Challenges and Opportunities of Private Investment, Case of South Wollo Zone

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Research Work On:

“Challenges and Opportunities of Private Investment in South Wollo Zone”

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Abstract

This paper was designed to analyze the challenges and opportunities of private investment in South Wollo zone manufacturing firms perspectives. The paper contains five parts; part one about the introduction section comprising of background of the study, problem statement, objectives, significance, and scope of the study, part two empirical and theoretical literature, part three the research methodology, part four the analysis of data, and part five summary of major findings, conclusion, and recommendation. Both primary and secondary data was utilized for the accomplishment of the intended objectives. The secondary data focused on the macro economic factors those are perceived to affect the smooth functioning of private investment and show the future potential of the private investment section. The totals of 34 manufacturing firms are surveyed in the paper using census method. In the time series data 10 years data was utilized and the investment distribution by sector and by region was also analyzed. The findings of the study showed that the distribution of investment both by sector and region was not fair enough. The macro economic factors can determine the growth of the private investment including the expansion of public investment. According to the findings in this paper distribution of investment by region was dominated by Addis Ababa (69.7%), Oromia, Amhara, Dire dawa, and SNNP regions took the 2nd, 3rd, 4th, and the 5th ranks. The distribution by sector showed that rent, real estate, and business activities takes the highest investment with about 61.3% and Hotel and restaurant takes the lowest portion of investment with about 3% and the manufacturing sector takes the second rank with not more than 14.3% but in terms of approved project capitals the manufacturing takes the largest portion with about 31.6%. Lack of demand, getting credit, higher level of interest, infrastructure are among the major obstacles for private investment. Moreover the uncertainty variables can highly affect the investment sector. Demand uncertainty, interest rate uncertainty, and foreign exchange rate uncertainty variables are the major factors those affect the private investment sector. Macro-economic variables and the expansion of public investment affect the expansion of the private investment as the finding showed in this paper.

Key words: private investment, macroeconomic variables, government investment, uncertainty variables

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List of Acronyms

ERP: Economic Reform programme

FDI: Foreign Direct Investment

FX: Foreign Exchange

GDP: Gross-Domestic Product

GTP: Growth and Transformation Programme

IMF: International Monetary Fund

BOP: Balance of payment

C/A: Current Account

PUBI: Public investment

PRIVI: Private investment

GDI: Gross domestic investment

CSA: Central statistics agency

RRB: rent, real state, and business

MN: Manufacturing business

CN: Construction business

AG: Agriculture

HR: Hunting and Forestry

AA: Addis Ababa region

OR: Oromia region

AM: Amhara region

DR: Diredawa region

SNNP: Southern nations and nationalities region

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CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The theories of investment date back to Keynes, who first called attention to the existence of an independent investment function in the economy (Yaw, 2000). A central feature of the Keynesian analysis is the observation that although savings and investment must be identical ex-post, savings and investment decisions are, in general, taken by different decision makers and there is no reason why ex-ante savings should equal ex-ante investment. The next phase in the evolution of investment theory gave rise to the accelerator theory, which makes investment a linear proportion of changes in output. In the accelerator model, expectations, profitability and capital costs play no role. Keynesians have traditionally favored the accelerator theory of investment while disregarding the role of factor costs (Ibid).

A more general form of the accelerator model is the flexible accelerator model. The basic notion behind this model is that the larger the gap between the existing capital stock and the desired capital stock, the greater a firm's rate of investment. The hypothesis is that firms plan to close a fraction of the gap between the desired capital stock, K^* , and the actual capital stock, K , in each period.

According to Asante and others (2006), within the framework of the flexible accelerator model, output, internal funds, cost of external financing and other variables may be included as determinants of desired capital stock symbolized as K^* . The flexible accelerator mechanism may be transformed into a theory of investment behavior by adding a specification of K^* and a theory of replacement investment. Alternative econometric models of investment behavior differ in the

determinants of K^* , the characterization of the time structure of the investment process and the treatment of replacement investment. In the flexible accelerator model, K^* is proportional to output, but in alternative models, K^* depends on capacity utilization, internal funds, the cost of external finance and other variables.

Jorgenson (1971) and others have formulated the neoclassical approach, which is a version of the flexible accelerator model. In this approach, the desired or optimal capital stock is proportional to output and the user cost of capital (which in turn depends on the price of capital goods, the real rate of interest, the rate of depreciation and the tax structure).

In the "Q" theory of investment (which is also in the neoclassical framework) associated with Tobin (1969), the ratio of the market value of the existing capital stock to its replacement cost (the "Q" ratio) is the main force driving investment. Tobin argues that delivery lags and increasing marginal cost of investment are the reasons why Q would differ from unity.

Another approach dubbed "neoliberal" (Galbis, 1979:423) emphasizes the importance of financial deepening and high interest rates in stimulating growth. The proponents of this approach are McKinnon (1973) and Shaw (1973). The core of their argument rests on the claim that developing countries suffer from financial repression (which is generally equated with controls on interest rates in a downward direction) and that if these countries were liberated from their repressive conditions, this would induce savings, investment and growth. Not only will liberalization increase savings and loanable funds, it will result in a more efficient allocation of these funds, both contributing to a higher economic growth.

In the neoliberal view, investment is positively related to the real rate of interest in contrast with the neoclassical theory. The reason for this is that a rise in interest rates increases the volume of financial savings through financial intermediaries and thereby raises investible funds, a phenomenon that McKinnon (1973) calls the "conduit effect".

Thus, while it may be true that demand for investment declines with the rise in the real rate of interest, realized investment actually increases because of the greater availability of funds. This conclusion applies only when the capital market is in disequilibrium with the demand for funds exceeding supply.

More recent literature has introduced an element of uncertainty into investment theory due to irreversible investment (Pindyck, 1991). The argument is that since capital goods are often firm-specific and has a low resale value; disinvestment is more costly than positive investment. He argues that the net present value rule invest when the value of a unit of capital is at least as large as its cost must be modified when there is an irreversible investment because when an investment is made, the firm cannot disinvest should market conditions change adversely. This lost option value is an opportunity cost that must be included as part of the cost. Accordingly, "the value of the unit must exceed the purchase and installation cost, by an amount equal to the value of keeping the investment option active" (Pindyck, 1991: 1112).

Rodrik (1991) introduces another element of uncertainty policy as a determinant of private investment. When a policy reform is introduced, it is very unlikely that the private sector will see it as one hundred percent sustainable. A number of reasons may be adduced, among them the expectation that the political-economic configuration that supported the earlier policies may resurface. There is also the fear that unexpected consequences may lead to a reversal. Investors must respond to the signals generated by the reform for it to be successful. However, rational behavior calls for withholding investment until much of the uncertainty regarding the eventual success of the reform is eliminated.

It is clear from the discussion in the above section that private investment depends on three broad categories of variables: Keynesian, neoclassical, and uncertainty variables.

Variables that may be included in the Keynesian tradition include growth rate of GDP, internal funds (for example, change in credit to the private sector) and capacity utilization. The neoclassical determinants of private investment include Tobin's Q , real interest rate, user cost of capital and public investment ratio. There are three uncertainty variables. The first is variability (variance, moving standard deviation or moving coefficient of variation) of the user cost of capital, real exchange rate, inflation rate, distortions in the foreign exchange market (proxied by the black market premium) and real GDP. The second uncertainty variable is the debt/GDP ratio and the third is debt service as a ratio of exports of goods and services.

Ethiopia, located in Eastern Africa, is the most populous landlocked country worldwide and the second most populous country in Africa. The economy is agriculture based, despite some

diversification in recent years. The degree of modernization in agriculture is low, so the economy is highly susceptible to weather conditions. Ethiopia has a history of frequent droughts leading to famine. Large hydropower capacity makes Ethiopia the largest energy supplier in East Africa. The country's most important trade partner is China. However, neighbor Djibouti is a particularly important business partner, as it gives Ethiopia access to the sea (World Bank, 2013).

Ethiopia's economy is dominated by the state and is relatively closed, since authorities restrict private and/or foreign participation in many sectors for instance, telecommunication. Prioritizing pro-poor spending has led to marked improvement of human development. For example, poverty almost halved between 2005 and 2011 and the country is one of the few African states with a social assistance programme. Ethiopia is one of the oldest countries in the world (2000 years) and the only African country that maintained independence from colonial rule, bar 4 years of occupation by the Italians (World Bank, 2014).

In 2002, the Government of Ethiopia launched its Economic Reform Programme (ERP), which was intended to reverse the Command economy of the military government (Derg). Prior to this, inappropriate domestic policies coupled with civil wars led to a severe deterioration in economic and financial performance (Demetiru, 2014).

Large fiscal deficits, financed primarily from domestic revenue collected from tax and other sources gave rise to high rates of inflation and an over-valued exchange rate. Heavy government intervention in the economy, as well as massive expansion of the public sector through the establishment of a large number of state enterprises, worsened the distortions in the economy and destroyed any incentives to produce, save and invest (Ibid).

Initially, the ERP focused on macroeconomic and infrastructural policies intended to address certain imbalances and distortions in the economy. A lot of progress has been made. The government has pursued a programme of financial and structural reforms that have been hailed by the international community as a good example of adjustment with growth.

These reforms have been supported not only by the IMF and the World Bank but also by bilateral and multilateral external financial assistance. As a consequence, Ethiopia's

macroeconomic and financial performance has improved substantially after a prolonged period of decline.

Despite the improvements in economic performance, however, Ethiopia continues to be confronted with a number of constraints. Among the constraints are levels of savings and investment that are too low to allow self-sustained growth. This has caused a lot of concern in government and academic circles about the sustainability of the achievements so far. According to the World Bank and other sources (2008-2009), the level of domestic savings and investment is inadequate to fuel the growth needed to raise living standards and generate sufficient productive employment. The Bank notes that the major share of the additional savings and investment required must come from public sources. Consequently, the present study seeks to study investment behavior. Investment plays a crucial role in models of economic growth. It is an essential component of aggregate demand, and fluctuations in investment have considerable effect on economic activity and long-term economic growth. The view that capital formation is the key to growth, called "capital fundamentalism" by Youopoulos and Nugent (1976), was reflected in the development strategies and plans in many countries. While capital accumulation is no longer viewed as a panacea for poor countries, it is nevertheless clear that even mildly robust growth rates can be sustained over long periods only when countries are able to maintain investment at a sizeable proportion of GDP. The proportion can rarely be less than 10% and in some cases it must go as high as 10%, 8.2% in 2013 and 7.9% in 2014 (Dumetiru et. 2014). Based on the determinants of private investment, policy makers could better control private investment in the desired direction to foster economic growth and development.

The attitude of government towards private investment has changed very little over time. The hostility attitude towards private investment started with the Federal democratic Republic of Ethiopia government in the 2000s. After taking the view that the Ethiopia's economic policy is based on a 5-year Growth and Transformation Plan (GTP), which envisages improvements in infrastructure, human development and agricultural productivity through public support. The large public investments (19% of GDP, third highest in the world) are largely financed domestically, including through compulsory financing by commercial banks and direct financing by the central bank. These high investment levels led to very strong domestic demand, which on its turn fuelled inflation, with consumer price inflation reaching 40% in August 2011, and

increased FX demand. FX restrictions are in place to prioritize public demand. Furthermore, private sector investment has been crowded out and private sector development in general has been hampered. Tighter monetary policy in the form of less monetary financing, aided by lower prices for food and imported fuel, brought down the inflation to single digits in 2013 (Dumetiru, 2014).

In Ethiopia there were about 2000 large and medium scale manufacturing industries according to the data from Central Statistical Agency. These industries are engaged in the production of food items, soft drinks, edible oil, metal and wood work products, beer, textile, and other similar products. The ownership composition is private and public, with very higher share of the private firms (about 88% of the total). This shows that the manufacturing industries in the country were dominated by the private owners with a higher level of difference.

In Amhara region there were about 182 large and medium manufacturing firms. Their nature of ownership is also dominated by the private owners (about 2% public and more than 87% private) manufacturing industries.

The distribution of the industries is unfair. For instance, in the capital of the country (Addis Ababa) and Oromia regions collectively more than 70% of the total. It shows that most of the investors are not investing in other places of the country at the regional, zonal, and woreda level. It is due to different constraints those affect the manufacturing industry. Accordingly, the researcher's intention was to investigate the determining factors those affect private investment of manufacturing firms and the opportunities exist in South Wollo and Oromia Zone; Dessie, Kombolcha, Kemissie, and Haik towns in Amhara National Region.

1.2. Statement of the Problem

The view that capital formation is the key to growth, called "capital fundamentalism" by Youopoulos and Nugent (1976), was reflected in the development strategies and plans in many countries. While capital accumulation is no longer viewed as a panacea for poor countries, it is nevertheless clear that even mildly robust growth rates can be sustained over long periods only when countries are able to maintain investment at a sizeable proportion of GDP. The proportion can rarely be less than 10% and in some cases it must go as high as 10%, 8.2% in 2013 and 7.9% in 2014 (Dumetiru et. 2014). Based on the determinants of private investment, policy makers

could better control private investment in the desired direction to foster economic growth and development.

The Industrial and Economic Growth in the country was very weak or absent in most areas of the country. All the infrastructures, Institutions and Instruments for accelerated manufacturing growth in particular and economic growth in general are either very weak or absent altogether (World Bank and different sources). This must be a critical factor in the low or weak performance of the economy in general and manufacturing in particular.

Such an environment affects both the domestic private sector and FDI. But before assessing the impact of the post-reform period on private investment, it will be better to briefly review the results of the reforms on the behavior of the private Investment; manufacturing and overall growth of Ethiopia's economies by analyzing the challenges and opportunities of private investment behavior using different indicators.

The pattern is as clear as it is depressing. All the indicators used have been going down reached their crisis point, and have continued to decline despite some improvement since the 2006s, which however, have not been enough to reverse the trend (the past) or reach the levels of the developmental economy. FDI was expected to change the picture somewhat, and despite the improvements and its performance reflects the depth of the problems of industrialization in Ethiopia. According to Alexandra (June, 16, 2014), Ethiopia continues to record robust growth. However, the state-led development model is constraining the private sector and has resulted, from time to time, in macroeconomic imbalances, and therefore seems unsustainable in the long term. The country showed narrow economic base and unsustainable economic model. Agriculture accounts for 50% of GDP, 75% of employment and more than 80% of exports. Hence, the economy is very susceptible to volatility on global commodity markets and to weather patterns.

Ethiopia's state-led development economic model is not sustainable in the long term, as financing by the central bank leads to macroeconomic instability and hinders private sector development. Moreover, the development trend is poor. Despite progress in recent decades, human development is very poor. Against this background, episodes of double digit inflation that erode purchasing power significantly could spark social turmoil (World Bank, 2014).

After a decade of very strong performance (9% average economic growth), economic growth slowed down somewhat, but remained nevertheless relatively high. In 2013, economic growth decreased to 7.1%, from 8.5% in 2012, driven down by a marked slowdown in gross fixed investments. Ethiopia's economic policy is based on a 5-year Growth and Transformation Plan (GTP), which envisages improvements in infrastructure, human development and agricultural productivity through public support. The large public investments (19% of GDP, third highest in the world) are largely financed domestically, including through compulsory financing by commercial banks and direct financing by the central bank. These high investment levels led to very strong domestic demand, which on its turn fuelled inflation, with consumer price inflation reaching 40% in August 2011, and increased FX demand. FX restrictions are in place to prioritize public demand. Furthermore, private sector investment has been crowded out and private sector development in general has been hampered.

Ethiopia's ambitious public investment plan has also increased pressure on the country's fiscal and external position. In 2013, the budget deficit increased from 2.8% of GDP in 2012 to 3.3% of GDP and public debt increased from 42% in 2012 to 48% of GDP. While net transfers remained strong at 12% of GDP thanks to remittances from the Ethiopian Diasporas and donor assistance, the current account deficit also deteriorated, from 7.2% of GDP in 2012 to 9.8% of GDP in 2013. As FDI is moderate (2% of GDP in 2013), Ethiopia relies on debt financing to cover the shortfall. Financing has been provided mainly by official creditors; in recent years, such financing came especially from China. Besides, the critically low level of FX reserves - just under 3 months of imports - makes the country highly vulnerable to a deterioration of the current or capital account balances. External debt is mainly public (at least 95% of it). Its favorable structure, 95% is medium to long term and 76% owed to official creditors, provides some comfort, but the strong increase of the debt burden in recent years is concerning. Indeed, external debt in 2013 was 30% of GDP, twice the level of 2006. The fact that the three international rating agencies have for the first time extended a sovereign rating to Ethiopia has widened access to international markets, which might contribute to a further deterioration of the balances. In 2014, the current account deficit is forecast at 11% of GDP and the public deficit at 3.4% of GDP. All in all, the government's infrastructure plans are set to further hurt external and fiscal balances. However, the still relatively low levels of both external and public debt provide some comfort. In general, the development of private investment in the region is limited, the

contribution to GDP is also very low, and most of the investor's attention to invest is on merchandise and service sectors rather than investing on manufacturing business. Based on this, the researcher designed to analyze the determinants of private investment behavior in the region in particular using the time series analysis and cross sectional analysis.

1.3. Objectives of the Study

1.3.1. General Objective

The primary objective of the study is to analyze the challenges and opportunities of private investment in South Wollo and Oromia Zones of the four towns in Amhara national region between the years 2004/5 and 2014/15. For this purpose, the researcher was used both time series and cross sectional analysis. The cross-sectional analysis was used to determine whether the factors identified in the time series analysis are still constraints to private investment.

1.3.2. Specific Objectives

Specifically, the study seeks to:

- (1) Estimate a time series model with private investment as the dependent variable to determine significant explanatory variables;
- (2) Identify the factors that are perceived to influence the investment decisions of private manufacturers by surveying manufacturing firms;
3. To analyze the major economic factors those perceived to affect the investment sector in the country.
- (4) To analyze the consistency of the time series analysis (secondary data) with the cross-sectional analysis, (primary data immediately collected), and
- (5) To suggest possible solutions for the problem.

1.4. Hypotheses to be tested

The following specific hypotheses were tested:

1. Macroeconomic and political instability have inhibited private investment.
2. Lack of a financial system oriented towards business has been a constraint to private investment.
3. Public investment crowds in/out private investment.

1.5. Significance of the Study

This study will be important to the growth of investment sector in particular and the Economic growth in Ethiopia in general by providing recommendable solutions those mitigate the obstacles in private investment and providing conducive investment theories and models important for the country's policy makers and governors because the government support the prospects of private sector in the country irrespective of the determinants of private investment behavior in each region. In addition to the above described significance, it will also help private investors (both existing and potential), the government in providing the needs and interest of both parties each other, and the society in general for the contribution of knowledge, material and other factors important for the growth of private investment. Furthermore, the results of this study will be used as a reference for further investigations by showing the important gaps those need more and deep study for academicians and researchers including students.

1.6. Scope of the Study (Delimitations)

This study was bounded to cover the medium and large scale Manufacturing Industry Investment South Wollo and Oromia Zones of four towns in Amhara national region.

These regions were account for massive investment activity in the area according to the Central Statistical Agency. The subjective scope of the study will be limited to analyze the time series data related with economic growth indicators (e.g. growth rate of GDP, internal funds, etc) and cross sectional analysis related with firm characteristics, perceptions about the economy and business environment, production and sales pattern and so on and their impact on manufacturing industries.

1.7. Conceptual (Theoretical) Framework

According to Yaw (2000), private investment depends on three broad categories of variables. The first one is the Keynesian model that described it as “the growth rate of GDP, internal funds (e.g. change in credit to the private sector, and capacity utilization) can affect private investment and shown in the following equation: $I = \delta (K^* - K_1)$, where,

I = net investment, K^* = desired capital stock, K = last period’s capital stock and δ = partial adjustment coefficient. The second model shows that (neoclassical) private investment can be determined by the ratio of market value of existing capital stock to its replacement cost, real interest rate, user cost of capital, and public investment ratio. Finally, there are uncertainty variables that can affect private investment. This include the variability of user cost of capital, real exchange rate, inflation rate, distortions in FX market (peroxided by the black market premium), real GDP, and the debt to GDP ratio, and debt service as a ratio of exports of goods and services. The relationship between the dependent and Independent Variables is depicted with the diagram below.

Figure 1.7.1. Model of Private Investment decision variables (Source: Own Developed)

CHAPTER TWO

LITERATURE REVIEW

2.1. Overview of Investment in Ethiopia

The Ethiopian Investment Agency and Regional Investment Offices licensed 69,079 investment projects with an aggregate capital of Birr 1.3 trillion in the period between 1992/93 – 2012/13. Of these projects, 58,735 (85 percent) were domestic, 10,220 (14.8 percent) foreign and 124 (0.2 percent) are public. In terms of capital, Birr 518.2 billion (38.8 percent) was from domestic investors, Birr 515.6 billion (38.6 percent) from foreign investors and Birr 303.0 billion (22.6 percent) from the public sector (Table 7.1). Similarly, during the GTP period the Ethiopian Investment Agency and Regional Investment Offices licensed a total of 18,980 projects with a capital of 507.7 billion birr. In 2012/13, a total of 7,011 investment projects with a combined capital of Birr 112.1 billion were approved. The number of domestic investment projects reached 6,273 which accounts for more than 89.5 percent of the total projects approved during the review period, whereas foreign projects reached 722 (10.5 percent). The capital performance for foreign investor projects during the review period found to be about 19.5 percent higher than the same period last year. Regarding to investment capital, domestic private projects which made up Birr 34.8 billion or (31.1 percent) while foreign investment projects accounted for Birr 49.5 billion (44.2 percent) of the total approved investment capital while the remaining (24.8 percent) was carried out by the government. Upon commencement of operation, the approved investment projects are expected to create job opportunities for 125,658 permanent and 255,931 casual workers.

2.1.1 Investment by Sector in Ethiopia

The total number of approved projects during the FY 2012/13 was to much more than the past years. When distributed to different sectors, 61.3 percent were in real estate, renting and business activities (RRB); 14.3 percent in manufacturing (MN); 10.3 in construction (CN), 6.7 in Agriculture, hunting and forestry (AHF); and 3 percent in hotel and restaurants (HR). In terms of approved investment capital, manufacturing constitutes the largest share (31.6 percent), followed by electricity, gas, steam & water supply (24.7 percent), real estate, renting & business activities

(18.5 percent), agriculture, hunting & forestry (10.9 percent), construction (4.9 percent) and hotel & restaurants (4.7 percent).

Figure 2.1. Investment by sector in Ethiopia (in percentage)

The figure above shows that the highest amount of money was invested on real estate (about 61.3%) and the lowest amount of investment was on hotel and restaurant, which was about 4.7% of the total amount of investment. The manufacturing sector takes the second rank which was about 14.3%, construction and agriculture, hunting and forestry take the second and the third rank with about 10.3 and 6.7% consecutively. But in terms approved projects or investment capitals the manufacturing sector takes the largest which was about 31.6% followed by electricity, gas, steam, and water supply with about 24.6%.

2.1.2 Investment Distribution by Region

In Ethiopia the total 7,011 investment projects approved in the review period; Addis Ababa attracted 4,890 projects (69.7 percent) with Birr 36.1 billion investment capitals, followed by Oromia 846 (12.1 percent) projects with capital of 49.1billion, Amhara 829 (11.8 percent) projects with 10.5 billion birr of capital, Dire Dawa 170 projects and SNNPR 125 projects, and only 0.4% was shared by other regions.

Figure 2.2. Investment distribution by Region

The figure above shows the investment distribution by region in the country. Addis Ababa (the capital of the country) takes the largest portion with about 4,890 projects (69.7%) followed by the Oromia region with 846 projects (12.1%). The Amhara, Diredawa, and Southern Nations and Nationalities take the 3rd, 4th, and 5th rank with 11.1, 2, and 1.9% respectively. The other regions take very small share that was only 0.4%. This shows that the distribution of investment projects was not equally attracted investors due to different factors discussed in this paper.

Table 2.1.number and capital of approved Projects by Region (Capital in millions of ETB).

Region	2010/2011		2011/2012		2012/2013		Project share to:	
	Total No.of projects	Investment Capital	Total No.of projects	Investment Capital	Total No.of projects	Investment Capital	Total No.of projects	Investment Capital
Tigray	349	11,112	7	130	17	580	0.2	0.5
Afar	26	399	50	190	89	1,174	1.3	1.0
Amhara	722	32,753	612	38,642	829	10,469	11.8	9.3
Oromia	1,386	32,219	510	25,714	846	49,111	12.1	43.8
Somalia	127	2,738	50	1,001	4	24	0.1	0.0
Benshangul gumuz	56	81,611	50	354	33	114	0.5	0.1
SNNP	160	49,751	49	2,845	125	3,140	1.8	2.8
Gambella	14	3,920	11	6,265	4	163	0.1	0.1
Harari	48	276	4	974	1	10	0.0	0.0
Addis Ababa	3,221	30,627	4,170	62,264	4,890	36,160	69.7	32.3
Diredawa	207	2,995	134	660	170	1,730	2.4	1.5
Multi regional	6	1,067	2	7,129	3	9,397	0.0	8.4
Grand total	6,322	249,469	5,649.0	146,168	7,011	112,072	100.0	100.0

Source: Ethiopian Investment Agency

2.2. Micro and Small-Scale Enterprises

The five-year Growth and Transformation Plan envisages creating a total of three million employment opportunities at the end of the Plan period. This sector development is believed to be the major source of employment and income generation for a wider group of the society in general and urban youth in particular. According to the Federal Micro and Small Scale Enterprise Development Agency (FeMESDA), a total of 77,415 new MSEs were established during the fiscal year 2012/13 which employed 1,223,679 peoples. The number of establishment has grown by 10 percent and total employment has grown by 51.8 percent, compared to a year ago. The total amount of loan received from micro finance institutions was more than Birr 2.7 billion under the review period, 150 percent higher than last fiscal year which shows higher credit deepness per MSEs. In terms of regional distribution of new MSE's established Amhara region took the leading share (38.6 percent) followed by Oromia (21.8 percent), Tigray (17.6 percent) and Addis Ababa (9.8 percent). However Oromia constituted about half of the

employment created during the review period (48.7 percent) followed by Addis Ababa (17.9 percent), Amhara (12.5 percent) and Tigray (10.8 percent) Meanwhile, regarding the amount of credit placed to each region Amhara region took 35.9 percent of the credit distributed to the sector followed by Addis Ababa (29.7 percent), Tigray (17 percent) and Oromia (11.5 percent).

2.3. Manufacturing in Ethiopia an Empirical Evidence

Manufacturing is under-developed in Ethiopia even by African standards. Several mutually reinforcing factors have conspired to prevent the emergence of a stronger manufacturing base in the country historically, including a history of isolation from global markets. Ethiopia has had limited success in a few narrow areas, such as leather and textiles. (Henok , Assefa, Benien and Suriak, 2012). However, Ethiopia has the means to change that as a number of factors are coming together at the same time: Among the constraints Ethiopia has a surging supply of young, increasingly well-educated, trainable and inexpensive labor, Ethiopia has an advantageous geographic position to access global value chains: Addis Ababa is already the air cargo hub of Africa, within non-stop reach of all the major G7 and BRICSA economies. Moreover, with new high-speed road and rail corridors being built to connect Ethiopia to the Red Sea, the sense of landlocked isolation that has historically characterized Ethiopia will be transformed Ethiopia will be seen as perched on the main trade route from Asia to Europe and the Americas. Ethiopia is implementing what will amount to a quantum improvement in trade logistics: its new industrial parks will give their tenants, as authorized economic operators, seamless multimodal links to the global economy. With duty-free, quota-free access to the US and EU markets already in hand, Ethiopia's manufacturing sector is well positioned to absorb some of the basic manufacturing jobs being shed in East Asia due to rising labor costs in that region. The supply of energy in Ethiopia is being expanded in quantum leaps through major new infrastructure developments. Ethiopia has no hangover of legacy manufacturing technology.

Finally Ethiopia has a supportive policy framework aimed at leveraging the agricultural and mineral resource base which will provide the feedstock for downstream manufacturing activity. The inflow of foreign direct investment is now being encouraged by the experience of first movers who have entered the Ethiopian market with success. According to Dinh et al (2012), Ethiopia has significant potential in several light manufacturing subsectors: apparel, leather

products, agribusiness, wood products, and metal products. With policy reforms that have already been proven in application in other countries, Ethiopia's export potential could be expanded by orders of magnitude. Ethiopia's advantages lie in the combination of natural resources that serve as inputs for light manufacturing industries (e.g., cattle for the leather industry, forests for the furniture industry, cotton for the garment industry and a large agricultural base for the agro-processing industry), abundant low-cost labor, which gives it a comparative advantage in less-skilled, labor-intensive light manufacturing, and cheap hydroelectric power.

2.3.1. Apparel production in Ethiopia

In Ethiopia, the main constraints are poor trade logistics and access to trade finance. Proven solutions are a green channel for apparel at customs, providing free and immediate access to foreign exchange, reducing the cost of letters of credit, and setting up an industrial zone close to the main port of export (Djibouti). Competitiveness could be reinforced by developing textiles industry based on its high-quality cotton and cheap hydro-energy. Potential impact while Ethiopia's apparel sector currently generates only about USD 8 million in exports and 9,000 jobs, Vietnam has with policies similar to those recommended above achieved USD 8 billion in exports and created 1 million jobs. (Henok, Benien and Suriak, 2012).

2.3.2. Leather production in Ethiopia

Ethiopian leather is highly regarded. With modest, targeted reforms Ethiopia's large animal herds could produce vast amounts of some of the best leather in the world to feed downstream leather products industries. The immediate binding constraints on input supply, which constitute the main constraint, could be lifted by allowing the import of processed leather, while straightforward reforms to cattle herding practices and allowing the export of raw hides would stimulate investment in hide production, providing a longer-term solution to the input problem. Potential impact: With similar policies, Vietnam, which has a similar sized population to Ethiopia's, created 600,000 jobs in the leather products industry.

2.3.3. Agribusiness in Ethiopia

Ethiopia's coffee and cut flower successes demonstrate the potential for agribusiness based on low wages, varied soil and climatic conditions, opportunities to increase yields on cultivated land, and large tracts of unused arable land. The main constraints are identified as high input prices. The relevant reforms are to improve the supply and reduce the cost of agricultural inputs, including by facilitating investment (e.g., removing trade restrictions and allowing use of cattle as collateral). Potential impact: The World Bank observes that Ethiopia has the second largest dairy herd in Africa, offering the potential for large-scale downstream processing.

2.3.4. Wood and metal production in Ethiopia

Ethiopian wood and metal products manufacturers rely on expensive imports of wood and steel, made more expensive by high tariffs and poor trade logistics. The sector is dominated by smaller, mostly informal, firms with no large or exporting firms. For wood the government should facilitate access to rural land and financing for private wood plantations. For metals the cost of inputs could be reduced by cutting the 10 percent import tariff on steel and exploiting Ethiopia's proven reserves of iron ore. For both subsectors the government could support the most deserving enterprises by facilitating their access to skills, finance, and industrial land as part of "plug-and-play" industrial parks. The potential lies not in exports (at least initially) but in the growing domestic market given the high weight-to-value ratio of finished wood and metal imports. Ethiopia's manufacturing can benefit from the same advantages in many other sectors that feature processing trade. For example, several multinational firms are already assembling cell phones in Ethiopia for the local and regional market. In that sense, in Ethiopia's case, the past is not necessarily going to be prologue to the future.

The Ethiopia Business Landscape 2012 provides examples of the impact of effective trade facilitation for firms that operate export processing manufacturing in Ethiopia. For example, Ayka, a Turkish leather products manufacturer, imports production inputs from Djibouti. Ethiopia Shipping Lines takes the sealed containers from ship onto truck and straight to Ayka's premises. They are unsealed in the presence of a customs official and go straight into production. From dockside to factory, this process takes 2-3 days at present. The major current bottleneck, slow, sometimes uncertain, and costly trucking from Djibouti, will be relieved in the near future with the completion of the new rail link to Djibouti. According to Ethiopian Shipping Lines and companies, time will be cut to hours, uncertainty eliminated and cost sharply reduced. The roll-

out of the Authorized Economic Operator concept across the growing number of export-orient industry parks is thus building on established practice. However, while the actual business operating environment is much less problematic than the pro forma accounts recorded in the World Bank's *Doing Business* surveys (a point confirmed by the World Bank's Enterprise Surveys, as reported by Hallward-Dreimeier and Pritchett, 2011), for many firms' problems remain. To offset the frictions that firms may experience while the full package of reforms are still being implemented, the Government of Ethiopia offers attractive terms to foreign investors, as described earlier in the macroeconomic scan.

2.4. Ethiopia's Investment Environment

2.4.1 Macroeconomic Scan

Ethiopia has been one of the fastest-growing countries world-wide since 2003. The growth momentum is expected to be sustained in 2012 and 2013, although at a slower pace in the 7% range. Excluding oil and gas exporters, only China has outpaced Ethiopia in the last eight years. Although forecast growth is well below the ambitious growth projections under the Growth and Transformation Plan (GTP) of between 11.2% and 14.9%, it still places Ethiopia among Africa's and the world's growth leaders over the medium term. Headline inflation has been strongly affected by volatility in food prices, much of it reflecting international price developments and the exchange rate adjustment. Non-food-price inflation has been steady but relatively high at approx. 20%. While the temporary surge in head line inflation in 2011-2012 was worrisome, inflationary pressures have since eased as the effects of some of the shocks that had contributed to the surge including the rise in import prices following the currency devaluation in September 2010, steep international commodity price increases, and drought have run their course. IMF analysis suggests that Ethiopia is in a position, given appropriate monetary policies (in particular increases in interest rates), to restore a reasonable measure of macroeconomic stability (IMF, 2012a). A restoration of positive real interest rates would also activate the Treasury bill market which would facilitate monetary policy management and mobilize domestic savings which in turn would provide the basis for the investment required to maintain the pace of development. Inflation declined over the course of 2012, and the most recent IMF projections (IMF, 2012) suggest the measures taken will result in inflation being contained to single digits over the medium-term horizon. After appreciating steeply during much of the

past decade, Ethiopia's real exchange rate temporarily returned to more competitive levels due to a series of nominal exchange rate adjustments in 2009 and 2010, but this trend reversed in 2012, therefore calling for renewed policy attention.

Ethiopia's international trade has grown rapidly over the past decade. Until 2008, import growth was especially strong, reflecting not only Ethiopia's rapid industrialization but also the real exchange rate appreciation. Export growth picked up strongly in 2010 and 2011 following the real exchange rate adjustment, which has resulted in a stabilization of the trade deficit, although there was a significant slowdown in the final quarter of 2011, which the National Bank of Ethiopia attributed to both reductions in volumes of major export products and the pace of international prices of the export products.

2.4.2. Policy Framework

Ethiopia's economic policy framework is set out in the Growth and Transformation Plan (Ministry of Finance and Economic Development, 2010). This plan involves government stepping in where there are apparent market failures (e.g., trade logistics), the identification of strategic sectors to drive economic growth (textiles, leather, agro-processing, and mining), and an ambitious program of economic infrastructure development (transport, energy, telecommunications), together with the continuing drive to meet the socioeconomic Millennium Development Goals by 2015, and to achieve middle-income status for Ethiopia by 2020–23. Framed in terms of the developmental state model of industrial policy, the Plan applies all the tools of traditional industrial policy. Targeted financial support, such as subsidies, loans from domestic policy banks, and equity participation, including setting up public corporations or, where necessary to address a market failure, nationalization of firms or even industries (as it recently did with the trade logistics industry which was folded into Ethiopian Shipping Lines);

trade policies that favor export-oriented and import-substituting industries; tax incentives, including import duty exemptions, tax holidays, etc. that promote priority sectors, particularly where these sectors face particular handicaps such as the currently inadequate trade logistics. Strategic government procurement (e.g., assured profit margins for domestic pharmaceutical manufacturers in government health-care procurement). Investment in specific supporting economic infrastructure, and/or regulatory exemptions to attract, preserve or foster the growth of

particular industries, including by attracting foreign direct investment. The scale of public involvement is large: for the five-year GTP period, the sum of budgetary government spending and off-budget spending by public enterprises is programmed to reach ETB 1.26 trillion or an average of 41% of GDP, disproportionately weighted to capital spending.

As regards policy delivery, overall governance is comparable to African peers – Ethiopia is in the middle of the pack on most indicators, with the strongest suit being government effectiveness, an area where there has been marked improvement since 2000.

The 2013 edition of the World Bank’s doing Business ranks Ethiopia 127 out of 185 economies in terms of overall “Ease of Doing Business”. This is roughly in line with the average score of regional peers. Ethiopia’s relatively low rank is mainly the result of low scores in three sub-indices: **“getting credit”**, **“trading across borders”**, and **“protecting investors”**. The first of these indicators is of limited importance to foreign investors, which rarely source funding on the destination country’s capital market. With regard to the facilitation of trade across borders, Ethiopia’s low score is confirmed by the World Bank’s Logistics Performance Index (LPI), which measures on-the-ground trade logistics performance. Down from number 123 in 2010. However, as discussed in the introduction, major initiatives are currently under way to improve trade logistics. These include: new high-speed rail and multi-lane highway connections to the main port of Djibouti and improved border connections to neighboring countries; reforms to shipping logistics through the consolidation of the management of Ethiopian Shipping Lines, logistics operators and interior dry ports; and the establishment of new industrial parks for export production in which all firms will benefit from the Authorized Economic Operator (AEO) procedures for dealing with import and export processes. With regard to protection of investors, Ethiopia provides an attractive policy regime for foreign investment in terms of protection of investments and repatriation of profits: The Constitution and the Investment Law protect private property and assure the repatriation of capital and profit.

No restrictions are made on the modality of participation, nor does Ethiopia discriminate between domestic and foreign investors. Investments can also benefit from guarantees from the Multilateral Investment Guarantee Agency (MIGA), and from measures in Ethiopia’s Bilateral. There is also a comprehensive set of incentives, particularly for investors in priority sectors. Exemption from the payment of customs duty on capital goods and construction materials and on

spare parts whose value is not greater than 15% of the total value of the imported capital goods. In Ethiopia the investment incentives were in practice since two decades. For instance, Income tax exemption from two up to seven years for manufacturing or agro-processing and agricultural investments, Carry forward of losses half of the tax holiday period. Moreover, several export incentive schemes, such as a Duty Draw-Back scheme, a Voucher scheme, a Bonded Manufacturing Warehouse scheme, and an Export Credit Guarantee scheme. Finally, the process for approval of investments has been expedited recently passed legislation will make a reality of the promise of one-stop shopping for investment approvals. Together with pre-approval and post-approval services to foreign investors (facilitation & aftercare services), foreign investors can expect to obtain the necessary approvals within a few hours (EIA, 2012).

2.5. Ethiopia's Global Integration: Trade and Investment Trends

In terms of geographical trade patterns, while China and India have been the most important sources of Ethiopian imports, China has also become Ethiopia's most important foreign market in recent times. At the same time, exports reflect Ethiopia's global position at the cross-roads between the East and the West. It is telling, therefore, that the three most important destinations of Ethiopia's exports are China (east), Germany (west), and Somalia (region). This pattern of export markets ensures that Ethiopian exports are not vulnerable to business cycles in any one of the global regions. The stock of inward FDI in Ethiopia has grown steeply in the past decade, although the rate of accumulation has slowed since the onset of the global crisis in 2008. The level in 2011 was almost five times the level in 2000.

2.6. Reasons to Invest in Ethiopia

To attract potential investors from the abroad or from the domestic market there may be a number of reasons but this may depend on the effects of economic, social, political, or other factors in the host country. In Ethiopia some of the important factors make the investment sector conducive for investors was presented by EIA and witnessed by different people in the country will be discussed in short below in the following paragraphs.

2.6.1. Stable Economic Environment

Ethiopia has been able to achieve macro-economic stability and Stable annual economic growth in double digits since 2003. Stable exchange rate, Government commitment to private sector,

Safe and secure working and living environments, identified by the U.N. and the International Chamber of Commerce (ICC) as key assets for investors in Ethiopia. Absence of corruption - Ethiopia is described by the U.N. and ICC as “exceptional in its almost complete absence of routine corruption.”

2. 6.2.Liberalized Economy

All major economic sectors are liberalized for investment and marketing, Remittance out of Ethiopia from invested capital (dividends and interest) is permitted. Remittance also permitted for principal and interest payment on external loans, payments associated with technology transfer, proceeds from sales or liquidation of an enterprise, salaries and other payments, 100% foreign ownership of investment is permitted. \$100,000 minimum initial investment required from foreign investors to start a business, reducing to \$60,000 where the foreign investor is in a joint venture with a domestic partner (\$50,000 for consultancy or publishing business). This figure reduces to \$25,000 (in cash or in kind) for foreign investors working in partnership with a domestic investor in the areas of engineering, accountancy, architecture, auditing services or business/management consultancy.

2.6.3. Security of Investment

Government guarantees (Investment Code, 1991) and constitutional protection from expropriation, Ethiopia is a signatory to the main international investment related institutions, for example, it is a Member of the Multilateral Investment Guarantee Agency (MIGA) Ethiopia is also a signatory of the Convention on the Settlement of Investment Disputes between States and nationals of Other States.

2.6.4. Significant Tax Incentives

Customs Import Duty - 100% exemption on all import of investment capital goods (plant machinery, construction materials, etc.) including spare parts worth up to 15% of the imported investment capital goods; plus exemption for import of raw materials needed for the production of export goods. Export Customs Duty - Products and services developed in Ethiopia are exempt from export tax.

2.6.5.Conducive tax environment

Corporate income tax (tax on profit) is 30% Excise tax is levied (minimum 10%) on selected local or imported products. Turnover tax at 2% for priority sectors such as tractors, combine harvesting, grain mill etc. and 10% on other sectors, Customs duty on unexempted imports ranges from 0 to 35%. Income tax ranges from 10 to 35% on monthly income of \$16.50 and above, Withholding tax is payable on imports at 3% of cost, insurance and freight, 15% VAT is payable on businesses with a turnover above \$54,000. Dividend tax (on income derived from dividends from a share company or withdrawals of profits from a private limited company) at 10%, Royalty tax (on income derived from technology and intellectual property rights) at 5%, Capital gains tax - share of companies 30%; business, factory or office buildings 15%; residences 0%, Rental income tax (on annual rental income) between 0 and 35% dependent on level of rental income, Stamp duty - Leasing 0.5% of value; registering title to property 2% of value; contract of employment 1% salary; bonds 1% of value, etc. Tax treaties to avoid double tax payment are signed with several countries, along with bilateral treaties for the protection and promotion of investments.

2.6.6. Investment Opportunities in Ethiopia

In Ethiopia there are different investment opportunities which were given more priority. All investment areas may not be successful without considering the important factors significantly affect the growth of the investment sector of the country. The government of Ethiopia clearly specifies the areas of investment those are conducive to both foreign and domestic investors. Foreign investors are given more priority by establishing different incentives for potential investors who were capable of investing their money in different areas. All the areas were based on careful study and analysis done by different agencies, specifically by EIA and NBE. These areas were discussed below based on the data gathered from different sources.

2.6.6.1. Agriculture and Agro-processing

Ethiopia is the country which is rich in fertile land conducive to agriculture and agro-processing products. Private investors are more invited for such investment opportunities. Cash crops, flowers, fruits and vegetables are the important areas given priority.

New private investment is sought in the production and processing of agricultural crops such as coffee (the country's single most important cash crop), tea, sugar, flowers, fruits and vegetables, teff, wheat, maize, beans, peas, lentils, soybeans, chickpeas, starch production, oil crops such as

rapeseed, linseed, groundnuts, sunflower, sesame, maize, Niger seed and cotton seed, as well as investment opportunities for introducing modern commercial livestock breeding and processing into the largest livestock population in Africa (cattle, sheep and goats), plus significant fresh water fishery and livestock resources. Investment is also required in the provision of agricultural support services such as pest and disease control, agricultural machinery, cold storage, etc. A number of crops are grown organically.

2.6.6.2. Textiles leather and Hide

There were a higher Opportunities for production and processing of cotton in Ethiopia, as well as producing and finishing textile fabrics and garment production. There were also Leather and Hide - Opportunities for investment in tanning up to finishing, manufacture of luggage items, handbags, saddler and harness items, footwear, garment and other leather goods.

2.6.6.3. Horticulture/cut flowers

For investors who wish to invest on Fruit, vegetable and cut flowers these are fast-growing export businesses, with great potential for private investment. There are already some integrated agro-industrial processing plants.

2.6.6.4 Building Materials

The construction sector in Ethiopia is showing growth from time to time and it results with the higher demand in construction or building materials. This rapid growth in the construction of road, buildings, air ports, railways ...etc can need different construction inputs those helps in facilitating the smooth functioning of the sector. If these materials are produced in the country it has dual purposes; firstly, it can save the foreign hard currency that can be paid in importing such products from the abroad, secondly; it can receive foreign currencies if it can be exported to foreign markets. Moreover, it may help in creating employment opportunities for local community. The important products produced for this purpose may include cement, marble, granite, limestone, ceramics, and other similar products.

2.6.6.5. Tourism Sector

In Ethiopia the growth of tourism sector was not showed a significant growth as compared to other sectors. When we see the potential of the country it has a diversified and untapped tourism potential in eastern and sub-Saharan Africa. The untapped tourism potential, particularly investment opportunities in hotels, lodges and international restaurants waiting investors in different areas of the country were the most attractive tourism investment areas.

2.6.7. Strong Market with Excellent Market

In Ethiopia there was Strong internal market with second largest population in Sub-Saharan Africa at 100 million (in 2017), Located in the Horn of Africa at the crossroads between Africa, the Middle East and Asia, within easy reach of the major ports of the Horn. The membership of the Common Market for Eastern and Southern Africa (COMESA) embracing 23 countries with a population more than 300 million. Ethiopia enjoys the benefits of preferential tariff rates on exports to these countries. Ethiopia is an ACP member (African, Caribbean and Pacific Group) and accession to the WTO is under negotiation. Duty and quota free access into the U.S. (AGOA) and EU (EBA) markets. Export products from Ethiopia to the EU market are entitled to duty reductions or exemptions and are free from all quota restrictions under the terms of the Lome Convention. The trade preference accorded Ethiopia includes duty free entry of all industrial manufactured products. Under the generalized system of preferences (GSP), a wide range of Ethiopia's manufactured products are entitled to preferential duty treatment in the United States, Canada, Japan and most EU countries. The large and fast growing domestic market offers good prospects for investment in and the development of consumer goods industries such as food, beverages, tobacco, plastic products, soap and detergents, drugs and pharmaceuticals, paper and paper products and electrical and electronic.

2.6.8. Strong Natural Resource Base

When the country (Ethiopia) has been seen in natural resource base it is rich in good rainfall, rich soils, and favorable temperature ranges. The Climate as identified by the U.N. and ICC as “exceptional” offering “an excellent environment for various agricultural activities.” The nation is highly rich in unexploited mineral deposits, specifically gold, tantalum, platinum; nickel, potash and soda ash are some of the many. In current policy and strategy of the country there is

urban and rural land available on a leasehold basis. Lease rights over land can be transferred, mortgaged or sub-leased together with on-build facilities. Leaseholders have the right to use urban land for up to 60 years in Addis Ababa and up to 80 years in other smaller towns, with leasehold renewal permitted (generally the range in the country is between 50-99 years depending on purpose and location).

2.6.9. Trainable Labor

The labor force is becoming the most important resource helpful for the growth of every nation. It is among the factors of production important for the enhancement of investment. Ethiopia presently turns out more than 100,000 university graduates per year, including business, management, economics, accounting, law and engineering graduates. There were 151 technical and vocational education and training schools in Ethiopia. The number of Private universities and colleges were flourishing in Addis and regional cities. The average private sector wage is about \$25 per month, with graduate salaries ranging from approximately \$85 to \$105. Expatriate employees permitted in senior positions with prior consent from the Ethiopian Investment Commission (where employer is sole or major owner or shareholder of enterprise). Expatriate experts are also permitted, as long as the investor trains his/her replacement within a designated time period.

2.6.10. Good Infrastructure Standards

The infrastructure of the country as a physical factor can highly affect the smooth functioning of investment sector and other sectors important for the growth of the economy of the nation. Among these road, airports, railways and other may be the important ones.

The country was established three international and 18 domestic airports, with international flight links to over 45 cities on four continents (12 in Africa, 12 in Asia, five in Europe and two in North America), and domestic links to 26 destinations. The national and international Ethiopian Airlines has an outstanding safety record and modern fleet. Modern air cargo terminal and maintenance has in progress in Addis soon to be completed.

In Ethiopia, investment in road infrastructure has given a high priority, with an expanding road network and international highways linking Ethiopia with its neighbors. The construction of

railways and Ports 500 mile rail service linking Addis to the port of Djibouti (on the Red Sea coast) via the eastern cities of Dire Dawa and Nazareth. Ethiopia also has access to Berbera in the East and Mombassa in the south. Microwave links connect all regional cities and a number of smaller towns have automatic telephone services. International communications links are maintained through two satellite earth stations, providing telephone, internet, telex, fax and TV services. Microwave links exist with Kenya, Djibouti and the Sudan. Ethiopia has vast hydropower and promising geothermal energy resources, with nine hydroelectric power plants. To date, the aggregate electricity generated is less than 2% of the potential, and developing this area is a Government focus. The main industrial towns are all connected to the national grid, and electricity is relatively cheap. The Government has liberalized the sector, allowing foreign investors to participate in generating electric power by setting up hydroelectric power plants, although national grid transmission and distribution remains with the state-owned Ethiopian ElectricPower Corporation.

The above infrastructure elements are the most important ones in facilitating the growth of the investment sector in the country. Road as the means for transporting goods and services from different areas, say from the rural to the urban divide. Communication, specially the telecommunication also hinders the growth of the investment sector, in rural areas, even in the urban there is a greater problem in failures of connection and network. The air transportation including cargos also contributes for the facilitation of both private and public investment sector. The most dangerous and serious problem that hinders the investment sector is the electric power. There was a greater power fluctuation seen in the country, but there will be a hope expected from the power generated from the renaissance dam of the country.

2.7. Success stories of Investing in Ethiopia

Practice makes perfect as many believed on, stories may be important to initiate others to do so, different countries or companies can gain the experience of successful companies. When companies are capable of sharing the practice of successful companies it makes them perfectly successful. Below we will discuss some of the important stories of successful companies conducting their business in Ethiopia.

In the words of Richard Ponsford (managing director Unilever Ethiopia) "Many companies have had successful experiences in Ethiopia, after making the decision to invest. "Unilever returned to Ethiopia in 2000 after a longish hiatus, having decided that we would capture a larger share of the local market by being on shore and building a manufacturing base than by staying off shore and relying on imports. As they concluded "The changes we have seen in the last couple of years, in such things as the speed of approval by the EIC, tell us that we made the right decision. The size of the population alone gives Ethiopia market potential but it is the changes in the business climate that suggest that the potential might actually be realized."

Chief Executive Officer of MIDROC Ethiopia Arega Yirdaw, witnessed that "MIDROC Ethiopia is proud to be the largest foreign investor in Ethiopia a country with a huge and trainable workforce, a wonderful climate and almost no corruption. The current political environment is also very hospitable to investors. Once the world knows that there is untapped investment potential, as well as continuous improvement in incentives and governance, we are bound to see more DFI in this beautiful country. MIDROC would certainly welcome it." Chris De Muynck, Managing Director, MOENCO S.C. stated the following about success factors in Ethiopia; "When we decided to come to Ethiopia in 1998, it was because of its natural advantages – in particular its climate, which was ideal for growing roses. We are delighted that now, in 2004, the natural advantages are beginning to be matched by man-made ones, those deriving from improvements in policies and procedures. If these improvements can be sustained, there is almost no limit to investment opportunities in Ethiopia." (Ryaz Shamji, General Manager, Golden Rose Agro-farms Limited). "During my two years in Ethiopia, I have seen great progress towards good governance and economic liberalization. Although a lot remains to be done, the path is now set. And all this has been done during a severe drought, which absorbed a tremendous amount of energy and resources. Even though purchasing power is still very low, our principals believe strongly in the future potential of this huge market of 70 million."

Moreover "Worku Zewde, Managing Director, Garment Express Private Limited expressed his feeling with the following statements "We believe that this is exactly the time to invest in the garment business in Ethiopia. Not only are labor costs low and the workforce trainable, access to major markets like the U.S. and the EU is available on preferential terms. What's more, the investment climate has improved notably in the past year or so. Our own recent experience has

been positive enough to lead us to expand our garment business (tripling employment) and setting up a related dyeing and knitting venture with two other foreign investors.

2.8. Considerations for International Finance Support

There are some important Specific considerations for international public finance insupport of private sector investment for countries those are expected to get public financing services from lending finance agencies or countries. These considerations are depending on the goal and the criteria established by the lending institutions or countries, the diplomatic relationship, or the type of the loan and other factors. For instance, there may be a loan guaranteed for the control and prevention of HIV, women support or empowerment, poverty alleviation and others. So, each and every lending agencies vest specific considerations for the borrowing countries to support their public expenditures including public and private investment. There may be bilateral or multi- lateral agreement between countries related with such issues.

In using scarce international public financial resources to support private investment, appropriate criteria for assessing alternative uses of public funds have to be found. This is all the more important as past practices in blended financing have aroused a number of concerns.

2.9. Approaches to blended Finance for Private Investment

Private investment by itself has its own rationale like public investment of every country to be conductively enhancing the development of the nation. The government of the country either local or national can catalyze to establish the alignment of private investment and the government policy. The government helps the private sector investment by financing it. In Ethiopia there was an agency facilitating the activities of both private and public investment, namely Ethiopian Investment Agency (EIA), Federal Economy and finance, and to some extent NBE. In addition to generating profit, as a secondary objective it can work for CSR, thinking for the community or the whole public as their main goals. Private investors should try to work for poverty reduction, infrastructure development, and other philanthropic activities.

In many sectors, there may be strong rationales for national or local governments to catalyze and try to better align private investment with poverty reduction and sustainable development

objectives. As global ODA stagnates, several aid agencies have suggested a dramatic scaling up of public finance devoted to supporting private sector investments (Kwakkenbos, 2012). Policymakers have been exploring a broad spectrum of public instruments to foster private investment (Glemarec et al., 2011). The common objective of these instruments is to create conditions for attractive investment risk/reward profiles, adapted to different types of investors, either through reducing risks (and hence lowering the weighted average cost of capital demanded for these investments) or increasing rewards (through premium prices, tax credits, etc.). This is achieved through two actions: first, by reducing the risk of the activity, for example through a regulatory policy such as guaranteed access to the grid for independent power producers (IPPs); and, second, by increasing the return on investment through financial incentives such as a price premium for renewable energy.

The challenge is to use public resources in the most efficient way, by leveraging private resources and expanding the profitability domain where private finance is willing to operate. Essentially three broad types of intervention are available to governments in this respect: (i) establishing a policy environment that addresses legal, regulatory and other practical barriers to investment to reduce investment risks in given sectors (often called “investment-grade policy infrastructure”); (ii) interventions aimed at deepening financial intermediation in order to facilitate access to finance by private investors; (iii) investing directly (co-investment), aiming to leverage private sector investment. The main types of interventions at the disposal of national governments are also available to the international community. Compared to the national level, international institutions benefit from access to low-interest finance, made possible by explicit or implicit sovereign backing. International development institutions also have an often considerable capacity as knowledge brokers and providers of technical assistance, capacity building, in particular for support to regulatory reforms and pilot projects.

The three main approaches to blended finance are mutually supportive. Capacity of the international community to use both grant and low-interest capital can simultaneously increase access to, and reduced cost of, financing through both reduced risk and increase rewards.

2.9.1. Upgrading the policy environment

Public authorities are responsible for establishing the legal infrastructure and ensuring a predictable business environment to support investment. Broadly speaking, investment risk can be reduced by the public sector in three ways: by mitigating risk; by transferring risk; or by compensating for risk. Together, these activities are referred to in the investment literature as reducing risk or “derisking”. Policy derisking instruments address and attempt to remove the underlying barriers that are the root causes of risks (quality policy design to reduce the risk of policy reversal, streamlining of licensing processes, etc.). Financial derisking instruments do not seek to directly address the underlying barrier but, instead, function by transferring the risks that investors face to public actors, such as the government or development banks. These instruments can include development banks loans and guarantees, political risk insurance and public equity co-investments. Recognizing that all risks cannot be eliminated through policy derisking or transferred through financial derisking, efforts to reduce risks might need to be complemented by a third group of public instruments, direct financial incentives, to compensate for any residual risks and costs. These incentives can take a number of different forms including price premiums, tax breaks, such as production tax credits, and proceeds from carbon offsets.

2.9.2. Deepening Local Financial Intermediation

While establishing an adequate policy environment is critical to mobilize private finance, capital market conditions are also important determinants of the conditions under which private sector investment operates. At the risk of simplifying, least developed and low-income countries tend to have weakly developed financial markets and capital markets, as well as low capacity in financial sectors. The situation in middle-income countries is variable, with often limited development of local capital markets (with lack of long-term financial products in local currency being a critical hurdle), sometimes in combination with abundance of liquidity in the banking system but underdeveloped financial intermediation and missing lending business lines.

The degree to which countries are able to influence the allocation of lending to the private sector varies. Some countries have relied on directed credit to achieve public policy goals. For example, while the outstanding growth of clean energy technologies in China has been fueled by the strength of its capital markets, the return on many of China’s investment at home has been below their costs of capital (McKinsey, 2013). Thus, the inflow of investment into renewable is at least in part the product of directed investment by the government through public banks. While this

undoubtedly has benefited renewable energy and other capital intensive industries, this model may not be easily transposable to other countries where market returns are expected.

Many countries have relied on public or quasi-public institutions to lend directly to project proponents in specific sectors. Those institutions are usually at the service of national economic development strategies and industrial policies, thus channeling support to economic sectors and companies that are considered of strategic importance. To do so, they rely on other sources of finance or capital e.g. (sovereign funds, pension funds), that can be more easily mobilized than private resources to cater to un-served or underserved sectors or subsectors. Notably, some developed countries have deeply rooted special financing circuits aiming to lend funds on favorable terms to municipalities and local governments as well as certain sectors (e.g. public social housing). Development banks in developing countries have also played an important role in past decades.

2.9.3. Co-investment aiming to leverage private sector investment

While the private sector is at the origin of most of global investment, some of it is directly or indirectly supported by public sector resources from national governments, national development banks, bilateral and multilateral financing institutions, through various instruments. The idea of “blending” resources by combining grants and concessional finance (e.g. loans) with market finance to finance development projects or programmes is not new. It has a long tradition in bilateral and multilateral development finance (Núñez Ferrar and Behrens, 2011). The two most commonly stated objectives that blended finance is supposed to fulfill are: (1) to increase the leverage of public resources and in particular official development aid (ODA), by mobilizing additional co-financing by the private sector for development projects; and (2) to finance global public goods.

Donor governments and multilateral institutions have provided grants and loans to private companies operating in developing countries for decades. However, since the 1990s the scale of this support has increased dramatically. In 2010 external investments to the private sector by international financing institutions (IFIs) exceeded \$40 billion (IFC, 2011). By some estimates, by 2015, the amount flowing to the private sector could exceed \$100 billion – making up almost one third of external public finance to developing countries. These interventions often do not deal

with final clients. Rather, they tend to use the existing networks of financial institutions, which retain the responsibility of evaluating the risks, selecting projects, and managing project portfolios. For example, guarantees may be offered in the form of portfolio guarantees. In 2010, on average over 50% of public finance flowing from bilateral financing institutions to the private sector went to the financial sector. In 2010 lending and investments in the financial sector by bilateral and multilateral financing institutions had increased, on average, more than two fold compared to pre-crisis levels. (Kwakkenbos, 2012). Among financial intermediaries, commercial banks are by far the largest recipients of funds, although private equity funds are quickly becoming a favored vehicle. (Kwakkenbos, 2011). This direct support to the financial sector is taking place in the broader context of rethinking the role of public private partnerships to catalyze private investment. As recently as the 1990s, the emphasis of institutional reform in the context of development was on sector restructuring and private participation or “public-private partnerships”. This approach was advocated by international financing institutions across a wide array of sectors. In some regions, private sector participation has increased dramatically over the last decade. For example, according to a 2009 World Bank report, private finance to African infrastructure increased from very low levels to provide a flow of funds comparable in magnitude to traditional ODA to that sector (Foster, 2009). This type of PPPs has yielded often positive results in the telecommunications sector, but elsewhere the benefits were often limited and showed great variability across countries, with many instances of problematic situations. A more nuanced, less academic, view of the comparative advantages of optimal relationships between the private and public sectors has subsequently emerged, which values the significant private financing contribution that can be made in certain key areas (mobile telephony, power generation, ports) while recognizing its limitations in others (roads, power and water distribution). The concept of private sector participation has evolved, with greater emphasis put on the role of national firms (as opposed to international firms), and increasing exploration of hybrid models that experiment with different ways of allocating responsibilities between public and private sector partners.

When we summarize the empirical and theoretical part of chapter two there are important models and experiences of different companies or principles, rules, regulations, and issues regarding private and public investment, as well as the factors those are expected to predict the private investment of the nation. Economic, political, and social factors are addressed in the literature.

The linkage between the public and private investment was discussed and conclusions were drawn up. The situations of Ethiopian private and public investment are highlighted either as positive or negative element those significantly affect the investment environment as an empirical or theory.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1. Research Design and Data collection

Both primary and secondary sources of data were used for the analysis. The secondary data was obtained from such publications as Quarterly Digest of Statistics, World Tables and International Financial Statistics. The data on public and private investment was obtained from the country Finance and Investment Agency and Central Statistical Agency. The survey analysis was based on primary data collected via a questionnaire survey of 31 manufacturing firms (medium and large scale). There are certain variables (especially qualitative ones-political instability, policy uncertainty, perceptions about the economy, etc.) that may affect private investment but cannot be captured in the time series analysis (secondary data). Additionally, it was important to examine whether the conclusions of the time series analysis was consistent with firms' perceptions of the importance of those variables in affecting their investment behavior.

3.2. Sample and Sampling Procedures

The sampling technique chosen was purposive and census method. The firms were taken from Dessie, Kombolcha, Kemissie, and Haik towns. These four regions were account for massive manufacturing activities in the regionand convenient for the researcher to conduct parallel to the other academic duties. So, the sampling technique was purposive (for selecting the regions) and census (for selecting the firms).

3.3. Data Analysis

The collected data was analyzed with the use of the SPSS (statistical package for the social sciences) program. The percentage, mean, standard deviation, coefficient of variation and simple ranking was utilized for the descriptive part. The reliability and internal consistency of the data

was assessed using Cronbach's Alpha and the minimum acceptable level taken was above 70 as recommended by (Carmines and Zeller1999)

3.4. Limitations of the Study

In this study the researcher feared that there may be two main limitations. The first one is related with the problem of representation to draw inference at national level. This was be the gap for further study in a wide survey at the national level that can investigate every investor. The other pitfalls may be related with respondent's willingness and transparency to disclose accurate and relevant information and filling the questionnaire papers and returning it on time due to little concern or know-how on the benefit of such investigations.

CHAPTER FOUR

DATA ANALYSIS AND DISCUSSION

4.1. INTRODUCTION

This part of the paper deals with the analysis and description of the characteristics of the firms, presentation and analysis of the study variables and their effect on private investment. The financial, economical, and political aspects of private investment can be analyzed and discussed.

Table 4.1: Selected Economic Indicators

year	GDP growth %	BOP m's \$	C/A M's \$	Pub. INV. % of GDP	Priv. INV % of GDP	Inflation Rate (%)	FDI M's of \$	GDI % of GDP	Interest Payment % of GDP
2005/6	11.5	194	-6.3	15.4	9.0	6.8	365.1	20.5	0.6
2006/7	11.8	117	-9.1	17.1	10.7	15.1	521.2	21.2	0.5
2007/8	11.2	-261	-4.5	14.2	11.4	55.1	814.2	23.3	1.2
2008/9	10	555	-5.6	12.1	11.5	2.7	893.7	23.1	0.9
2009/10	10.6	-6,265	-4.1	14.9	8.7	3.4	956	23.6	0.4
2010/11	11.4	-5,506	-0.7	19.6	7.5	19.8	1,243	27.2	0.4
2011/12	8.5	-7,908	-6.6	26.5	8.1	34.1	1,072	34.6	0.3
2012/13	7.0	-8,500	-6.4	24.3	8.3	11.3	1,179	32.6	0.4
2013/14	7.5	-8,899	-2.849	18.8	8.4	7.0	1,399	27.2	0.4
2014/15	7.5	-9,690	-3.283	20.9	8.5	8.9	1,689	29.4	0.5

(Source: IMF, World Bank, NBE, 2005/6-2014/15 self-computation)

The table above indicates that the growth of GDP in the country for the consecutive ten years was shown decreasing at a rate of 1 to 1.5 percentages per year except that in the years of 2009/10 and 2010/11 showed an increase at 0.6 and 1 percent respectively.

When analyzing each economic indicators relative to GDP growth rate (percentage of GDP or Millions of dollar);balance of payment showed positive figures for two years in 2005/6 and 2006/7 about \$197 and \$117 respectively. The rest of the years (2007/8-2014/15) showed negative balances except the year 2008/9 balance that showed a positive figure of \$555. This was due to the trade and other balances of payment imbalances between Ethiopia and the other world and defined in terms of the differences between import and export balances and remittances from different countries from the rest of the world.

The current account balance figure was presented using the US dollar value in millions. As it was seen in the table the current account balance showed the deficit balances with higher level of variability or fluctuations of 1percent to 4 percent per year, showed highest balance in the year of 2006/7 (-9.1) and very lowest balance in the year 2010/2011(-0.7).

The other variable taken as economic indicator for the nation was foreign direct investment indicated as millions of US dollar. The data indicated that foreign direct investment increased at an increasing rate from the year 2005/6 to 2014/15. The foreign direct investment was increased about 50 million dollar to 100 dollar per year on average.

The other important economic indicators were public and private investment measured as percentage of GDP. As showed in the table above, public investment as percentage of GDP showed significant increase for the indicated years except decline in some years, (\$ 14.4 million in 2007/8, \$12.1 million in 2008/9, and \$18.8 million in 2013/14). The percentage of private investment showed an increase for four years (2005/6- 2008/9) and showed a decline for the next three years and small percentage increase with about one percent for the years between 2012/13- 2014/15. When comparing the percentage of GDP for public and private investment public invest for all the 10 years was higher for public investment than private investment.

The gross domestic invest as percentage of GDP was showed an increase through the 8 years and a decline for the rest two years.

The highest inflation was showed in the year of 2007/8 (about 55.1%) and showed higher decline for the next two years (2.7% in 2008/9, 3.4% in 2009/10).

Figure: 4.3. GDP growth rate in percentage per year

(Source:IMF, World Bank, NBE, 2005/6-2014/15)

The graph above shows the percentage growth in GDP from the year 2005/6 to 2014/15. The highest growth in GDP has been recorded in the year of 2006/7 which was about 11.8% with very low record in the year of 2012/13 with about 7%. There were small fluctuations in the growth rate of GDP with not more than 1 to 2% except the years 2010/11 and the rest succeeding years 4 years. The average growth of GDP was about 10.1% per year.

Figure: 4.4. The growth in percentage of GDP, private investment, and public investment

(Source: IMF, World Bank, NBE, 2005/6-2014/15)

The data depicted in the figure above (fig 4.3) shows the growth in GDP, private investment, and public investment. The private investment, public investment shows direct positive relationship for the years 2005/6 and 2006/7 with GDP (11.5 to 11.8% for GDP and 9 to 10.7% for private investment, and 15.4 to 17.1% for public investment) but the public investment shows anegative relationship with GDP for the succeeding years that means when public investment increased from 17.1% to 20.1% GDP and private investment decreased (from 11.8% to 7.5% for GDP and 10.7% to 8.5% for private investment).

Figure 4.4. Annual inflation rate as percentage of GDP

(Source:IMF, World Bank, NBE, 2005/6-2014/15)

The graph above (fig 4.4) shows the annual inflation rate as a percentage of GDP. The highest inflation was recorded in the year of 2007/8 which was about 55.1 percent and the lowest inflation was recorded in the year 2008/9 which was about 2.7%, this rapid improvement may be due to the remedies taken by the government to adjust the economic conditions in the country, immediately from 55.1% to 2.7% in that particular year. But after the two years of relief the highest growth in inflation was recorded which was 19.8% in 2010/11 and 34.1 in 2011/12.

Figure: 4.5. GDP and Gross Domestic Investment(percentage)

(Source:IMF, World Bank, NBE, 2005/6-2014/15)

In the figure above (fig 4.5) gross domestic product (GDP) and gross domestic investment (GDI) were depicted. The gross domestic product (GDP) and gross domestic investment have direct relationship. As seen in the figure GDP decreased from 8.5% to 7.5% GDI also decreased from 34.6% to 29.4%.

Figure: 2.6. Interest payment as a percentage of GDP

(Source:IMF, World Bank, NBE, 2005/6-2014/15)

Figure 2.7. Foreign direct investment growth in millions of US Dollar

(Source:IMF, World Bank, NBE, 2005/6-2014/15)

4.2. Characteristics of the firms

Here the time of establishment, type of product, ownership structure, legal status, and other characteristics necessarily determine the firm's nature of operation and success in the region was presented and analyzed.

Table 4.2: Firm Characteristics: Ownership structure

Variable determine firm characteristics	Frequency	%age
1.Ownership structure:		
Private Ethiopian only	30	88.00
Private foreign only	1	2.90
Private Ethiopian- foreign	-	-
State and private Eth.	3	8.83
State and private foreign	-	-
State and private Ethiopian and foreign	-	-
Total	34	100

(Source: CSA, 2015/16)

The ownership structure of the firms in South Wollo Zone shows that majority of the business was owned by private Ethiopian nationals (about 88% or 30 firms) and no businesses owned by private Ethiopian-foreign, state and private foreign, and state and private Ethiopian and foreign. About 8.83% or only 3 firms are owned by state and private Ethiopian and 2.9 % or only 1 firm was owned by private foreign. In summary, the number of medium and large manufacturing firms in the area is too small and majority of it were private and owned by Ethiopians which shows there was no foreign investment in this area.

Figure: 4.5. Firm ownership structure

(Source: CSA, 2015/16)

The figure above shows the owner structure of the firms. The majority of the firms (about 88%) of the firms are owned by private Ethiopians. The rest of the businesses are owned by state and private Ethiopians and state and private foreign investors which was about 8.8% and 2.9% respectively.

Table 4.3: Legal Status

2. Legal status:		
sole proprietorship	12	35.3
partnership	11	32.3
Family business	5	14.7
Limited liability	2	5.9
cooperative	4	11.8
Multinational corporation	-	-
Total	34	100

(Source: CSA, 2015/16)

The legal structure of the firms in the table above indicated that most of the firms legal status was sole proprietorship and partnership with more than (35 percent or 12 firms and 32 percent or 11 firms) respectively for sole proprietorship and partnership. The Family business and cooperative associations take the next rank with more than (14.7% or 5 firms and 11.8% or 4 firms respectively for family business and cooperatives. There was very small number of limited liability type of business firms only (5.9% or 2 firms) and no multinational corporation in the area.

Figure 2.5.lega status of the firms

(Source: CSA, 2015/16)

The figure above shows that 35% of the firms are owned by sole proprietorship, 32.3% are partnership businesses, 14.7% of the businesses are family businesses, the rest of the businesses legal status are limited liability and cooperative associations with 11.8% and 5.9% respectively.

Table 4.4: Product Exporting

3. product exporting		
Not exporting	31	91.17
Export directly	3	8.83
Export indirectly through traders	-	-
Export both directly and indirectly	-	-
Total	34	100
Future initiations of non- exporters to export	6	17.6
Future initiations of non- exporters not to export	25	82.4
Total	31	100

(Source: Survey, 2015/16)

The product exporting situation of the firms as indicated in the table 4.4 above most of the firms about (91% or 31 firms) were producing for domestic market but few firms about (9% or 3 firms) were exporting directly to foreign markets. The future initiations of non-exporters to export is about (17.6% or 6 firms) have initiative to export but majority, about (82% or 25) firms decided not to export due to different factors.

Table 4.5: Capacity utilization

4. Capacity utilization:		
Full capacity utilization	26	76.5
Increasing capacity utilization next year	8	23.5
Total	34	100

(Source: Survey, 2015/16)

The firms capacity utilization indicates that more than (75% or about 26 firms) currently use the full capacity and 23.5% or 8 firms were decided to increase capacity utilization next year.

Table 4.6: Business Making

5. Business making:		
Business making after tax profits		
Profits over the last 5 years rising	22	64.7
Profits over the last 5 years are the same	6	17.6
Profits over the last 5 years are declining	4	11.8
Profits over the last 5 years are not available	2	5.8
Total	34	100

(Source: Survey, 2015/16)

In the table 4.6 above, the firm's business making conditions for the last five years was showed that about (65% or 22 firm's) profits was showed an increase, about (18% or 6 firm's) profits are the same, about (12% or 4 firm's) profits are declining, and about (6% or 2 firms) were not earned profits for the last five years.

Table 4.7: Future business plan

6. Future business plan		
Producing same good, same production level, and composition	24	70.6
Maintain production level but switch to new product	4	11.8
Expand production	6	17.6
Total	34	100

(Source: Survey, 2015/16)

Table 4.7 shows about the future business plan of the firms whether to increase production capacity, switch to new product, or maintain at the current production. About 71% or 24 firms planned to produce the same good, at the same production level, and composition, about 12% or

4 firms to maintain production level but switch to new product, about 18% or 6 firms decided to expand production.

4.3. Investment Obstacles

Here, constraints facing future exporters, major and minor obstacles, uncertainty as a constraint, serious obstacles, and government attitudes and perception and investment was discussed.

Table 4.8: Constraints Facing Future Exporters

7. Constraints facing future exporters:		
	Freq	%age
Credit	30	33.33
Lack of demand	50	55.55
Cannot meet local demand	10	11.11
others	-	-
Total	90	100

(Source: Survey, 2015/16)

Figure 4.6: Constraints facing future exporters

(Source: survey 2015/16)

The constraints facing future exporters depicted in the (figure 4.6) above indicates that lack of demand for their products was the major problem about 55.55% or 50 respondents agreed, credit access to expand production and increase their capacity about (34% or 30 respondents), and about 11% or 10 respondents agreed that they can meet the local demand to produce for foreign market.

CHAPTER FIVE

SUMMARY OF MAJOR FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

5.1. SUMMARY AND CONCLUSIONS

In Ethiopia the investment sector was affected by different factors which were classified as macro-economic, political, social, and other uncertainty variables besides its success factors. The macro-economic environment consist factors which dominantly control the growth of investment in the country. The interest rate, the exchange rate, inflation, and similar variables play an important role in the growth of investment in the country. The macro-economic environment is the general or the aggregate economic situation of the nation that seriously affect the condition of the existence and expansion of investment opportunities in the country. The rate of interest payment measured as percentage of GDP showed that 0.6% in 2005/6, but this number increased to 1.2% in 2007/8. The inflation rate of the country in 2005/6 was 6.8%, but this rate was showed a significant increase in 2007/8 which was about 55% where as a significant decrease in 2008/9 which was about 2.7%. The growth of gross domestic investment measured as GDP of the country showed an increase for consecutive years except some fluctuations seen in some periods. The changes in GDI as measured in terms of GDP showed there was no exaggerated fluctuation but between the years 2010/11 there is an increase from 23% to 27%. Again in the years 2011/12 and 2012/13 there was a rapid increase which reaches about 34% and a decrease in the consecutive years of 2013/14 and 2014/15. The private investment growth as measured in terms of GDP showed a rapid increase for four consecutive years of 2005/6 to 2008/9 which was about 9% to 11.5%. This number showed a decrease and a constant move for the next years of 2009/10 to 2014/15. In this paper it is better to see if the factors analyzed above really can affect the private investment and what relationship they have in the long run. The boundary between the variables which are ready to attack the growth of private investment are too silly and not practical visible but are hidden warriors not seen but intervening variables those singing always

to attack private investment recognized as a challenging factor for investment (private investment). As the researcher observed and analyzed the conditions in which the factors may affect the smooth functioning of private investment may be considered because there are internal factors those increase the effect of the independent variables may be facilitated by the management style or the strategy they are designed to manage their business.

5.2. Recommendations

The findings of this paper and other previous studies finds out that the major obstacles and challenges for private investment sector are access to credit, interest rate, infrastructure, exchange rate, and other macroeconomic variables are among the serious factors those need considerations. More over the expansion of public investment can make the private investment out of the game, that means as the size or number of public investment expands the number or the size of private investment become out of competition as depicted in the figure 4.4 the growth go together up to some period but becoming shifting its move toward downward direction. The macro economic variables are uncertain or beyond the control of investors because this are external factors so it needs some improvements by the concerned bodies. Accordingly the researcher recommends some of the important solutions may assume to alleviate the problems in showed in the findings.

- Building strong or modern financial system to improve the problems related with credit for the investment sector, financial markets should be modernized especially secondary markets should be established and helps the private investment sector.
- The availability of infrastructure should be seriously improved; especially interruption of electricity, water supply for some of the sectors was a great problem, road, land is among the problems as seen in this study.
- Improving the problems related with foreign exchange because for the businesses those are importing inputs and other accessories from the foreign market are highly affected with exchange rate volatility and even availability of FOREX reserves making payments for the imports. Increasing the margin of exports to attract more foreign currencies especially the US dollar and other strong international currencies may be another option in addition to accumulation.

- Lack of demand for some goods was also another problem for firms those are planned to export or currently in the position of exporting, for such problems searching a new market segment internationally through invitation and promoting their products to foreigners using different mechanisms like bilateral or multi-lateral agreements which was officially established, sharing of know-how and experience of international firms in advance.
- The distribution of firms in different areas was not fairly distributed; this may affect the market segmentation and the perfect competition of the firms for a given demand in a limited access for their products, strategic building and increasing the capacity of the firms who feed each other and minimizing the costs for both buyers and the firms themselves.
- The other important factor should be lowering the rate of interest for borrowers those engaged in private investment through fair competition and increasing the financial sectors those engaged in such activity
- Increasing the interest rate to be paid for savers to encourage saving than short term advert or promotion.
- The institutional improvements should be highly conducted and the perceptions and the attitudes about the facilitation of the private sector both for new investors and the investors already engaged in the business need improvements viz; licensing, tax matters, incentives, and other legal issues should need consideration.

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