

AFRICA RISK CONSULTING

Ethiopia Monthly Briefing November 2015

Ethiopia Summary 6 November 2015

Ethiopia improves its ranking in the World Bank's Doing Business index to 146 of 189 countries assessed. Ethiopia's highest rankings are for construction permits and enforcing contracts. Its lowest rankings are for accessing credit due to state dominance of the financial sector. State-owned Ethio Telecom will soon launch an international infrastructure upgrade tender, but CEO Andualem Admassie insists that it does not mark a liberalisation of the sector. Humanitarian agencies prepare to respond to the ongoing humanitarian crisis in northeastern and eastern Ethiopia. Agencies compare the scale of the Horn of Africa drought to the one that occurred in 2011.

Ethiopia makes small gain in Doing Business ranking

Ethiopia marginally improved its ranking in the **World Bank's Doing Business** index from 148 in its 2015 report to 146 in *Doing Business 2016*.¹ The *Doing Business* report provides objective measures of business regulations and their enforcement across 189 countries, in an effort to identify legal and regulatory barriers facing investors. The *Doing Business* ranking did not contain any major surprises for investors with Ethiopia still a daunting destination for companies with a limited risk appetite. Ethiopia's highest ranking was for dealing with construction permits (73) and enforcing contracts (84).² Despite the World Bank ranking, property rights more generally remain a deterrent for investors as they are unable to purchase land. The state owns all land and its property records are poorly maintained.³ The lack of transparency in allocation increases corruption risks.⁴ In the category of enforcing contracts, it takes 530 days to resolve a commercial dispute in Ethiopia and costs 15% of the value of the claim.⁵ This is favourable compared to **Kenya, South Africa** and **Rwanda**⁶ and will reassure investors who have complained that the investment regulatory framework is outdated.

*"The government is revising the 1996 **Investment Code**, but this is a long process and may not include all the changes that investors want, especially about liberalisation."*⁷

Despite delays to the revised Investment Code, the contract enforcement ranking is indicative of government efforts to improve the bureaucratic and legal environment. The **Ethiopian Investment Commission** has improved its record of service delivery, as has the **Federal Ethics and Anti-Corruption Commission** in curbing corruption.⁸

*"At lower levels, stringent bureaucratic oversight means that corruption in Ethiopia is actually quite subdued – at least in comparison to most other **sub-Saharan African** countries. Graft such as petty tax fraud in the private sector, for example, is rare. Corruption in Ethiopia is difficult to execute and is dealt with severely if uncovered. In the majority of cases, the benefits of acting*

1 www.doingbusiness.org

2 www.doingbusiness.org

3 Addis Fortune, 27 Feb 2014.

4 Addis Fortune, 27 Feb 2014.

5 www.doingbusiness.org

6 www.doingbusiness.org

7 Source, investment advisor, Addis Ababa

8 Source, investment advisor, Addis Ababa

*corruptly are outweighed by the risks of getting caught for the **Addis Ababa** business community.”⁹*

The World Bank ranked Ethiopia 167 for accessing credit, down from its 2015 ranking of 165.¹⁰ The report cites low levels of foreign reserves and the diversion of domestic credit to state-led infrastructure projects. These additionally raise investor concerns about the hard currency required to repatriate profits. A March 2011 directive forces commercial banks to buy bonds from the state-owned **Development Bank of Ethiopia** to channel national savings into financing state-owned long-term infrastructure projects.¹¹ While the government continues to guard the banking sector closely, international banks are seeking first mover advantage with the **Standard Bank of South Africa Ltd** opening a representative office in Addis Ababa on 30 October.¹² Standard Bank said its priorities are power projects, infrastructure, agribusiness and fast moving consumer goods.¹³

The World Bank has amended its data collection tools, and now considers ‘quality’ and not just ‘efficiency’ in its rankings. This punished Ethiopia in a number of categories, notably in terms of electricity. Whereas previously the World Bank considered only the time and cost of connection to the national grid, it now factors in the dependability and transparency of tariffs. Ethiopia received the lowest possible score for the reliability of supply.¹⁴ While Ethiopia has the cheapest electricity in the **Horn of Africa**, the reliability of supply is extremely poor due to inadequate and underdeveloped infrastructure including in urban centres. Although Ethiopia’s current generation capacity of 2,250MW exceeds domestic demand, demand is growing 25% annually¹⁵ while dilapidated infrastructure also results in failures “*as frequently as every second day*”.¹⁶ **Ethiopian Electric Power (EEP)** is set to increase tariffs imminently to close the gap between electricity generation costs and selling price.¹⁷ The tariff increase is the result of a reduction in subsidies and will increase electricity prices approximately 50% to 9 cents per kWh.¹⁸ The tariff revision will allow for greater investment in EEP’s generation and transmission networks, and may attract increased foreign investment.

The World Bank additionally adapted its ‘trading across borders’ indicator to include the cost of documentary compliance, border compliance and domestic transport. The World Bank now follows the chain of a single item: in the case of Ethiopia, the World Bank selected the importation of auto parts from **Japan** and the export of coffee to **Germany**. Both items passed through the **Port of Djibouti**, Ethiopia’s major export-import terminal and gateway to international shipping lanes. Ethiopia ranked 166 in this category.¹⁹ With regard to imports, the time for border compliance is 203 hours (compared to a sub-Saharan Africa average of 160 hours), the cost of border compliance is \$668 (average \$643), documentary compliance is 209 hours (average 123), and documentary compliance is \$750 (average \$350). With regard to exports, the time for border compliance is 57 hours (average of 108 hours), the cost of border compliance is \$144 (average \$542), documentary compliance is 126 hours (average 97), and documentary compliance is \$175 (average \$246).

Importing and exporting remain burdensome. Procedures involve different agencies and there is no legal framework in place to recognise electronic documents including online signatures and payments due to delays in the **Ethiopia Revenue and Custom Authority’s** implementation of the **Single**

⁹ Source, business analyst, Addis Ababa

¹⁰ www.doingbusiness.org

¹¹ Addis Fortune, 10 Nov 2013.

¹² Government statement, 3 Nov 2015.

¹³ The Reporter, 31 Oct 2015.

¹⁴ www.doingbusiness.org

¹⁵ AllAfrica.com

¹⁶ Source, senior financial sector executive

¹⁷ Ethiopian Herald, 31 Oct 2015.

¹⁸ Ethiopian Herald, 31 Oct 2015.

¹⁹ www.doingbusiness.org

Window System Solutions for Customs and International Trade.²⁰ Transporting goods along poor roads to the distant border is expensive. The domestic transport cost to the border for exports is \$550 and imports \$529. Logistics risks in the form of high trade costs remain a deterrent for foreign investors and large export-orientated companies. Logistics and supply chain professionals view Ethiopia in a negative light, rating it behind **Syria, Iraq, Iran** and **Libya** for potential as an emerging logistics market in the **2015 Agility Emerging Markets Logistics** survey.²¹ Transportation will improve when the **Ethiopia-Djibouti Railway** begins operating in the first quarter 2016. The railway will decrease transportation times of bulk and containerised cargo from two days to approximately eight hours.²²

Ethio Telecom to launch infrastructure tender

State-owned **Ethio Telecom** will launch an infrastructure upgrade tender in the fourth quarter 2015 or January 2016.²³ CEO **Andualem Admassie** was careful to state that while the upgrade was open to international companies, this did not reflect a liberalisation of the telecommunications sector. The planned upgrade will increase Ethio Telecom's mobile coverage by approximately 72%.²⁴ In December 2014, Ethio Telecom signed an infrastructure expansion and network vendor contract with **Sweden-based Telefonaktiebolaget L. M. Ericsson**.²⁵ Ethio Telecom had originally signed the contract with **China-based ZTE Corp** in 2013 as part of a wider \$1.6 billion contract with ZTE Corp and China-based **Huawei**. The government annulled parts of the contract due to a disagreement over the costs of upgrading the network. Andualem confirmed that the tender is open to all companies, but told reporters that the government did not plan to allow foreign telecom operators into its domestic market.

*"The answer to your question [whether] Ethiopia is planning to open up the telecom sector to foreign operators is no. We will not open the telecom sector to foreign companies because we need to use the money from the sector as an enabler of growth of the country."*²⁶

The latest deal does not necessarily indicate a change of policy. The Ethiopian government was happy to use private companies in the telecommunications sector in the past. In 2010, the government turned over management of Ethio Telecom's predecessor **Ethiopian Telecommunications Corp** to **France Telecom**. However, there is political reluctance for further liberalisation:

*"This is partly because jobs at Ethio Telecom are an important source of political patronage. Profits from the company boost government revenue, and amount to more than the government can obtain through a privatisation or joint venture agreement."*²⁷

Ethio Telecom's monopolistic control over the sectors results in little incentive to decrease its prices or improve service delivery. Despite profits of over 21.5 billion birr (\$1 billion) in the 2014/2015 financial year, Ethio Telecom lacks a long term strategic plan to increase telecoms penetration.²⁸

Government and NGOs begin drought response

Humanitarian agencies are gearing up to respond to the ongoing humanitarian crisis in northeastern and eastern Ethiopia. The inaction so far is on the part of both the Ethiopian government and humanitarian agencies. The Ethiopian government was reluctant to admit the scale of the problem it faced.

²⁰ Source, business analyst, Addis Ababa

²¹ www.agility.com

²² Capital, 15 Jun 2015.

²³ Reuters, 28 Oct 2015.

²⁴ Reuters, 28 Oct 2015.

²⁵ Reporter, 15 Dec 2014.

²⁶ Africa Review, 1 Nov 2015.

²⁷ Source, analyst, East Africa

²⁸ Source, analyst, East Africa

“Up until only three months ago, the Ethiopian government did not say anything about the looming drought in many parts of the northeastern and eastern parts of the country. Then, right after NGOs said there could be acute food shortages in those areas, it came up with the story that there are food shortages in some areas but that doesn’t amount to a drought.”²⁹

The government has now issued an appeal for \$596m of food assistance and has openly acknowledged that there are 8.2 million people who require food assistance.³⁰ **El Niño** weather conditions have exacerbated the failed spring and weakened summer rains.³¹ On 30 October, state minister for agriculture **Wondirad Mandefro** told reporters that there was 40% less rain than normal this year, with some heavily affected areas experiencing no rain at all.³² The conditions have resulted in acute food insecurity and malnutrition, and impacted livelihoods.³³

“We have managed to significantly increase food production in the past five years but we have not yet managed to achieve food self-sufficiency. We will transform the agriculture sector in the next five years but until then our safety net and other pro- poor programmes will continue.”³⁴

One of Wondirad’s major announcements was the proposed transformation of the agriculture sector through increased commercialisation.³⁵ Wondirad also talked about a focus on smallholder farmers working on specific high priority commodities in identified geographies for the coming five years.³⁶ Despite the government discussing the potential of the agriculture sector, humanitarian organisations are pressuring it to focus on the seriousness of the current problem. The **United Nations** said on 27 October that Ethiopia is experiencing its worst drought in 30 years, with levels of acute need across all humanitarian sectors having already exceeded levels seen in the Horn of Africa drought of 2011, and which are projected to become far more severe in 2016. It further highlighted that its humanitarian team in Ethiopia and the government have held a series of briefings with donor partners – separately and together – to raise the alarm about the on-going El Niño-caused drought emergency and to warn about what is coming ahead. It is feared that an extended El Niño could threaten the next rains, which normally would begin in March.

“The lean season in some of our operational areas, when food is scarce between harvests, is usually for three months, from April to June. It is hard to predict, but there are serious concerns that the lean season in 2016 could last for eight months as opposed to three.”³⁷

The government has provided \$192m funding to provide food assistance but analysts say this has already overstretched government resources.

“... no one expected the food shortages to be this big so the government is using all its emergency reserves for this purpose and even going too deep in its pocket to fill funding gaps.”³⁸

The government has urged donor support to ensure a healthy food pipeline for the coming months. Humanitarian agencies are beginning to accelerate their responses.

*“There has been a definite escalation in response. The comparisons to the 2011 Horn of Africa drought are an intentional strategy. It is the one benchmark that gets donors listening as their lackadaisical approach exacerbated the situation then and they cannot afford a repeat. The crisis in Syria and **Greece** had definitely distracted attention and finances over the past couple of months, but things are clicking into gear now. Donor fatigue is no longer the issue it was even a*

²⁹ Source, journalist, Addis Ababa

³⁰ Source, journalist, Addis Ababa

³¹ Source, senior INGO official, East Africa

³² Source, journalist, Addis Ababa

³³ Source, senior INGO official, East Africa

³⁴ Source, journalist, Addis Ababa

³⁵ Source, journalist, Addis Ababa

³⁶ Source, journalist, Addis Ababa

³⁷ Source, journalist, Addis Ababa

³⁸ Source, journalist, Addis Ababa

*month ago. Negotiations over access have started with the Ethiopian government. But do not forget, it is very much part of a wider Horn of Africa response so competing priorities, stretched logistical chains, and factoring in the egos of four governments [Kenya, **Somalia**, **Sudan** and **South Sudan**] rather than just the one.”³⁹*

Implications

The World Bank ranking alone will not sway investor sentiment towards Ethiopia. Tangible reforms to customs and trade regulations, reliable electricity, and meeting the infrastructure deficit are more likely to be persuasive. This will take time but the government appears committed to the process, especially to improving trade logistics. The government’s reluctance to liberalise the banking sector will continue to make access to credit a business bottleneck. This will constrain capital injection, foreign exchange access and banking skills. Partial liberalisation will limit private capital, hampering productivity and export revenue.

Ethiopia’s telecommunications sector would benefit from increased competition. The government may time announcements about liberalisation to coincide with the **World Trade Organization** ministerial summit in **Nairobi** (Kenya) between 15 and 18 December.

While donors are mobilising rapidly, the humanitarian crisis in Ethiopia is quickly becoming acute. Beyond the lives at risk, the drought is a reminder that Ethiopia remains susceptible to climate shocks, which may curb its economic growth and damage investor perceptions.

³⁹ Source, journalist, Addis Ababa

About Africa Risk Consulting:

Africa Risk Consulting (ARC) is a pan-African consulting company that provides timely, relevant information and advice that enables its clients to take informed investment decisions and to safeguard their reputations.

ARC's core consulting services include integrity due diligence and corporate investigations, political advisory and country assessments, opportunity monitoring and reputation risk management. Most relevant to private equity firms is ARC's integrity due diligence and corporate investigations capability. Specifically, ARC offers pre-deal integrity checks to highlight red flags before negotiations start; full detailed multi-jurisdictional reputation due diligence; and supplier and senior hire vetting and repeat due diligence for compliance programmes. ARC is unique in that it offers a 10-day delivery for a routine integrity due diligence. ARC also offers a suite of corporate investigations services from immediate investigation, evidence gathering, e-discovery, forensic accounting and whistleblower support on one end to crisis media management and regular monitoring on the other.

www.africariskconsulting.com

About ARC Briefing:

ARC Briefing is ARC's essential online business information service.

Companies at any stage in their Africa expansion, whether building or communicating an Africa strategy, investing directly, expanding current operations, financing other investors, doing the legal leg-work or researching the Africa growth trend, need ARC Briefing.

ARC Briefing is an online information service keeping you:

- Up to date with Country Chronologies of business-critical events
- In the know via Country Briefings on political, economic, business and operating trends. Written in-country, ARC experts analyse and comment
- Ahead with Country Planner which details future elections, budgets, regulatory changes etc.

www.briefing.africariskconsulting.com

Getting in touch

Please contact us by email info@africariskconsulting.com or call + 44 (0) 20 7078 4080

Follow us on Twitter: [@ARCBriefing](https://twitter.com/ARCBriefing)