



The Case for Deeper Economic Reform in Post-election Ethiopia¹

Berhanu Abegaz

Undertaking second-generation economic reform is timely and yet difficult. Following the historic 2005 Ethiopian legislative elections, deeper reforms are timely given the bright prospects for scaled-up aid, remittances, and reallocation of domestic resources. Ethiopia's challenges, however, go beyond liberalizing repressed markets. The more difficult task involves husbanding weak markets and creating new ones. More specifically, Ethiopia must rectify three of its structural impediments: myopic politics, outmoded institutions, and many misguided policies. This paper offers a "big picture" framework for appraising competing reform agendas concerning governmental and land institutions, development strategies, and policy dialog among major stakeholders. It recommends full market development.

First-order economic principles—protection of property rights, contract enforcement, market-based competition, appropriate incentives, sound money, debt sustainability—do not map into unique policy packages. Good institutions are those that deliver these first-order principles effectively... Reformers have substantial room for creatively packaging these principles into institutional designs that are sensitive to local constraints and take advantage of local opportunities. Successful countries are those that have used this room wisely.

-- DANI RODRIK [2003]

Ethiopia finds itself once again at the cross-roads. The May 2005 national elections have presented the country with a clear-cut choice between a functional multiparty democratic system or a patrimonial state-party system. For the first time in the country's history, the long-suffering citizens have courageously voted their strong preference for an accountable political system. They, in effect, reached out for a double franchise of the free ballot and the well-earned berr— the latter coming out of a full-fledged market economy.

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This window of opportunity must not be squandered, since it is so well suited for undertaking second-generation reforms. With a growth-friendly policy framework, Ethiopia can expect as much as \$50 billion in US currency in the next ten years from the planned big push in development aid to Africa that is designed to meet the United Nations Millennium Development Goals (MDGs). Its Diaspora is also keen to augment the country's supply of skills and investment [COA, 2005; UNMP, 2005]. Absorptive capacity, rather than insufficient financial resources, may ironically be the binding constraint [Agenor, et al., 2004].

The purpose of this paper is to highlight, in a form that is accessible to the widest readership, the major issues of economic reform facing the newly elected government. It seeks to provide a framework for rethinking the strategic choices in the areas of development strategy, fundamental institutional reforms, and policies for short-term economic recovery.

THE PARADOX OF ETHIOPIA'S UNDERDEVELOPMENT

This is not the place to address this question in any detail, but it must be broached because policy disagreements are in no small measure rooted in different preconceptions concerning this paradox. Ethiopia's lingering underdevelopment is paradoxical because the country is characterized by many features that are typically associated with rapid and sustainable economic development. These include an old multi-ethnic state which ensured social order, a high level of access to land by its peasantry, a long history of engagement with world civilizations and international trade, a rather modern family system, and a minimal exposure to slavery and colonialism that ravaged the rest of Africa.

There are, however, many factors that mitigated or even nullified the positive effects of the above attributes. One set of factors has to do with geography in both its geopolitical and geophysical dimensions [Sachs, 2005; Milas and El Aynaoui, 2004].

Geopolitically, the country's location near the Red Sea made it vulnerable to invasion and destabilization in the age of commerce and industry. The effects of Ottoman control of the Red Sea and the pressure from European colonial encirclement are two notable examples that had distracted the country from development efforts.

Geophysically, the large ecological differences between the temperate highlands and the tropical lowlands have created enormous economic barriers. Massive soil erosion and the virtual absence of navigable rivers mean that transportation costs are among the highest in the world, access to seaports is





precarious, and tropical diseases (such as malaria) are rampant. Although the country has enormous potential for hydroelectricity, geothermal energy, and irrigation, the investment requirements remain far beyond the capabilities of a low-income economy.

Among the domestic culprits cited for Ethiopia's economic failure are rapid population growth, environmental degradation, excessive risk averseness, and even a religiously inspired glorification of a life of poverty. These are certainly relevant factors. Upon a little reflection, however, it becomes rather obvious that they are more correlates or manifestations of poverty than its ultimate causes.

Ethiopia's agrarian institutions may provide a more compelling explanation for the reversal of its fortune. In a nutshell, the rather counter-intuitive argument is as follows:

The most important historical fact about pre-Revolution Ethiopia is ironically the landedness of some two-thirds of the peasantry. Being propertied, and contrary to conventional wisdom, the Ethiopian peasantry was able to preempt the emergence of feudal relations. Predictably, the regionally fragmented overlord class had to resort to institutionalized as well as hit-and-run predation in order to exact tribute. The product of tributarism turned out to be a poverty trap that was inevitably reinforced by Malthusian forces [Berhanu, 2005]².

Didn't the 1974 Revolution change all that, one might wonder. It did modify some of the institutions for sure, but not the underlying disincentives. The peasantry for sure ceased to be landed in the sense that the majority lost its land ownership rights. The landless, mostly in the southern provinces, instead became tenants of the state. By the same token, the intermediary classes, the *balabat*, were completely eliminated. Village community lost its traditional leadership and came face-to-face with cadres of the new state-class.

As will be shown below, a number of inappropriate institutions and misguided policies have also contributed to the perpetuation of Ethiopian underdevelopment. The point here is that a sober appreciation of this legacy is essential for formulating an appropriate development strategy and institutional architecture that resonate with the society.

SOME GUIDING PRINCIPLES

One barrier against thoroughgoing reform is the difficulty of supplanting a universalist, faith-based economic policy by a particularist, evidence-based economic policy. Judging from the nascent public debate on economic policy,



the country has a long way to go [Alemayehu, 2004; Kibour, 2003; FSS, 2001].

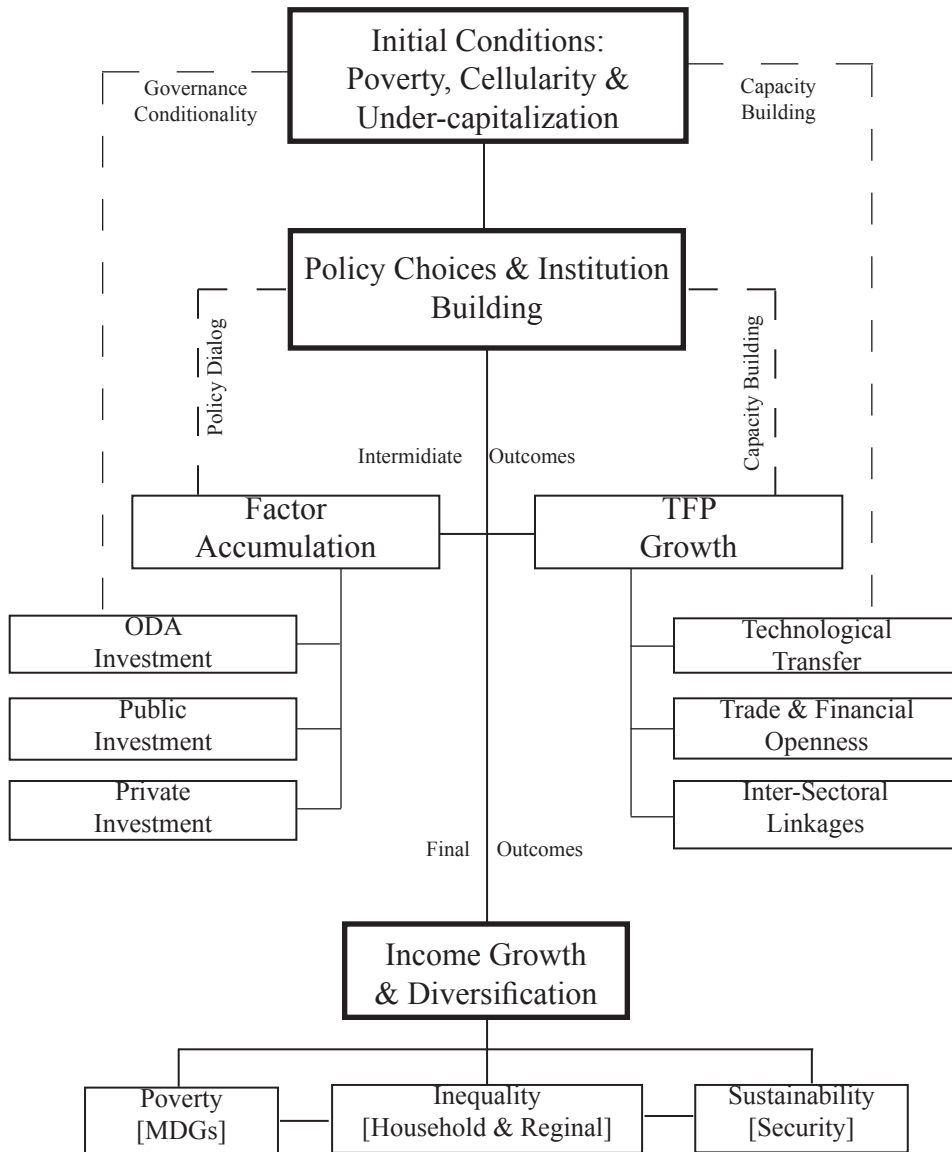
The Power of Ideas

Recounting his journey from the Ivory Tower to the lowly tukul, Jeffrey Sachs [2005, 79-80] makes the case for “clinical economics” in these insightful terms:

The five key lessons of clinical medicine have clear counterparts in good economics practice as well. First, economies, like individuals, are complex systems... Second, economists, like medical clinicians, need to learn the art of differential diagnosis. Clinical economics should train the development practitioner to hone in much more effectively on the key underlying causes of economic distress, and to prescribe appropriate remedies that are well tailored to each country’s specific conditions... Third, clinical economics, like clinical medicine, should view treatment in “family” terms, not just individual terms... Fourth, good development practice requires monitoring and evaluation, and especially a rigorous comparison of goals and outcomes... Fifth, the development community lacks the requisite ethnical and professional standard... [Providing economic advice] requires a commitment to be thoroughly steeped in the history, ethnography, politics, and economics of any place where the professional adviser is working.

How might these principles apply to the current conditions of Ethiopia? The development prospects of an aid-dependent economy like Ethiopia are shaped by three sets of factors as depicted in Figure 1. They encompass factors that are meant to be taken as givens (geography, the legacies of its three postwar governments, enduring mindsets, geopolitical realities, and cultural diversity), factors that are amenable to policy manipulation (capital and skill accumulation, technological transfer, and institutional innovation), and factors that endogenously evolve with the economy (poverty levels, inequality, income security, and sustainability). Fruitful dialog on economic reform focuses on those areas that are most amenable to sensible intervention.

Figure 1
A Framework for Thinking about Aid, Investment and Growth in Ethiopia



ODA = Official Development Assistance
TFP = Total Factor Productivity
MDG = Millennium Development goal

The key idea behind this framework may be summed up as follows:



As the current ascendancy of China and India clearly shows, countries that stand to benefit greatly from globalization are those that have built up their domestic capability for growth through long-standing investments in physical and human capital, and modern institutions. To exploit this capability, opportunities have to exist, domestically as well as internationally, primarily in the form of access to markets. When sensible policies are pursued, governments are then able to facilitate the matching of opportunities with a patiently built-up comparative advantage [Landes, 1999; Rodrik, 2003].

Ethiopia has indeed benefited from a number of first-generation reforms aimed at liberalization since 1992. To its credit, the EPRDF government has managed to boost the annual rate economic growth from 0.5 percent in the 1980s to 6 percent between 1993 and 2002. This outcome is attributable to the combined effects of liberalization, the end of the civil war, occasional good rains, and large aid flows [Abegaz, 2001; FDRE, 2002]. If the task was one of liberalizing repressed markets, as in Latin America, the reforms introduced by the EPRDF would have been sufficient to produce robust growth.

Unfortunately, they are not. The process of deeper institutional as well as policy reform has gotten stuck on a treadmill of secondary reforms since 1998. The greater task for Ethiopia is, therefore, one of husbanding weak markets or non-existent markets. That means Ethiopia has to get its politics, institutions, and its policies “right” almost simultaneously.

Millennium Development Goals (MDGs³)

Two major international reports on the state of development assistance were issued in early 2005. The first came out in January by the United Nations Millennium Project [2005], and the second in March by the Commission for Africa [2005].

These grand pronouncements call for full debt forgiveness and the pooling of donor funds within a common framework. Regarding aid effectiveness, they call for scaling up aid flows to meet presumed thresholds by doubling aid to Africa, providing it in the form of general budget support or sector-wide programs, and supplementing aid with greater access for African exports.



Under the new motto of the aid business, “global partnership, and recipient leadership,” what the two reports have to say about Ethiopia is quite interesting. They patronizingly consider EPRDF’s Ethiopia a well-governed country that is capable of absorbing at least twice as much in investment-oriented aid (currently about \$2 billion in US currency per year). This is in part due to their belief that the institutional capacity of the central government is high. Accordingly, the linchpin of the new policy agenda is a massive increase in aid-financed investment in human and physical infrastructure.

The reservations that remain, especially for the Commission for Africa, include the unacceptably low administrative capacity at the sub-national level, and the less than optimal input of the private sector and civil society organizations in the formulation of the regime’s development agenda. Unfortunately, they have precious little to say about the terms under which domestic resources are to be mobilized and utilized. It also appears to have escaped attention that these issues, in fact, lie at the core of the interface between political governance and economic management.

Premises and Initial Conditions

In the interest of candor, it would be helpful at the outset to make one’s assumptions explicit regarding reform goals and the political and economic conditions that prevail in the country. An acceptable post-election economic reform program, most would probably agree, must meet at least three preconditions.

Firstly, the Program must be consistent with one’s socio-political vision for the country. Mine is one that melds the trinity of prosperity, democracy, and multiculturalism in a manner that is quintessentially Ethiopian. Turning this dream into reality presupposes, at the very least, support for a free peasantry, a model of government that balances multiple identities with loyalty to shared national values and economic institutions, diverse and vibrant civic associations and political parties, an affordable social safety net that covers basic needs, and a cosmopolitan outlook that embraces openness and the Diaspora [*see Table 1 for details*].

Secondly, the Program must be consistent with sound principles—economic as well as political. It must, for example, appreciate the power of economic incentives and tradeoffs, and the need to devise properly sequenced and locally appropriate institutions [Rodrik, 2003; Easterly 2001; World Bank, 2000]. It must likewise respect key political imperatives, especially those pertaining to the fundamental task of taming state or corporate power with built-in restraints, accommodating a diversity of interests in pivotal policy deliberations, and respecting the country’s most noteworthy traditions [van de Walle, 1999; Rodrik, 2003; Grindle, 2002].



Table 1
Ethiopia: Two Contrasting Visions

Area	Status Quo	The Alternative
Political System	<ul style="list-style-type: none"> - Federal model: ethnic states under the control of a vanguard party - Fusion of economic and political power - Revolutionary democracy under vanguard party - Horn policy: secure access to Nile Basin and ports 	<ul style="list-style-type: none"> - Federal model: strong center with multiple, self-governing regional units - Robust market economy and multiparty system - Liberal or social democracy with vibrant civil society - Equitable access to the Nile Basin and regional ports, and the return of Assab
Economic System	<ul style="list-style-type: none"> - Foreign policy: maximize foreign aid - A regimented market economy - Macroeconomic stability - Rapid and equitable growth 	<ul style="list-style-type: none"> - Integrate the Diaspora, facilitate aid and investment - A full-fledged market economy - Macroeconomic stability - Rapid and equitable growth
Economic System		(See Table 2 for details)
Signal Achievements	<ul style="list-style-type: none"> - Article 39: political ethnicity - Article 40: state ownership of land - Business empire of ruling party - Decoupling political power from economic control 	<ul style="list-style-type: none"> - Multiple, complementary identities of citizens - Predominance of private property

Thirdly, the Program must fully reflect the objective realities of economic life as they affect the prospects for rapid, sustained, and widely- shared growth. Ethiopia's initial conditions and current economic profile, we suggest, are less than enviable.

For the average Ethiopian, economic life is a reflection of:

- 1) A fragile growth engine that relies on a low-input, rainfed subsistence farming which accounts for 55 percent of income, 85 percent employment, and 90 percent of exports;
- 2) A sedentary as well as transhumant peasantry that is politically too fragmented to establish its own political party and is likely to remain dependent on the good-will of the urban-based parties to mind its interests;
- 3) A service-based urban economy with only a slightly lower poverty rate and whose income base is almost equally divided among the state, registered enterprise, and informal sectors; and
- 4) One of the most egalitarian distributions of income and wealth in the world—a Pyrrhic victory of equality-in-poverty that has been bequeathed by radical reformers of the past thirty years;

The economic system as a whole exhibits:

- 1) Heavy dependence on foreign economic assistance, one troubling implication of which is that the ruling party no longer has to rely on vigorous domestic tax mobilization; and
- 2) Serious structural impediments including incomplete privatization (ownership diversification) of state enterprises and liberalization, debilitating politicization of public-sector economic management, shallow factor markets, and exceedingly slow diffusion of technology from abroad;

The political sphere may be safely caricatured as:

- 1) A State that is strong enough to control the commanding heights of the economy but too weak to lead the largely mercantile business class onto the road of rapid industrialization; and
- 2) An illiberal and low-trust political culture of clientelist patrimony, extreme risk aversion by political winners in the absence of a system for orderly succession, an enfeebled but regenerating sense of citizen sovereignty, and a long history of *de facto* local political autonomy under autocratic “big men.”



Finally, the country's resource endowment exhibits:

- 1) Negligible amounts of readily exploitable mineral or forest resources but plenty of land and water resources that unfortunately require massive amounts of investment in malaria eradication, irrigation, and transportation infrastructure; and
- 2) An unfavorable geopolitical environment, historically and presently. The bitter fruits of the longstanding and relentless destabilization of the Ethiopian state by Arab and European interests include the secession of Eritrea and the blocking of financing for large projects in the Nile Basin.

BIG POLICY COMMITMENTS

When a national electoral campaign is centered on fundamental (constitutional) issues, as was the case with the May 2005 elections, a country is said to be undergoing a revolution of sorts. Mindful of the need to take full account of the unavoidable peculiarities and complexities of Ethiopia, it is time for forward-looking policymakers to advance an economic platform that is built around the following five commitments.

Right to Food Security and Literacy

A national party worthy of the name must commit itself to the age-old communal ideal that every Ethiopian is entitled to, at the very least, protection against debilitating malnutrition much less death by starvation. Ensuring the internationally recommended daily caloric intake is a goal even the poorest country on earth can afford. In addition, clean water for all, universal primary education for children and universal literacy shall be guaranteed, as would immunization against major infectious and communicable diseases. These MDGs are generally low-cost vehicles for achieving significant immediate gains in average life expectancy.

Secure Property Rights

Secure private rights to land and other economic assets are among the hallmarks of a *bona fide* market economy. The others are vigorous competition mediated by an appropriate regulatory framework, and the provision of key public services in support of the fledgling private sector. All three are essential for creating a robust engine of economic growth.





Common Economic Space

A politically fragmented system is antithetical to the emergence of a competitive national economy. It is, therefore, important that the central government protect and nurture the common national market from protectionist or inept regional governments that impede the movement of legitimate commerce and scarce factors of production to where they are most productive.

Deinstitutionalizing Corruption

The building of business empires by ruling parties (Ethiopia and Eritrea) and politically driven theocratic entities (Sudan) has introduced a novel form of institutionalized corruption in the Horn of Africa. This trend is pernicious mainly because, by fusing political and economic power in the hands of groups who happen to capture the State, it deforms the governance of political and economic markets. Although such firms may fill needed gaps or compete directly with foreign capital, they must not be allowed to frustrate the emergence of a competitive market economy (van de Walle, 1999; World Bank, 2003; 2004).

The Government should accordingly be permitted by law to engage in profit-making activities of critical importance only where the private sector is not capable; rigorously enforce the ban on political entities from owning profit-making enterprises, and liquidate those in existence; regulate or dismantle private monopolies that abuse their market power; and grant civic organizations full access to public information to enable them to discharge their watch-dog responsibilities.

Openness for Industrialization

Labor-intensive and agro-based industrialization is Ethiopia's proverbial Great Transformation and must be the central concern of economic policy. Recognizing that the diffusion of technology and flexible development institutions provides a proven escape from poverty, the highest possible public investment is necessary for kick-starting an industrialization drive. Ethiopia's commercial policy will have to give due regard for regional stability, access to a diversity of regional seaports, and the attraction of foreign trade and capital. We will expound on this issue below.



INSTITUTIONAL REFORMS

Economic institutions define and enforce rights as well as the rules of the game. Institutional reform is, therefore, often a contentious and deliberative process. Bereft of nuances and essential details, Table 2 provides a listing of the key areas of institutional and policy reform that were recently on offer to Ethiopian voters. The following areas of institutional change are of paramount importance for Ethiopia.

Table 2
Ethiopia: Two Competing Economic Platforms

Item	EPRDF Platform	CUD Platform
Development Strategy	- Agriculture-led industrialization	- Urban-rural industrialization
Rural Development	- Land: to issue land-use certificates - Service: limited public investment - Growth strategy: lease to investors,	- Full title to rural land - Provision of adequate public services - Regional growth poles linked to and support smallholders agro-processing and exports
Urban Development	- Land: streamline lease system - Service: haphazard planning	- Full privatization with restitution - Comprehensive urban plans, and investment in job creation
State Activism	- Command can control - Rent seeking - Competition: blunted	- Private-public partnership for development - Provision of infrastructure and public services - Competition: privatization of most SOEs & POEs, regulation of conglomerates
Financial System	- Low transparency - Narrow Treasury market - Selective, and donor-driven aid	- Open and NBE autonomy - Broad-based securities market for LT investment - Progressive: use aid to enhance domestic productivity and competitiveness
Openness		
	SOE = State-Owned Enterprise; EPRDF = Ethiopian Peoples Revolutionary Democratic Front;	POE = Party-Owned Enterprise; LT = Long Term; CUD = Coalition for Unity and Democracy.

Balance between Addis Ababa and the Regions

Political devolution to self-governing regions, as federal units or as decentralized components of a unitary state, remains hollow if it is not complemented by decentralization of economic decision making. The EPRDF government's recent efforts in the area of fiscal decentralization and the development of local capacity, down to the *woreda* level, deserve support and further deepening [FDRE, 2002]. The current model of manipulative decentralization must, however, be reformed in a manner that curbs local authority to unduly restrict inter-regional mobility of labor and capital while enhancing local power to raise revenue⁴.

Balance between the State Sector and the Non-state Sector

Ethiopia's enfeebled (and poorly organized) modern private sector consists primarily of merchants, small-scale builders, and small processors. This is, in part, an outcome of a long history of political entrepreneurship by its ambitious elites in search of tribute. The political class has been mainly preoccupied, as in the rest of Africa, with the myopic project of converting political power into private—personal and organizational—wealth.

Leapfrogging from a regime of “primitive accumulation” by kleptocratic political entrepreneurs to the brave new world of “productive accumulation” by economic entrepreneurs entails a new conviction by the state elite and the nascent capitalist class concerning the necessity of mutual accommodation. The new social contract might take the East Asian form of a public-private sector “partnership for development”—that is, one that transforms the grabbing hand of the State into a helping hand for development.

A developmentalist Ethiopian state will have to view itself as an incubator of pioneering enterprises slated for timely privatization and a supporter of promising private ventures to be reciprocated by the latter in form of quick acquisition of competitiveness. The private sector, in turn, holds up its end of the bargain by self-enforcing product standards and codes of conduct, and serving as an effective countervailing power against the excesses of the bureaucracy. A jointly formulated development strategy would then dictate the allocation of grants, soft loans, foreign investment, public spending, and domestic private-sector resources. This way, the country may finally have the chance to run as fast as it possibly can on two legs.

Land Policy

Land policy is arguably the most important economic and political issue of institutional reform. Politically, it is key to ending for good the three-decade-old strangulation of the peasantry by the cadre systems of the vanguard party. Economically, it is a necessary, if not sufficient, condition for the emergence of optimal farm sizes and the development of off-farm activities that are key to ensuring income diversification and food security.⁵

Ethiopian subsistence farmers neither own land nor enjoy universal access to essential public services. Without these, they could not possibly muster the ability or the incentive for improving farm or off-farm productivity. The institutional and policy reforms needed to escape from this destitution trap must, therefore, embrace land privatization, significant increases in aid-supported public investment in the rural economy, and small-scale industrialization.

Three options exist for land reform in Ethiopia, the detail of which is provided in Berhanu [2004]. One is to strengthen the status quo by providing land certificates as more secure forms of state tenancy. The second option is transferring ownership rights to communities with full access to land (but no right of sale) to members.

The third option is to extend individual titles of full ownership. This may hasten, as Vladimir Lenin feared, the emergence of an empowered peasantry with a vested interest in a market economy: "Peasants are revolutionary when they want land, and counter-revolutionary once they have obtained land."

Individual title provides the strongest security of land rights for all. It also amounts to a restoration of the age-old right enjoyed by at least two-thirds of the peasantry. To minimize disputes, allocation may be based on the 1975 Land Reform Proclamation. The Proclamation eliminated tenancy but also ensured that the peasantry is: (a) spatially trapped in a vicious circle of destitution, and (b) rendered politically dependent by linking state-supervised access to land to village residence.

Land ownership is no magic escape out of the poverty trap. After all, some 60 percent of the smallholder population is land-poor, while some 10 percent are landless. Without complementary public investments to kick-start the growth process, agrarian transformation will be a pipe dream.

The transformation of subsistence agriculture into a commercial one is ultimately predicated on an African green revolution. For Ethiopia, agrarian transformation is premised on adequate investment in research and development on tropical agriculture, rural roads and related infrastructure, extension services and farmer education that includes full participation of women, and improved access to long-term capital for the most enterprising farmers.



The same applies to urban land whose privatization is key to spurring investment in housing and business structures. Previously nationalized houses and factories should also be returned to their rightful owners or full restitution paid to Ethiopians as was done for foreign owners. Redressing this injustice provides a unique opportunity for reaffirming the rule of law and delegitimizing the contrived justness of confiscating legally obtained private property willy-nilly just because political power has changed hands.

Financial Sector Reform

Ethiopia's financial system is characterized by a shallow bond market, regimented forex allocation, and short-term-oriented commercial lending. The current banking laws have stifled modernization, even by Eastern African standards, by discouraging robust competition between private banks and state banks. They do not afford sufficient political insulation of the National Bank of Ethiopia (NBE) to do its job of regulating the banking system or conducting a prudent monetary policy.

While monetary discipline has been the hallmark of Ethiopia's postwar governments, even in the face of a tax system with low buoyancy, the current banking regime lends itself to unconstrained political interference. This state of affairs has left the Commercial Bank of Ethiopia with a huge debt overhang and hamstrung private banks poised to overtake it in terms of loan volume and financial innovation.

The government has invoked the banking crises in emerging markets, a transitory problem that exists only in diversified financial systems that arguably were nudged into full openness imprudently, to argue against deregulating and deepening such a backward system. In Ethiopia's case, prudential deregulation needs to be undertaken to level the playing field between the state banks and the private banks, allow for the entry of foreign banks on a mutually beneficial basis, diversify the financial system through entry of non-bank (insurance and casualty) and non-traditional (postal savings, credit unions) institutions, preempt politically driven loans, and provide NBE with the right mix of autonomy and accountability.

Regional Strategy for the Horn

Ethiopia, as the anchor state of the Horn of Africa, needs to devise a regional development strategy to maximize positive spillovers and minimize negative ones. The regional strategy must be designed to ensure equitable use of the rivers' basins, secure access to the region's ports, and facilitate the integration of the Horn's economies. Absent a stable and dynamic neighborhood, the





region will likely continue to dissipate its scarce resources on unproductive and mutually destructive activities.

DEVELOPMENT STRATEGY

There are two sets of interrelated issues that define the economic strategy of a development-friendly government. One deals with the appropriate relationship between city and country. The other pertains to regionalization of economic activity.

Growth Strategy: Rural-led versus Urban-led

EPRDF's development strategy, dubbed Agriculture Development-led Industrialization (ADLI), envisions the smallholder rural economy as the engine of development. The strategy has so far proven ineffective in providing food security, much less in fostering industrial development. The limits of this rural-based strategy are many. It depends on productivity gains from a subsistence economy with a high chronic vulnerability to a number of risks, and it ignores critical linkages between farming and non-farming activities. Not surprisingly, one can hardly find historical examples of industrialization generated by this smallholder-led model.

Another, and perhaps a more promising alternative, is what may be called Urban-led Agro-industrialization (ULAI). This strategy recognizes at least two key features of Ethiopian underdevelopment. The country has public and private sectors, both of which are weak. Furthermore, its fledgling modern urban economy has a much higher potential for serving as a growth engine than the moribund subsistence economy of the countryside. The urban advantage stems from various sources. Cities, with ample supply of skills and good infrastructure (transportation, storage, communication, and energy), are the primary conduits of technological and financial transfers from globalization.

In many ways, the choice between properly conceived ADLI and ULAI is a false one. A pro-poor development strategy must focus on the rural population and use its urban population, and rely on its urban population to spearhead its industrialization drive. In fact, the development trajectory of successful developers in East Asia and India was one of brief, rural-led development propelled by the green revolution which was followed by a prolonged urban-led development propelled by manufacturing and services.

Ethiopia's development strategy must, therefore, envision walking on two synchronized legs. One leg is the minority (say, 25 percent) of skilled and better landed farmers who have the competitive advantage to produce most of the marketable surplus of food and fiber needed by the industrial sector.



The other leg is a reinvigorated urban economy. The latter would integrate the former by serving as the primary conduit for new technology, supply of marketable skills, innovative business organization, and wider access to internal as well as external markets.

Economic Regions

The above considerations are neatly fused together in the concept of economic regions for a country like Ethiopia that, by virtue of its underdevelopment, is dominated by cellular local economies. An integrated “growth poles” approach will, however, have to factor in such issues as risk, factor supply, infrastructure and inter-sectoral linkages [Miller, et al, 1969; World Bank, 2003; Milas and El Aynaoui, 2004].

An Ethiopian regional development strategy would allocate scarce resources, on the basis of well-researched plans, to the following geographic areas. The tasks include:

- 1) creating an enlarged Menagesha Region that provides Addis Ababa with an agricultural and industrial hinterland, and, furthermore, converting the leading urban centers (especially metropolitan Addis Ababa and the Nazret-Mojo-Dire-Dawa corridor) into full-fledged “industrial districts” of interlocking small-and medium-scale manufacturers;
- 2) developing the country’s enormous potential for tourism with a special focus on Addis Ababa (as an international city), the historical centers of Christianity and Islam (especially the northern provinces, and Harrer), and the eco-tourist attractions (the southern lakes and forest regions);
- 3) converting other cities (such as Jimma, Dessie, Bahirdar, Gonder, and Awassa) into sub-regional commercial centers that would be progressively integrated with their rich agricultural hinterlands;
- 4) developing sub-regional growth poles in those areas with the greatest agricultural potentials, including investing in irrigation whose estimated potential size is 4 million hectares⁶, and exploiting the potential for supplying Europe and the Near East with high value-added agricultural products (notably vegetables, spices, and cut flowers);
- 5) developing strategic distribution-processing centers at the confluence of major transportation arteries and seaport connections (such as Kombolcha, Awash, Gambela, Metema, Moyale, Woldya, Mekele, and Dire Dawa). This way, the urban and semi-urban growth centers would radiate into the vast subsistence economy;



- 6) developing a “regional growth triangle” encompassing the entire Horn region to exploit economies of scale in hydroelectric power generation and transmission, oil and gas pipelines, transportation-communication hubs, and transborder river basin development. In addition to its economic advantages, this super-regional approach would facilitate political stability by interlocking the economic interests of the region’s political and economic elites; and
- 7) embracing the growing Ethiopian Diaspora (including the granting of dual citizenship), whose income probably equals the national income.

POLICY SPACE AND PROCESS

A well-crafted economic policy reform program is designed to provide positive incentives for economic actors to do good for society by doing well for themselves. Policy is most effective when it is tailored to changing circumstances, open to public scrutiny, and cognizant of the need to compensate losers, by taxing winners [Grindle, 2002; World Bank, 2004].

Two issues will be raised here. One issue deals with the need to formulate a crash program to ensure adequate availability of food in the most vulnerable districts and to provide employment for restive youths in the cities. The other addresses the need for cultivating a transparent and inclusive policy process.

Transition Program

As J.M. Keynes once quipped, “In the long run, we are all dead.” Recurrent food insecurity in the rural areas and an unacceptably high rate of urban unemployment and underemployment means that the new administration has to devise a crash program of economic recovery.

The main opposition parties did extraordinarily well in the urban areas during the hotly contested 2005 parliamentary elections in part due to extravagant promises of plentiful jobs [CUD, 2005]. The initiative for economic recovery may very well involve more than the usual public works program. It may include an economic *zemetcha* of sorts in the towns by mobilizing the idle youth and in the villages by boosting the food-for-work programs. A pertinent recognition here is that Ethiopia lacks a well established tradition of producing high quality crafts and manufactures unlike its historical counterparts including Egypt, Turkey, India, Vietnam, or China. A medium-term program then has to be devised to increase the supply of intermediate, marketable skills especially among the educated youth. This would certainly entail, among other things, establishing of model workshops, factories, and vegetable gardens.





In the future, vocational-oriented institutions as well as traditional universities will have to pay more attention to the development of marketable skills that complement ambitious programs of private-sector development. There already exists an unmet export market niche in the Diaspora for high quality cultural goods.

The Policy Process

On the dubious assumption that things can never get worse, the basic principle of the Ethiopian Left seems to have been: "Some change is good. Big change is even better." True to form, policymaking in the country has inevitably been driven largely by self-serving and absolutist ideology rather than by an open and pragmatic approach to setting targets, selecting the right instruments, and evaluating the outcomes.

Neither a vibrant market economy nor a viable democratic system can exist in Ethiopia in the absence of respect for fair play, and without a culture of consultation and evidence-based policymaking. To this may be added the need for reclaiming policy sovereignty from donor agencies, technocratic policy implementation by adequately compensated and accountable civil servants, and broad stakeholder participation. The time has indeed come to create a policy space for a hard-headed but a soft-hearted approach to economic management.

Political parties with a good grasp of what is meant by enlightened self-interest would surely appreciate the virtues of having a large menu of realistic policy options to choose from, an informed public to sift out those choices driven by narrow interest from those driven by ideas, and a workable mechanism for evaluating policy outcomes.

One course of action is the promotion of promoting economic literacy especially among legislators and civic and political leaders. Another is providing strong support for universities, specialized think tanks, and professional associations to facilitate the generation of credible policy options. The same goes for the motley of advocacy groups, the free press, and concerned citizens who lend legitimacy to the economic policy agenda.

CONCLUSIONS

This paper takes stock of the challenges of deeper economic reform in Ethiopia in the hope of framing the debate more fruitfully. It argues that Ethiopia has to make a clean break with the misguided statism of its recent past in order to advance the cause of its insatiable need for long-term investment.





Though it is arguably the poorest country of its size, the country does boast some good things in its favor. The high degree of equality in asset and income distribution, the diversity of its agro-ecological zones, the large pool of semi-skilled labor, the growing stability of the Horn of Africa, and, though landlocked, its closeness to major international trade routes are all good for growth.

Furthermore, the deepening of democracy and re-professionalization of its civil service, the recent focus on Africa aid in the context of the MDGs, the intense loyalty of its Diaspora, and the sizable pool of merchant capital which can transform itself into an industrial capital are additional assets. The challenge for enlightened policymakers, therefore, is one of identifying the package of interlocking investments. The minimum goal is a sustained growth rate of national income on the order of seven percent per annum.

Finally, we will do well to remember that there are no failed people, only failed policies or institutions. Given a collective will to do what it takes to fight poverty, the operation of the law of cumulative causation can be made to operate in the reverse—that is, success often breeds success. Contemplating the end of Ethiopian poverty in our lifetime is, mercifully, no longer a pipedream.

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Notes

1 A combined and updated version of remarks made at the United Ethiopian Democratic Forces (UEDF) symposium in Washington, DC, in September 2004, and at the UCLA's African Studies Center Symposium on Contemporary Ethiopia: Revolution and Transformation? in March 2005. I thank the participants for helpful comments and suggestions.

2 The socio-political landscape of contemporary Ethiopia is also profoundly molded by tributarism. For one, the various Ethiopian peoples, from the Agaw or the Amhara in the North to the Oromo or the Somali in the South, invariably employed a territorially expansionist strategy in search of tribute payers thereby creating high rates of mutual demographic absorption. Secondly, and as a result, none of the major ethnic groups has a history of establishing unified and territorially-defined ethnic-states. Elites of various ethnic colors vied instead, and did take turns, to serve as flag bearers of the pan-ethnic Ethiopian state.

3 MDGs consist of eight goals: eradicate extreme poverty and hunger; (Add) achieve universal primary education; promote gender equality and empower women; reduce child mortality; improve maternal health; combat HIV/AIDS, malaria and other diseases; ensure environmental sustainability; and develop a Global Partnership for Development.

4 A little digression into a dispassionate reading of the history of the past 50 years illustrates the point about the chain of missed opportunities for building on good legacies. The imperial government, in all fairness, had laid down many of the foundations of good economic governance: a professional civil service, a modern civil and criminal code, a modern educational system, some space for fledgling professional associations, hosting international organizations that have made Addis Ababa a dynamic cosmopolis, and even a decree (see *Negarit Gazetta*, 1966) for the establishment of awraja-level regional, self-administration.

5 Taking 16 million metric tons of grain as the requirement for ensuring a daily caloric intake of 2100 for all, Ethiopia can achieve this goal in good years if it were to substantially reduce the unacceptably high pre-harvest and post-harvest losses alone. The institutional and policy reforms would, of course, boost productivity to exceed this goal in the medium run.

6 Leading candidates for modern agro-industrial zones are the regions of Debre Zeyt—Nazret, Debre Brehan—Fiche, Lake Tana, southern Wollo, greater Harrer, Sashemene, Debre Markos, Bako-Lekenti—Gimbi, Jimma—Bedele, Awassa—Moyale, Setit Humera, Assela—Ticho Robi—Begoji, and southern Tigray [Miller, et al., 1969; Milas and El Aynaoui, 2004].

7 A rough estimate of its significance can be derived as follows: The value of the annual output of the formal private sector (some 120,000 registered enterprises) is estimated to be around \$600 million in US currency. If we apply an average capital-output ratio of 4, this would give us a rule-of-thumb estimate for a private sector capital stock at \$2.4 billion in US currency. A widely-quoted estimate of the capital of EPRDF's companies is \$1.0 billion in US currency. That means, party-owned companies may very well account for well over one-third of the private sector capital stock. When MIDROC is factored in, the two conglomerates may account for well over half of the private sector—a remarkably high concentration ratio indeed.

