulf States as well. Therefore, investments in infrastructure development, agribusiness and manufacturing will strengthen Ethiopia's ability to serve the entire region.

5.4 Business Opportunities

Investors in specific areas may be eligible for investment incentives. These areas include agricultural development and agro-processing; agricultural production; manufacturing of equipment, machinery, spare parts, components and supplies, vehicle bodies, other products and assembly plants, and publishing or printed materials; large-scale capital road and building construction; waterworks such as well drilling, dam construction, and other related works; rural transportation facilities; and the purchase of spraying machinery, trucks fitted with refrigeration facilities, or other equipment for support services. The following is a brief listing of areas of opportunity:

Agriculture, agro-processing and livestock. Production of cash crops such as coffee, tea, tobacco and cotton will remain a priority as will the production and processing of fruits, vegetables and grains, oilseeds, flowers and other agricultural commodities. With Africa's largest population of livestock, Ethiopia is also seeking to increase domestic processing of hides and skins.

Fish farming (aquaculture). Given Ethiopia's vast water resources in the form of lakes and rivers, aquaculture possesses enormous potential for growth.

Consumer goods and manufacturing. This sector is dominated by the manufacturing of construction materials, metal and chemical products, food and beverages, textiles and clothing, leather products, rubber, tobacco and plastics.

Mining, oil and gas exploration. Significant opportunities currently exist in industrial minerals and precious metals such as gold, tantalum, soda ash, potash, nickel, platinum, iron ore, coal, marble, as well as oil and natural gas.

Tourism, hotels and resorts. Selected opportunities exist in hotels, resort operations and nature lodges. Ethiopia's highlands, the Rift Valley, the medieval palaces and churches of Lalibela, Axum and Gondar in the north, the walled city of Harar in the southeast, including the Sof Omar natural cave and clear water of the Webb River, all offer breathtaking scenery, wildlife and historic monuments to satisfy a wide-range of visitors. Therefore, the Government is actively promoting hotel and tourism development.

Water resources for irrigation and power generation. Ethiopia's water resources potential for irrigated agriculture and hydro-electric power generation is enormous but as yet underdeveloped. The country possesses 14 major river basins with a total annual runoff of about 102 billion cubic meters of water per year. Electricity generation and transmission to rural outlying areas has been identified as a high priority by the Government.

Services. Social services such as health, education and sports facilities as well as marketing are key growth areas for services.

Transportation, infrastructure and construction. Heavy investment will be needed in infrastructure, especially roads, rail, telecommunications, housing, sanitation and energy in the years to come. Key areas for foreign investment are road maintenance and rehabilitation; medium-scale air, rail and marine transport services; irrigation projects.

Banking and insurance opportunities. Five private insurance companies are now open for business. In addition, two new private banks are slated to commence business shortly. The latter may seek U.S. correspondent banking arrangements.

Chapter 6

The Environment for Foreign Businesses

6.1 Government Policy

The previous government made belated, largely unsuccessful attempts to attract foreign capital into the country. The transitional administration issued a new investment code which opens all sectors, except large-scale energy projects, transport and financial services, to foreign investors. The current EPRDF Government continues to promulgate this liberal policy.

In addition to the protection afforded to investors under the 1992 constitution, Ethiopia is a signatory to both the World Bank's Multilateral Investment Guarantee Agency (MIGA) and the U.S. Overseas Private Investment Corporation (OPIC). Disputes arising out of foreign investment involving the foreign investor and the state, may be settled by means agreeable to both parties. In addition, disputes can be submitted for arbitration to The International Convention on Settlement of Investment Disputes (ICSID) under the auspices of the World Bank. Ethiopia has established bilateral investment protection agreements with Eritrea, Italy, Greece, Israel, Switzerland, and Germany.

Ethiopia does not currently allow the development of free-trade zones, although a transshipment port is available in Djibouti.

6.2 Limitations on Foreign Investment

Private investors may invest on their own or jointly in most sectors of the economy. While the Government permits foreign investors up to 100 percent equity ownership in new investments, it prefers joint ventures with domestic investors. The extent of local control, ownership and management of the joint venture is a factor in the screening of new projects although it is not an eliminating criteria for approvals or incentives. The following are the major criteria for the approval of joint venture proposals:

- The transfer, absorption and adaptation of needed technology and know-how into the country.
- Improvement of the country's foreign exchange position.
- Utilization and development of the country's resources, including the generation of local employment opportunities.

- Development of forward and backward linkages and increased added-value in various economic sectors.
- Access to world markets and the foreign partners marketing facilities.

Areas for investment have been classified as follows:

A. Those reserved exclusively for the Government

Areas exclusively reserved for the Government include defense industries; large-scale production and supply of electrical energy; large-scale air, rail, and marine transport services; postal and telecommunications services; and import/export trade in those selected products deemed crucial to the economic life of the country such as petroleum and armaments.

B. Those where Government participation could include joint ventures with private investors

Areas where the Government may choose to enter into a partnership with private investors include large-scale engineering and metallurgical industries; capital intensive or technology-related investment in large-scale mining and energy production; large-scale manufacturing of pharmaceuticals and fertilizers; and industries that supply strategic raw materials to the chemical industry.

C. Areas fully open to private investors

Areas fully open to private investors include small to medium-scale investments in air, rail, and marine transport services, as well as in the production and supply of electrical energy under regulations issued by the appropriate governmental authority. In the financial sector, new laws opening banking and insurance to the domestic private sector have been also issued.

6.3 Acquisition of real estate

All land is owned by the state. Investors shall be entitled to the land required for the investment. A lease agreement would be required between those parties having the interest or title in the land and the investor, with the lease specifying the purpose for which the land is required, the period of use, the amount of rent, and other relevant matters.

6.4 Competition Rules

The privatization program regulates sale of Government enterprises. The investment code governs the approval process for new projects. With the exception of exchange regulations, there are no further official formalities needed for the acquisition of local private companies by foreign firms.

Chapter 7

Infrastructure

Ethiopia's physical and service infrastructure was damaged during the civil war. Strategically located at the crossroads of Europe and the Middle East, Ethiopia is in the process of rebuilding its transport and energy networks which are critical for growth.

7.1 Transport

The rehabilitation of Ethiopia's road, rail, port and airport network, some of which was damaged or rendered unusable during the war, will be critical to the nation's economic development strategy. The current transport network is incapable of supporting an efficient, market-based production and distribution system. Ironically, while Ethiopia has the world's lowest road density per capita in the world, Ethiopian Airlines (one of Africa's largest cargo and passenger carriers) is celebrating its 50th year of successful service by expanding its fleet and diversifying its operations. The coming to power of the EPRDF has opened up the potential for coordinated development of the infrastructure of all the regions of Ethiopia and Eritrea.

7.1.1 Railroads

Ethiopia's only working railway, the line from Djibouti to Addis Ababa, is in serious need of refurbishment. There has been some repair but a complete overhaul is urgently needed. Several fatal accidents have recently occurred underscoring the precarious nature of the railway. The railway carries about 20 percent of Ethiopia' imports and a negligible proportion of exports. Ethiopian and Djiboutian transport ministers have met to discuss refurbishment proposals. In the meantime, most traffic has been diverted to the Eritrean ports of Assab and Massawa.

7.1.2 Roads

Road density in Ethiopia is among the lowest in Africa with an estimated 21 km of road per 1000 square km and 0.43 km per 1000 population. Ethiopia possesses approximately 20,000 kilometers of roads, of which only 25 percent are in reasonable shape. Only 21 percent of the highway network is paved, with few interconnecting links between adjacent regions, and an insufficient feeder road network. The country's main route, the Addis Ababa-Assab road, is in poor condition and over-congested. Nearly three quarters of the farms are more than half-a-day's walk from all-weather roads. With 15 deaths per 1000 vehicles annually, Ethiopia also has one of the highest road accident rates in the world.

Therefore, in its current state, Ethiopia's road transport system is inadequate and underdeveloped. Extensive rehabilitation is needed to remedy the lack of maintenance, the effects of war and vehicle overloading. On a positive note, deregulation of the transportation system and liberalization of freight tariff rates have commenced. In addition, the Ethiopian Roads Authority has elaborated a detailed Road Sector Development Strategy (RSDP) which provides for priority road rehabilitation, upgrading and maintenance; strengthening of management capacity; new investment in all classes of roads (including regional and rural access roads), and the establishment of a Road Fund. This, in turn, should improve access to ports, access to existing and new resource areas as well as contribute to balancing the road infrastructure among regions.

7.1.3 Air Transport

Passenger and cargo air transport services are operated by Ethiopian Airlines (EAL). Its international flights link the country with 43 cities on three continents - Africa, Asia and Europe - and its domestic service links 43 airfields and 21 landing strips with Addis Ababa. EAL was established in 1946 with advice from TWA and Boeing Corporation. It has an excellent safety record and provides aircraft maintenance services to many African airlines at its facilities in Addis Ababa.

There are international airports at Addis Ababa and Dire Dawa. In addition, both Jimma and Bahr Dar (opened in 1986) can take international flights. All regional capitals and a number of other towns have airports for internal flights. Construction on Mekele International airport in Tigray has recently begun and is expected to be operational by 1997. The Addis Ababa international airport is also slated for expansion with financial help from several regional financial institutions.

EAL has recently diversified into aircraft maintenance and production of turbo-engined crop duster under license. In 1989, it announced the purchase of six Boeings and plans to invest $1.2 billion over ten years.

The airline's modern fleet includes Boeing 767 and 757 jets for international flights. In light of a recent upsurge in internal tourist travel, EAL recently acquired five Fokker-50 aircraft. The planes will be purchased with Dutch export credits over ten years.

Unlike many African airline companies which operate at a loss, EAL continues to be a major source of foreign exchange for the country. With tourism on the rise, EAL is poised to increase it positive role in the nation's vital service/transport sector.

7.1.4 Ports

Despite the effective loss of Ethiopia's coastline when Eritrea declared independence in 1993, the Ethiopian Shipping Line (ESL) continues to have full access to the Eritrean ports of Assab and Massawa. The port of Djibouti also serves Ethiopia's import-export trade needs. However, the poor condition of the railway which connects Addis Ababa and the Djiboutian port, has slowed traffic considerably. ESL provides regular cargo service to and from European, Mediterranean, African and Pacific Basin Ports. Like Ethiopian Airlines, ESL is a well-managed company which last year turned a profit of approximately Birr33m.

7.2 Power

Ethiopia has poorly developed energy resources. It is inordinately dependent on woodfuels and charcoal. Five small hydropower stations - Fincha, Koka, Melka Wakena, Awash III, Tis Abay -are operational. They total 371 megawatts of nameplate capacity and are tied to the national power grid, which is also fed by conventional power plants. Total existing capacity of the grid is less than 1000 megawatts for the entire country. However, Ethiopia's hydro-power potential has been surveyed, and is estimated to be about 15,000 megawatts.

The Calub Natural Gas project, a joint public-private enterprise, will add substantially to the national energy supply. Scheduled to go into operation in 1997, it will produce diesel fuel, gasoline, LPG, and kerosene. Natural gas reserves estimated at 68 billion cubic meters (732 billion cubic feet) have been identified so far.

7.3 Communications

The Ethiopian Telecommunications Authority (ETA) provides limited telephone, telefax, telex and data communication services via satellite. Internally, direct microwave telephone links are somewhat available to most regional cities; a number of smaller towns also have automatic telephone services. International communications links are maintained through two satellite earth stations. Microwave links exist with Kenya, Djibouti and Eritrea. Recently, digital telephone exchanges have also been installed.

Postal services, including sky-pack facilities, operate domestically and internationally. Although currently under government control, the ETA is likely to be privatized in the near future.

Chapter 8

Foreign Trade and the Balance of Payments

8.1 Recent Performance

The terms of trade have moved against Ethiopia since 1970, contributing to successive and growing trade deficits, averaging $542 million between 1987 and 1992, with increasing fluctuations between 1989 and 1992. The collapse of world coffee prices dimmed the outlook for export earnings from 1990 until mid-1994, and although the trade deficit shrank in 1991 as the final stages of the war restricted imports, it rose by over $500 million and $823 million in 1992. High public and private transfers following drought briefly pushed the current account into surplus in 1991, the first time since 1985. Ethiopia has a relatively high level of exported services---an annual average of $283 million between 1987 and 1992, largely due to revenues from Ethiopian Airlines and Ethiopian Shipping Lines. The latter continues to operate profitably from Djiboutian and Eritrean ports. Foreign exchange reserves have risen sharply since the change of government. They stood at $464 million at the end of September 1994, providing more than five months' merchandise import cover.

8.2 Exports

According to the Ethiopian Ministry of Commerce and Industry, the country earned over US$480 million in export revenues during the last fiscal year (July 1994 - July 1995), one third more than the previous year. The three top foreign exchange earners in rank order were: coffee, hides and skins, and gold. Coffee normally accounts for about 60 percent of foreign exchange. Ethiopia exported 600 kilograms of gold last year. Petroleum products generated about US$15 million, whereas oil seeds, horticultural and other agricultural products fetched about US$1 million in export earnings. A World Bank report indicates that exports will be further enhanced by efforts to diversify in horticulture products, sesame, and haricot beans. Over the long term, higher export earnings will depend on improved productivity in the agricultural sector, increased supply of capital imports, better infrastructure, improved incentives to exports, a greater role by the private sector, increased foreign investment, a stronger financial sector, further rationalization of the tariff and tax structures, and the development of an export-oriented light manufacturing industry.

8.3 Imports

Ethiopia's main imports consist of semi-finished goods, crude petroleum and petroleum products, food, transport and industrial capital goods, medical and pharmaceutical products, vehicles, civil aircraft, raw materials and agricultural capital goods.

About 17 percent of Ethiopian imports are conducted through government tenders. The tender announcement is made public to all interested potential bidders, regardless of nationality of supplier or origin of products/services. Both Ethiopian and foreign suppliers, especially those from Italy, Germany, France, Japan, and the UK who have local representatives, participate aggressively.

8.4 Direction of Trade and Trading Partners

In 1993 Ethiopia's major trading partners in rank order were the United Arab Emirates (UAE), Germany, Italy, the United Kingdom, Djibouti and the United States. As Ethiopia's second largest coffee export market, Japan is also an important player. Last year Ethiopia established diplomatic relations and trade ties with the Gulf states of Kuwait and Qatar. In addition, it solidified its growing commercial relationship with Saudi Arabia. Bilateral trade between Saudi Arabia and Ethiopia has been steadily increasing, amounting to over $21m in 1994. The primary Ethiopian exports to Saudi Arabia are coffee, tea and livestock. Lately the Ethiopian business community has been courting the Asian market. Industrialists from China and India have expressed interest in supplying quality machinery at competitive prices.

The Government introduced a complete overhaul of tariffs on foreign trade. These included substantial cuts in customs tariffs and sales tax on imported goods, bringing it into line with rates applicable to domestic goods.

Most projects open for international competitive bidding are funded by either the Ethiopian Government or major international financial institutions in which the U.S. participates such as the International Development Association (IDA) of the World Bank, the African Development Fund (AFDF) of the African Development Bank (ADB). Ethiopia has had a substantial trade deficit for many years.

MAIN TRADING PARTNERS	
Main dest. of exports 1991	**% of total**
Germany	27.9
Japan	22.9
Saudi Arabia	8.4
Italy	6.8

Main origins of imports	% of total
USA	13.1
Germany	11.4
Italy	10.2
Saudi Arabia	9.9

8.5 Exchange Rate Policy

The Ethiopian unit of currency is the Birr, previously referred to as the Ethiopian dollar, divided into 100 cents. The Birr was pegged to the dollar in 1974 at Birr2.07:$1, but was devalued for the first time in October 1992 to Birr5:$1. The rate was marginally lowered in April 1994. However, in an effort to close the gap between official and parallel exchange rates, the authorities introduced a system of bi-weekly foreign exchange auctions in May 1993. Individuals with import licenses (other than those for foods on a prohibited list) can apply for foreign exchange. The auction-determined price is then applicable for all transactions other than debt servicing and imports of fuel and fertilizer. With an average auction rate of around Birr6:$1, this mechanism has progressively narrowed the gap between official and parallel rates by late 1994 to just 15 percent.

8.6 Currency Outlook

As long as the auction mechanism remains in place assuring minimal disparity between the official and parallel rates, the outlook for continued stability of the Birr is positive.

8.7 Regional Organizations

8.7.1 COMESA -Common Market for Eastern and Southern Africa

Ethiopia is a founding and active member of The Common Market for Eastern and Southern Africa (COMESA), formerly known as the Preferential Trade Area for Eastern and Southern Africa (PTA). COMESA was established in 1981. Its aim is to increase regional trade and establish an African common market by the year 2000. COMESA has adopted a list of over 600 products for preferential tariffs among the 22 member states. Thus, investors in Ethiopia also have access to the wider COMESA market which has a total population of about 260 million. COMESA's generous tariff concessions offer considerable encouragement to Ethiopian exporters.

8.8 World Trade Organization (WTO)

Ethiopia is not yet a member of the WTO, formerly known as the GATT. However, adherence to the WTO is currently under consideration by the Government.

8.9 The United States' General System of Preferences (GSP)

The Generalized System of Preferences (GSP) is a system used by many developed countries to help developing nations improve their financial or economic condition through export trade. It provides for the duty-free importation of a wide range of products from certain countries which would otherwise be subject to customs duty. The U.S. Customs Service is responsible for determining eligibility for duty-free entry under GSP. In 1992, Ethiopia became eligible to participate in the GSP.

8.10 The Lomé Convention

The EU's principal vehicle for trade and development assistance for sub-Saharan Africa is the Lomé Convention. Under this Convention, 70 African, Caribbean and Pacific (ACP) countries are eligible for trade preferences and development assistance programs administered through the European Development Fund (EDF) and the European Investment Bank (EIB). The Fourth Lomé Convention was signed in December 1989 for a period of 10 years. Ethiopia is a signatory of the Lomé Convention.

Chapter 9

External Debt and Aid

9.1 Debt

Ethiopia's stock of external debt more than tripled between end-1982 and end-1992. By June 1992, arrears to creditors reached US$716 million. Since then, Ethiopia has made significant progress in improving its external debt situation and credit-worthiness. By the end of 1994, Ethiopia's total external debt outstanding, including the IMF, short-term and private non-guaranteed debt, stood at about US$ 5,059 million. About 87 percent of the debt was held by official creditors with multilateral organizations accounting for about 42 percent, and bilateral donors for 45 percent. Private creditors, both export and suppliers credits and credits from international financial institutions, account for 9 percent of Ethiopia's total debt outstanding.

9.2 Foreign Aid

With the Economic Reform Program on target and a second structural Adjustment Facility now in place, bilateral aid flows are steadily increasing. Ethiopia receives the bulk of official development assistance from bilateral donors such as Japan, the U.S., Germany and Italy as well as from the European Union, the World Bank Group, the UN, and the African Development Bank.

In December 1992, Ethiopia obtained favorable debt from the Paris Club reducing its debt service ratio from 82 percent in FY92 to 30 percent in FY95. The Government is attempting to secure comparable debt relief from other bilateral official creditors.

As an adjusting country, Ethiopia has participated in the World Bank's Special Program of Assistance (SPA) since 1992. The first Consultative Group (CG) took place in November 1992 and attracted donor pledges of over US$1.2 billion for the period up to mid-1994. The second CG was held in March 1994 which pledged US$1.1 billion for FY95.

To further underscore donor commitment to Ethiopian economic reforms, several bilateral agreements providing substantial financial and technical support have recently been concluded with Italy, France and Germany, and the United Kingdom.

Chapter 10

Labor

10.1 Employment and Unemployment

In Ethiopia, the labor force was estimated at approximately 22 million in 1988/90, of which about 80 percent were employed in the agriculture sector, mostly as subsistence farmers. The Government and the armed forces have been the most important sources of employment outside agriculture, providing work for almost 3 million people. The number of permanent and temporary workers employed in public sector manufacturing increased from 78,000 in 1978 to over 200,000 in 1989. In 1995, it is estimated that 30 percent of the Ethiopian workforce is unemployed.

Urban unemployment and underemployment are high, although this is partially offset by the parallel informal economy. The informal sector has burgeoned since the change of Government in 1991 due to the relaxation of trade restrictions. The forced or arbitrary conscription of urban youths into the army in the 1980's helped to mask the underlying unemployment problem. Just as many state-owned enterprises are to be dismantled or forced to downsize, the economy must find a way to absorb the over 200,000 largely unskilled young men who entered the labor market following demobilization. Nonetheless, the Government expects recently licensed private investors to create about 50,000 posts. Notwithstanding high levels of unemployment, there is an acute shortage of skilled personnel, exacerbated by the flight of trained cadres during the Mengistu regime. Because of Ethiopia's recent history of civil war and because some prominent Ethiopians abroad air their doubts as to the permanence of the present peace, some qualified expatriates harbor doubts over future stability or have become too inured to a higher standard of living abroad to re-adapt to conditions in Ethiopia.

10.2 Incomes and Wages Policy

Labor legislation in Ethiopia establishes the worker's right to a minimum wage. In 1985, a minimum wage was set for public sector employees who are by far the largest group of wage earners. Today, the public sector minimum wage is $16.80 per month, which is insufficient to provide a decent standard of living for a worker and family. According to the Office of the Study of Wages and Other Remunerations, a family of five requires a monthly income of $62.40 to subsist. There is no minimum wage in the private sector. The legal work week as stipulated in the 1993 Labor Law, is 48 hours, 6 days of 8 hours each, with a 24-hour rest period. However, in practice, most employees work a 40-hour workweek, 5 days of 8 hours each.

10.3 The Labor Act and Unions

The Constitution and 1993 Labor Law provide most workers with the right to form and join unions and engage in collective bargaining, but only about 250,000 workers are unionized. Employees of the Civil and Security Services (where most wage earners are found), judges, and prosecutors are not allowed to form unions. Workers who provide an "essential service" are not allowed to strike. Essential services include a large number of categories such as air transport, railways, bus services, police and fire services, post and telecommunications, banks, and pharmacies.

Unions are not affiliated with the Government or political parties. There is no legal requirement for unions to belong to the Confederation of Ethiopian Trade and Unions (CETU), which was established in 1993. CETU includes nine federations organized by industrial and service sector rather than by region. In December 1994, The Government de-certified CETU following a 30-day probationary period given to CETU to resolve internal disputes. In 1995, CETU Offices remained closed despite a court ruling that the CETU closing was improper. The law stipulates that a trade organization may not act in an overtly political manner.

The 1993 Labor Law explicitly gives workers the right to strike to protect their interests, but it also sets forth many constraints which apply before a legal strike may take place. These apply equally to an employer's right to lock out workers. Strikes may be supported by a majority of the workers affected by the decision. The Labor Law prohibits retribution against strikers.

Independent union and those belonging to CETU are free to affiliate with and participate in international labor bodies.

Collective bargaining is protected under the Labor Law and under the Constitution, and is practiced freely throughout the country. More than 90 percent of unionized workers are covered by collective bargaining agreements. Wages are negotiated at the plant level. Grievance procedures are in place to hear allegations of discrimination brought by individuals or unions. Employers found guilty of anti-union discrimination are required to re-instate workers fired for union activities.

Chapter 11

The Financial Sector

Banking and insurance institutions were nationalized in 1975. However, in keeping with the new economic policy of liberalization, new laws opening the banking and insurance sectors to the domestic private sector are now in effect, although foreign ownership is not allowed.

11.1 Banks

The National Bank of Ethiopia (NBE) serves as a central bank whose purpose is to foster monetary stability, a sound financial system and other credit and exchange conditions conducive to balanced economic growth. The NBE may buy, sell and hold foreign currency notes and coins and such documents and instruments including telegraphic transfers as are customarily employed in international payments or transfers of funds.

Commercial operations have been transferred to the Commercial Bank of Ethiopia (CBE). The CBE offers savings and checking accounts, extends short-term loans, deals with foreign exchange transactions, provides guarantee services, participates in equity investments and performs all other commercial banking activities. It has 151 branches including one in Djibouti.

In addition, there are two specialized banks, the Agricultural and Industrial Development Bank (AIDB) and the Housing and Savings Bank (HSB). The former extends medium to long-term loans for viable industrial and agricultural projects. The AIDB has 16 main branches and 15 sub-branches across the country. The HSB provides long-term loans for construction, acquisition or maintenance of dwellings, community facilities and real estate development.

The first private bank - Awash International Bank - began operations in early 1995. Since then, another private bank, the Dashen Bank, has secured a banking license and has recently started operations. The Bank of Abyssinia is also expected to open soon.

11.2 Legal and Regulatory Environment

Three fundamental proclamations were issued to regulate the banking and insurance sectors, namely:

1. Complete autonomy for the National Bank of Ethiopia to act as the Central Bank.

2. Establishment of private banks.

3. Establishment of private insurance companies.

Also, foreign enterprises which are formally registered and operating in Ethiopia are entitled to access to domestic credit borrowing, on the same terms and conditions applicable to Ethiopian companies.

11.3 Insurance

The insurance sector is also open for domestic private operators. The National Insurance Company of Ethiopia (NICE) started operations in early 1995. Four additional private insurance companies have opened their doors: United, Africa, Nile, and Universal.

11.4 Money and Capital Markets

There is no formal stock exchange in Ethiopia. The money and capital markets are underdeveloped and will take some time for economic and monetary policy, legislation and regulation to create the conditions for organized capital markets.

Chapter 12

Inflation and Price Controls

12.1 Inflation

Average annual inflation rate was reduced from higher than 20 percent during FY91-92 to 8 percent in FY93/95. However, the Addis Ababa retail price index showed that average annual inflation stood at almost 14 percent in August, calling into question the Government's ability to meet its 10 percent inflation target for 1995/96. Prices had risen steeply in the months to April.

12.2 Price Controls

Prices of most consumer goods have been significantly de-controlled. Exceptions include petroleum, fertilizer and pharmaceuticals.

Chapter 13

Public Finance

13.1 Public Expenditure

Ethiopia has made substantial progress in reforming its public expenditures. After two decades in which public finances were dominated by the effects of war and drought, budgets since 1992 have reflected the following reorientation in priorities: a substantial increase in capital budgets; expenditures transferred from the military to health and education; and increased regional control over expenditure.

Defense expenditure has been reduced from 31 percent of the total budget before the reform period to 7 percent of the total budget in FY95. In this latter year, defense spending was only about 2 percent of GDP, compared with a sub-Saharan average of 4.5 percent of GDP. Budgetary allocations for social expenditures encompassing health and education were increased from around 16 percent of total budget (4 percent of GDP) during the pre-reform period, to around 23 percent (nearly 7 percent of GDP) in FY95.

13.2 Tax Revenues

From the mid-1970's, war steadily eroded the Government's tax base. While Government revenue increased by an average of 8 percent per year between 1979/80 and 1987/88, the proportion derived from taxes fell from 83 percent to 73 percent over the same period. Much of the increase was financed by transfers of profits made by public enterprises.

The budget deficit before grants is projected to be approximately 8 percent of GDP annually for the period FY96-98. This is largely due to the need to increase operations and maintenance spending for the rehabilitation and expansion of infrastructure. A portion of imports will continue to support reconstruction of the war-torn economy. Growth prospects for exports are optimistic in the next few years due to expected increases in coffee receipts.

Some customs revenue has been diverted recently as a result of contraband at the country's porous borders. Estimates of revenue lost due to smuggling vary between Birr100m and Birr250m. However, illegal trade at Bole airport has been greatly reduced in recent years. Nonetheless, the Djibouti, Hargeisa and Dire-Dawa triangle remains the principal conduit for illegal merchandise entering the country. The Customs Authority identified airline employees, relief workers and NGO's as the main offenders.

Chapter 14

Taxation and Investment Incentives

14.1 Main Taxes and Duties

Main taxes levied by the Government of Ethiopia include the following:

- Personal Income Tax - Progressive
- Corporate Profit Tax - 40%
- Income tax on mining - 35%
- Tax on services - 10%
- Sales tax on domestic products - 12%

Duties levied by Customs Authority:

- Import duty - ad valorem duty varies according to product. Customs Tariff based on Harmonized System.

- Import sales tax - maximum 12%

- Excise Tax on luxury imports - 50% - 200%

14.2 Incentives

In order to promote private sector participation, both local and foreign, significant incentives are granted for selected industries. The incentives vary by industry and level of investment. Some of the major incentives and protections granted are:

- Exemption from payment of Import Customs Duties for up to 15 percent of the value of capital invested, provided that imported goods are unavailable locally. Exemption of such duties for raw materials necessary for export production.

- Capital goods and equipment imported without import duties are transferable.

- Ethiopian products and services destined for export are exempted from Export Customs Duties (for products other than coffee).

- Income Tax Holidays varying between 3-5 years on approved investment projects.

- Research & Development expenses are deductible in the calculation of corporate tax dues.

- Exemption from payment of Taxes on Remittance of Capital on proceeds from the sale or transfer of shares/assets upon liquidation or closure of an enterprise to a domestic investor.

- Remittance of funds in foreign exchange for the purposes of transferring profits, dividends, royalties, or any other payments for technology transfer or management agreements related to the investment.

New laws and incentives have been devised to ensure a modern legislative basis in line with international standards in addition to incentives listed above. Some of the major additional incentives granted by petroleum and mining legislation are:

- Exemption from payment of Import Customs Duties of any kind for any mining equipment and machinery.

- Personal income tax exemption for employees. Expatriate employees are entitled to import household goods, personal effects, including one sedan car free of any duties and levies of any kind.

- Companies investing in mining or petroleum operations are entitled to export goods free of export duties and taxes of any kind.

- No dividend withholding tax on petroleum operations. Dividend withholding tax of 10 percent on other mining operations.

- Corporate income tax rates of 35 percent for operations. Reinvested income shall be tax deductible, in addition to a wide range of qualifying expenses.

- Loss carry forward for 10 consecutive years.

- Accelerated depreciation within a useful life of four consecutive years.

- Royalty payments range from 0-5 percent depending on minerals extracted and the strategic importance of projects.

Appendix A

Economic Structure

Economic indicators	1990	1991	1992	1993	1994
GDP at factor cost[a] Birr bn	18.5	19.4	24.5	25.3	n/a
Real GDP growth %	-6.7	-8.7	12.3	1.4	5.5[b]
Consumer price inflation %	5.1	35.7	10.5	3.5	7.6
Population M	51.7	53.4	55.1	56.9	n/a
Exports fob $M	292	168	170	199	327
Imports fob $M	912	471	993	706	898
Current Account $M	-294	103	-125	-73	n/a
Total external debt $M	3,780	4,169	4,360	4,729	n/a
External debt/service ratio %	28.0	18.7	13.5	8.9	n/a
Coffee production[c] 000 tons	174	184	210	222	228[d]
Exchange rate (average) Birr:$	2.07	2.07	2.81	5.0	5.09

Principal exports 1993[a]	$M
Coffee	179
Hides & Skins	40
Gold	35

Principal imports 1993[a]	$M
Food & live animals	111
Crude petroleum	79
Petroleum products	64
Chemicals	44

Main destinations of exports 1993[a]	% of total
Germany	18.0
Japan	13.3
Djibouti	10.4
Saudi Arabia	7.7

Main origins of imports 1993[a]	% of total
Saudi Arabia[e]	13.3
Italy	11.6
USA	10.2
Germany	9.1

[a]Fiscal years starting July 8. [b]Government target. [c]Crop year beginning in calendar years (October-September). [d]Official estimate. [e]Includes transhipment of product originating in other parts of the world.

Appendix B

Contact List

CONTACT	ADDRESS	PHONE
I. CONTACTS IN THE USA and AFRICA		
U.S. Department of Commerce	International Trade Administration Office, Washington, D.C. 20230	Tel: (202) 482-0543
Embassy of Ethiopia	Main Chancery 2134 Kalorama Road, N.W. Washington, D.C. 20008 Trade Affairs Office 1800 K Street, NW Suite 624 Washington, D.C. 20006	Tel: (202) 234-2281 Fax: (202) 328-7850 Tel: (202) 452-1272 Fax: (292) 223-0137
Corporate Council on Africa	1660 L Street, NW, Suite 301 Washington, D.C. 20036	Tel: (202) 835-1115 Fax: (202) 835-1117
U.S. Trade and Development Agency	SA-16 Room 309 Washington D.C. 20523-1602	Tel: (703) 875-4357 Fax: (703) 875-4009
Overseas Private Investment Corporation - OPIC	Insurance and Finance Divisions 1100 New York Avenue, NW Washington, D.C. 20527	Tel: (202) 336-8400
Export-Import Development Bank (EXIMBANK)	811 Vermont Avenue, NW Washington, D.C. 20571	Tel: (202) 565-3946
African Development Bank	Office of the U.S. Executive Dir. Avenue Joseph Anoma 01 BP 1387 Abidjan 01, Cote d'Ivoire	Tel: 225-214616 Fax: 225-223259
U.S.-Ethiopian Trade and Economic Council (USATEC)	222 Ontario Street, Suite 502 Chicago, IL 60610	Tel: (312) 787-2716 Fax: (312) 787-2680
II. CONTACTS IN ETHIOPIA		
A. Ministry and Government Offices		
Ministry of Economic Development & Cooperation	P.O. Box 2428 Addis Ababa, Ethiopia	Tel: 2511-519684 Fax: 2511-517988
Ministry of Trade and Industry	P.O. Box 2559 Addis Ababa, Ethiopia	Tel: 2511-518200 Fax: 2511-514288
Investment Office of Ethiopia	P.O. Box 2428 Addis Ababa, Ethiopia	Tel: 2511-512400 Fax: 2511-514396

CONTACT	ADDRESS	PHONE
Ethiopian Chamber of Commerce	P.O. Box 517 Addis Ababa, Ethiopia	Tel: 2511-518240 Fax: 2511-517699
Ethiopian Import Export Corporation	P.O. Box 2313 Addis Ababa, Ethiopia	Tel: 2511-512400 Fax: 2511-514396
B. U.S. Official Representation in Ethiopia		
United States Embassy	P.O. Box 783	Tel: 2511-550666
C. U.S. Firms with Branch Offices in Ethiopia		
AFCOR (Ethiopia) P.L.C. IBM	P.O. Box 3533 Addis Ababa, Ethiopia	Tel: 2511-518444 Fax: 2511-517788
Airborne Express and United Parcel Service	P.O. Box 41519 Addis Ababa,Ethiopia	Tel: 2511-654206 Fax: 2511-654206
Boeing Commercial Airplane Company	P.O. Box 1755 Addis Ababa, Ethiopia	Tel: 2511-612222, ext. 484 Fax: 2511-610566
Coca-Cola Africa Ltd.	P.O. Box 2815 Addis Ababa, Ethiopia	Tel: 2511-513158 Fax: 2511-510064
Ethiopian Crown Cork & Can Mfg. Ind.	P.O. Box 5501 Addis Ababa, Ethiopia	Tel: 2511-340403 Fax: 2511-340216
Hunt Oil Company - Ethiopia	P.O. Box 5144 Addis Ababa, Ethiopia	Tel: 2511-613196 Fax: 2511-613521
MCI International	P.O. Box 10989 Addis Ababa, Ethiopia	Tel: 2511-653744 Fax: 2511-551630
Mobil Oil East Africa Ltd.	P.O. Box 1365 Addis Ababa, Ethiopia	Tel: 2511-651125 Fax: 2511-652058
Pepsi-Cola International, East Africa	P.O. Box 2311 Addis Ababa, Ethiopia	Tel: 2511-164216 Fax: 2511-654844
Pratt & Whitney	P.O. Box 1755 Addis Ababa, Ethiopia	Tel: 2511-611509 Fax: 2511-611677
Pioneer Hi-Bred Seeds, Inc.	P.O. Box 1134 Addis Ababa, Ethiopia	Tel: 2511-510725 Fax: 2511-510155
F.C. Schaffer-Servtech	P.O. Box 6660 Addis Ababa, Ethiopia	Tel: 2511-517550 Fax: 2511-512530
D. Banks in Ethiopia		
National Bank of Ethiopia	P.O. Box 5550 Addis Ababa, Ethiopia	Tel: 2511-517430 Fax: 2511-514588
Commercial Bank of Ethiopia	P.O. Box 255 Addis Ababa, Ethiopia	Tel: 2511-515004 Fax: 2511-514522

CONTACT	ADDRESS	PHONE
Housing and Savings Bank of Ethiopia	P.O. Box 3480 Addis Ababa, Ethiopia	Tel: 2511-512300 Fax: 2511-154590
Agricultural and Industrial Development Bank	P.O. Box 1900 Addis Ababa, Ethiopia	Tel: 2511-511188 Fax: 2511-511606
Awash International Bank	P.O. Box 12638 Addis Ababa, Ethiopia	Tel: 2511-612919, 614482 Fax: 2511-614477
Dashen Bank	P.O. Box 12752 Addis Ababa, Ethiopia	Tel: 2511-654585 Fax: 2511-653037
Bank of Abyssinia	P.O. Box 12947 Addis Ababa, Ethiopia	Tel: 2511-159966, 514752 Fax: 2511- 514754

Appendix C

Visiting Ethiopia

Entry and Exit Requirements

A passport and visa are required of all travelers. Airport visas are not available to travelers departing from or traveling through countries where an Ethiopian diplomatic mission is located. Evidence of immunization against yellow fever is also required upon entry. Visa applications and instructions are available at the Ethiopian Embassy in Washington, D.C. Departure taxes of $10, payable in hard currency, are levied on all foreign travelers.

Currency

Visitors must declare hard currency upon arrival and may be required to present the declaration upon departure. Strict penalties exist for exchanging money on the black market. Credit card use is not widely accepted and foreigners must pay in US$ or US$ denominated travelers cheques. Banking hours: 8 a.m. to 12 p.m. and 1 p.m. to 4 p.m., Monday through Thursday. Banks may be closed for a two-hour Moslem prayer period on Fridays. Banks are closed Saturday.

Hotel Accommodation and Car Rental Agencies

Two international standard hotels are available: Addis Ababa Hilton Hotel and Sheraton Addis Ababa. Various car rental agencies also provide a wide range of vehicles with or without drivers.

Medical Facilities and Services

Travelers generally arrive with their own supply of medication, both prescriptive and preventive. Medical services rendered are usually paid for in hard currency. A list of physicians for Americans can be readily obtained from the U.S. Embassy for internal medicine, pediatrics, general surgery, obstetrics & gynecology, dental, optical, HIV and veterinary services.

Public Holidays

September 11	Ethiopian New Year's Day
September 27	Maskal Day, feast of the Finding of the True Cross
January 7	Ethiopian Christmas
January (date varies)	Ethiopian Epiphany
March 2	Victory of Adwa
March 18	Id-al-Fitr
April 6	Ethiopian Patriots Victory Day
May 20	Id-al-Adha
Based on Ethiopian calendar	Good Friday and Easter
Based on Lunar calendar	Id-al-Adha, Maulid and Id-al-Fitr

Appendix D

Sources Consulted

1. The Economist Intelligence Unit
   a. 1994/1995 Country Profile
   b. Country Report 4th Quarter, 1995
2. World Bank Reports
3. 1996 U.S. Department of State Human Rights Report for Ethiopia
4. Country Commercial Guide - Ethiopia FY 1996 compiled by the U.S. Embassy in Ethiopia
5. The Indian Ocean Newsletter
6. Europa World Yearbook, 1995
7. The Investment Office of Ethiopia
8. The Embassy of Ethiopia, Trade Affairs Office
9. Ethiopian Bir: Business and Industry Report