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Ethiopia: Economic Development in a Harsh Environment: Part 1

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A visit to Ethiopia provides food for thought for an economist who devotes much of his time to the Middle East. During the last twenty years, despite many problems and a very difficult historical legacy, Ethiopia has experienced rapid economic growth. It remains a very poor, landlocked country with few natural resources and faces serious internal political problems but is experiencing something rare: relatively good governance. This has made the difference that is currently boosting growth and reducing poverty levels. This edition examines the political and economic development of Ethiopia in recent decades. The June edition will analyze the relevance of its experience for other countries.

Between 1930 and 1974 (with the exception of the Italian occupation of 1936-41) Ethiopia was ruled by the emperor Haile Selassie. In 1973-1974, tensions rose as oil prices rose and in September 1974 there was a coup led by army officers known as the Derg. The Derg abolished the monarchy and adopted communism making Ethiopia a Marxist-Leninist one-party state. It also abolished feudalism, raised literacy rates, nationalized many assets, and introduced radical land reforms. In 1977, Mengistu Haile Mariam became chairman and leader of the ruling group and he launched the Qey Shibir, or Red Terror, designed to eliminate political opponents, as a result of which more than 50,000 were killed.¹

The famine that affected Ethiopia from 1983 to 1985 was the worst in a century, resulting in over one million dead and was massively aggravated by government policies including its counter-insurgency strategy, and restrictions and burdens imposed on the population of non-insurgent areas designed to achieve social transformation. Around 400,000 refugees left the country and 2.5 million people were

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internally displaced, while almost 200,000 children were orphaned. Economic decline, the famine, increasing reliance on foreign aid from the Soviet Union, as well as mismanagement and corruption, the Eritrean War of Independence, and the Ethiopian Civil War between the Derg and ethnic militias all brought misery to the country.²

In the late 1980s, the geopolitical environment worsened for the Derg, as the Soviet Union under Mikhail Gorbachev abandoned its support for the expansion of communism overseas. Struggling to maintain its economy, the USSR ceased to provide aid to Ethiopia. This resulted in even more economic hardship, and in the face of attacks by guerrilla forces in the north, military rule collapsed. At the end of January 1991, a coalition of rebel forces, the Ethiopian People's Revolutionary Democratic Front (EPRDF), captured the northern cities of Gondar, Bahir Dar and Dessie. At the same time, the Eritrean People's Liberation Front had gained control of most of Eritrea. The Soviet Union could no longer prop up the Derg and in May 1991 its leader, Mengistu, fled to Zimbabwe. One of the most important components of the EPRDF was the Tigray People's Liberation Front (TPLF). Its existence was a response to the product of the marginalization of Tigray over many years. In May 1991 when the EPRDF took power in Addis Ababa as the Transitional Government of Ethiopia, the TPLF had 80,000 fighters and other groups about 10,000.³

In July 1991, EPRDF convened a national conference to establish a transitional government. In June 1992, the Oromo Liberation Front (the Oromo are the largest ethnic group in Ethiopia) withdrew from the government; in March 1993, members of the Southern Ethiopia Peoples' Democratic Coalition also left the government. In 1994, a new constitution was written that established a parliamentary republic with a bicameral legislature and a judicial system. A federal system of government with nine states was established. The first multiparty elections took place in May 1995 and were won by the EPRDF. The president of the transitional government, EPRDF leader Meles Zenawi a Tigrayan, became prime minister, and Negasso Gidada was elected president. Meles remained prime minister until his death in 2012 and was succeeded by his deputy, Hailemariam Desalegn.

Meles had clear views about economic policy and laid the foundations of Ethiopia's development. In a series of interviews with Alex de Waal, he defined the "developmental state". First the state must be autonomous from the private sector. It should use the private sector and guide it but not be dominated by it. The basis of the state is the peasantry, freed of tribal alliances and fully involved in improving its economic well-being. Banks, utilities and some key production sectors should be

controlled by the state. The state's main concern, even its ideology, is economic development and this should also be the main social norm.

Ethiopia should not, according to Meles, adopt the Washington consensus that emphasized minimizing the role of the state, privatization and encouraging foreign investment. It should adopt an eclectic approach using policies adopted in the Far East. He said: "I call it the 'Frank Sinatra' model: 'I did it my way'". One of Meles' major concerns was to avoid corruption and rent seeking (being rewarded for being in office without doing anything). "Corruption and rent seeking are connected. Rent seeking is the perfect environment for corruption to thrive. You can have the most perfect macroeconomic policies but if the politics are wrong, you have the wrong class alliance with rent seekers in power, it is a recipe for corruption. And once the institutions of government have become controlled by rent-seekers it is almost impossible to uproot the corruption. Look at the way in which anti-corruption drives simply become a mechanism for a leader to purge his rival and opponents".⁴

Meles ruled for twenty-one years. He organized one-party rule for the Tigray People's Liberation Front (TPLF) and his Tigrayan inner circle, with the complicity of other ethnic elites that were co-opted into the ruling alliance, the EPRDF. The Front promised freedom, democracy and ethnic devolution but was highly centralized, and closely controlled the economy and suppressed political, social, ethnic and religious liberties. Ethiopia has grown increasingly unstable largely because the TPLF has become increasingly repressive, while failing to implement the policy of ethnic federalism it devised over twenty years ago to accommodate the country's varied ethnic identities. The result was greater centralization, along with greater ethnic tension. The government restricted social expression and curbed journalists, non-governmental organizations and religious freedoms. Through these tactics, Meles adroitly navigated a number of internal crises and kept TPLF factions under his tight control.⁵

Discontent did not end with the death of Meles. In 2015, there were widespread protests calling for social and political reforms including an end to human rights abuses, government killings of civilians, mass arrests, government land seizures, and political marginalization of opposition groups. There were also complaints by the country's two largest ethnic groups, the Oromo and the Amhara, that they had long been shut out of power by the Tigray minority that dominated the ruling coalition. Another issue was Ethiopia's land tenure system, in which ownership rights were vested in the state. Under this system, the government has, in recent years, forcibly relocated tens of thousands of residents to make space for commercial agriculture projects.⁶

The government responded by restricting access to the Internet, attacking and arresting protesters. Hundreds were reported to have been killed. Desalegn ordered the release of thousands of political prisoners to ease tensions but in 2018, he became the first Ethiopian leader to resign.

In April 2018, the former intelligence officer and minister, Abiy Ahmed Ali became prime minister. He has a doctorate in political science and he is from the Oromo and Amhara ethnic groups. He also has a Muslim father and a Christian mother. These combinations raised hopes that he would be a unifying force in a country facing many ethnic and other pressures.

Abiy began by launching a major program of political and economic reforms, not all of which were welcomed by supporters of the federal-based constitution of Ethiopia. Since taking office, Abiy's government has released thousands of political prisoners and liberalized the country's political system. In May 2018 alone, over 7,600 prisoners were pardoned in the Oromo region. Parliament lifted the ban on three opposition groups, Ginbot 7, Oromo Liberation Front (OLF), and the Ogaden National Liberation Front (ONLF) in June, but the ruling party controls all the seats in parliament.⁷

In May 2018, it was announced that the draconian anti-terrorism law, widely felt to be a tool of political repression, would be amended. In June 2018, parliament approved the necessary legislation, ending the state of emergency. In his first briefing parliament in June 2018, Abiy countered criticism of his government's release of convicted "terrorists", which according to the opposition was a name the EPRDF gives those who oppose it. In June 2018, the ruling coalition also announced its intention to pursue the large-scale privatization of state-owned enterprises and the liberalization of several key economic sectors long considered off-limits, marking a major change in the country's state-oriented development model.

State monopolies in the telecommunications, aviation, electricity, and logistics sectors were to be ended and those industries opened up to private sector competition. Shares in the state-owned firms in those sectors, including Ethiopian Airlines, Africa's largest and most profitable, were to be sold to domestic and foreign investors, although the government will continue to hold a majority share in these firms, thereby retaining control of key sectors of the economy.

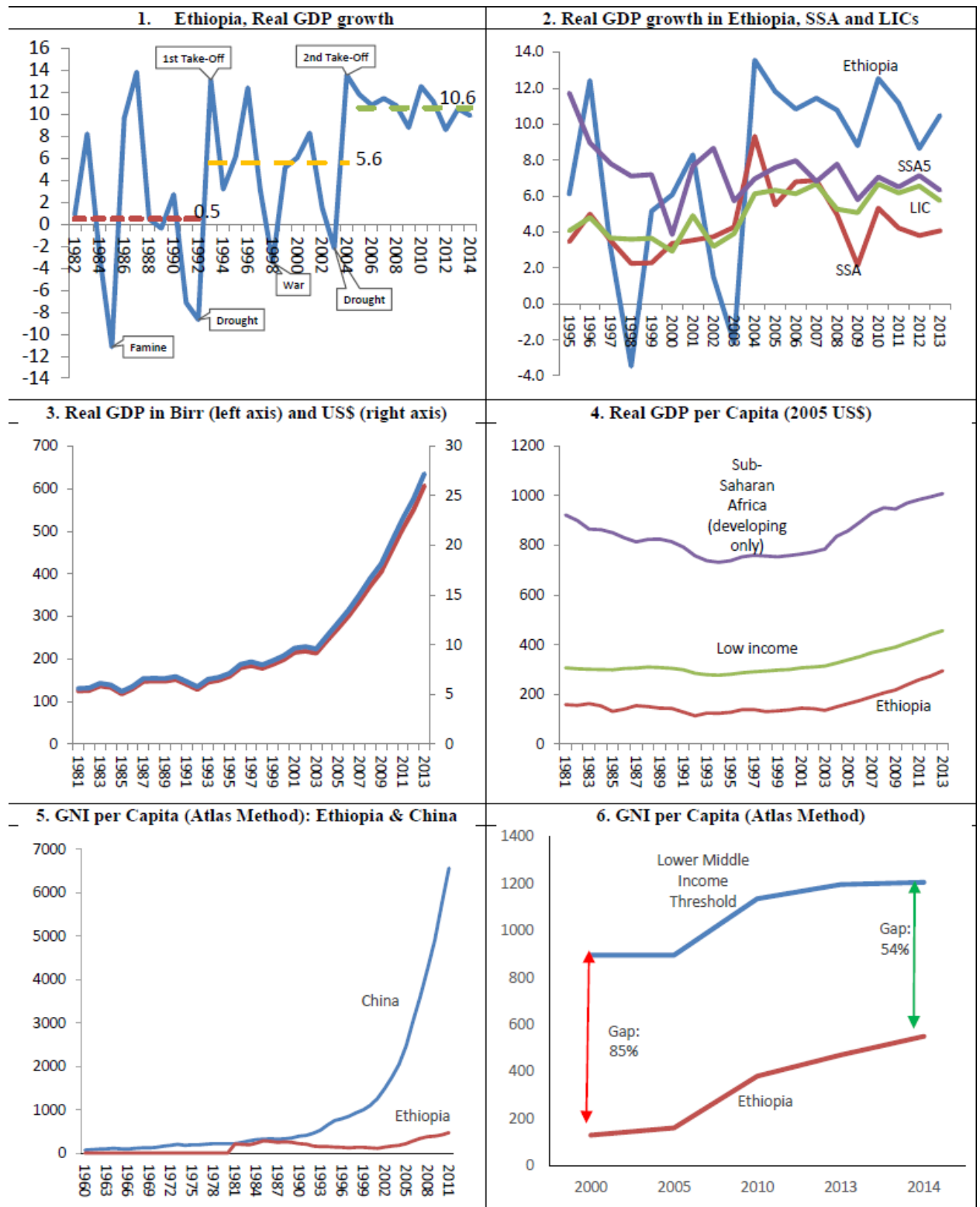
While this represented an ideological shift regarding the degree of government control over the economy, it was also a pragmatic measure aimed at improving the country's dwindling foreign-exchange reserves, which by the end of the 2017 fiscal year were equal to less than two months' worth of imports.⁸ In 2018, Abiy also announced plans to establish an Ethiopian stock market by 2020. In 2015 Ethiopia was the largest country in the world, in terms of both population and gross domestic product, not to have a stock exchange.⁹ In addition, Ethiopia is one of the largest countries in Africa, with an area of 1.104 million square kilometers.

In 2017, it had a population of almost 105 million people and was the second most populous nation in Africa after Nigeria. In that year, the population grew by about 2.5 percent a year compared with a peak rate of 3.6 percent in 1992. Although it has fastest growing economy in the region, it is also one of the poorest, with a per capita income of \$783 as of 2017.¹⁰ (The significance of the decline in the rate of population growth will be examined in the June edition of *Iqtisadi*). It is much less urbanized than other African states: its capital, Addis Ababa, has a population of about 5.5 million compared with 15-20 million in Lagos and 20 million in Cairo.

Ethiopia's economy experienced strong, broad-based growth averaging 10.3 percent a year from 2006/07 to 2016/17, compared to a regional average of 5.4 percent, but growth decelerated to 7.7 percent in 2017/18.¹¹ During the period 2004-2014, economic growth was both rapid and stable. According to official data, real GDP growth averaged 10.9 percent annually in 2004-2014. Given population growth of about 2.5 percent per year, real GDP growth per capita averaged 8.0 percent per year. This was much faster than the growth rates achieved during the monarchy (1951-73: 1.5 percent), the *Derg* regime (1974-91: -1.0 percent), or the first decade after the country's transition to a market-based economy (1992-2003: 1.3 percent; 1993-2004: 4.5 percent). Droughts and conflict resulted in unstable growth patterns prior to 2004, but since then growth has been rapid and stable which is impressive from a historical perspective. Ethiopia's growth rate also exceeded regional and low-income country averages over the past decade. (See Table 1, section 2, below):

Table 1

Ethiopia: Growth Comparisons

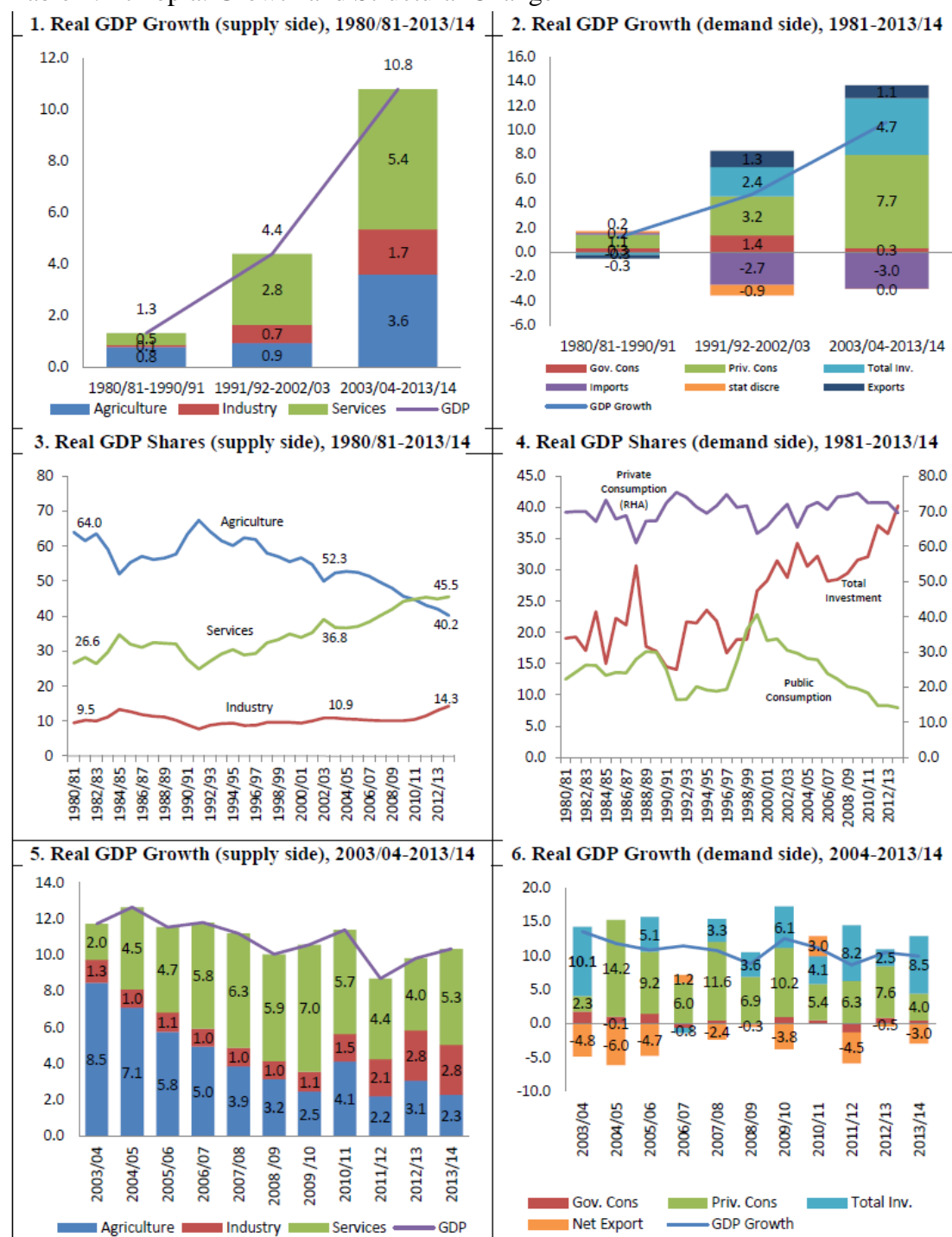


Source: World Bank (WDI). Note: SSA5 include Burkina Faso, Mozambique, Rwanda, Tanzania and Uganda.

Ethiopia's growth performance over the past decade was part of a broad and very successful development experience. In 2000, Ethiopia had one of the highest poverty rates in the world, with 55.3 percent of the population living below the international poverty line of \$1.90 (at 2011 purchasing power parity, PPP) per day and 44.2 percent of its population below the national poverty line. By 2011, 33.5 percent lived on less than the international poverty line and 29.6 percent of the population was below the national poverty line measure. Ethiopia is one of the most equal countries in the world in terms of income distribution and low levels of inequality have largely been maintained during the period of rapid development.

The bulk of the growth, despite being relatively widespread among the population, was concentrated in agriculture and services. In 2010, the services sector overtook agriculture in terms of output. (See Table 2, section 3) This process had been going on for a decade, and it accelerated after 2004. Since then, growth has accelerated in services and, more recently, in industry. The recent expansion of industry is due to a construction boom rather than an increase in manufacturing output which remains very small at about 4 percent of GDP. Private consumption and investment were the major sources of demand. The investment rate has increased substantially since the mid-1990s with a commensurate decline in public consumption.

Table 2: Ethiopia: Growth and Structural Change



Source: World Bank

Poverty reduction in Ethiopia has been faster in regions where poverty was highest in 2000. Ethiopia is one of the most equal countries in the world largely as a result of very equal distribution of consumption in rural areas. In urban areas, all measures of inequality showed a substantial increase in inequality from 1996 to 2005 and a substantial reduction in inequality from 2005 to 2011. In rural areas, there has been little change in inequality over time although inequality fell marginally from 1996 to

2005 and increased from 2005 to 2011. Nationally, urban and rural trends offset each other and many measures suggest inequality was quite stable from 2005 to 2011. However, measures of inequality that give more weight to poorer households show that national inequality increased from 2000 until 2011.

Since 2000, there have been substantial improvements in health, education and living standards. Life expectancy increased and progress was made towards the attainment of the Millennium Development Goals (MDG), particularly in gender parity in primary education, child mortality, HIV/ AIDS, and malaria. While in 2000 only one in five women in rural areas had an antenatal check-up, more than one in three women attended an antenatal checkup in 2011. Women are now having fewer births: the total fertility rate fell from almost seven children per women in 1995 to just over four in 2011. The share of population without education was also reduced considerably from 70% to less than 50%. Finally, the number of households with improved living standards measured by electricity, piped water, and water in residence doubled from 2000 to 2011.¹² Between 1990 and 2017, life expectancy at birth rose by 40 percent and between 2000 and 2017 the human development index, that covers health, education and income, rose by 64 percent.¹³

Since the early 1990s Ethiopia has pursued a “developmental state” model with the objective of reducing poverty. The involved a strong role for the government in the economy and high levels of public investment to encourage growth and improve access to basic services. The model has been one of agricultural development led industrialization in which growth in agriculture is emphasized in order to push economic transformation. The contribution of agriculture to value added has been large throughout this period, however over time the importance of agriculture has declined from 52 percent in 2004 to 40 percent in 2014 and the importance of the service sector has increased from 37 percent in 2004 to 46 percent in 2014. (See Table 2, section 3). Economic growth was broad-based and has been the main driver of reductions in poverty from 1996 to 2011. Growth has been important, but the average ‘growth elasticity’ was quite low: each 1% of growth resulted in only a 0.15 percent reduction in poverty, better than the sub-Saharan African average, but lower than the global average. Growth in agriculture was very inclusive and contributed significantly to poverty reduction. Ethiopia has a rural, agricultural-based labor force: more than four out of every five Ethiopians live in rural areas and are engaged in small-holder agricultural production. Poverty fell fastest when and where agricultural growth was strongest. For every percent of growth in agricultural output, poverty was reduced by 0.9 percent which suggests that agricultural growth has caused reductions in poverty of 4 percent per year on average since 2005 and 1.1 percent per year between 2000 and 2005.¹⁴

According to the World Bank, Ethiopia faces three main challenges. Its economy has limited competitiveness, which constrains the development of manufacturing, the creation of jobs and the increase of exports. The private sector is underdeveloped, which limit the country's trade competitiveness and resilience to shocks. Political and social tensions, could threaten foreign investment, tourism, exports and thus economic growth.¹⁵

¹ Jacob Wiebel, "[The Ethiopian Red Terror](#)." *Oxford Research Encyclopedia of African History*, 2017.

² Alex de Waal, "Evil Days: Thirty Years of War and Famine in Ethiopia" *African Watch*, (New York: Human Rights Watch, 1991).

³ "Tigray People's Liberation Front." *Encyclopedia Aethiopica*, (Wiesbaden: Harrassowitz Verlag, 2003).

⁴ Alex de Waal, "The Future of Ethiopia: Developmental State or Political Marketplace," *World Peace Foundation*, August 20, 2018, p. 3.

⁵ "[Ethiopia After Meles](#)," *International Crisis Group*, Briefing 89, August 22, 2012.

⁶ Claire Felter, "[Ethiopia: East Africa's Emerging Giant](#)," Council on Foreign Relations, October 5, 2018.

⁷ *Human Rights Watch*, "[Ethiopia: Events of 2018](#)".

⁸ *IMF*, "2018 Article IV Consultation-Press Release; Staff Report; and statement by the executive director for the Federal Democratic Republic of Ethiopia," 2018.

⁹ Kaleyesus Bekele, "[Addis Ababa Stock Exchange in 2020](#)," *The Reporter Ethiopia*, December 22, 2018.

¹⁰ *World Bank Group*, [Ethiopia population growth \(%\), 2017](#).

¹¹ *World Bank Group*, [Ethiopia overview](#).

¹² *World Bank Group*, "Ethiopia's Great Run," World Bank Other Operational Studies 23333, 2015.

¹³ United Nations Development Programme, "[Human Development Indices and Indicators: 2018 Statistical Update, Ethiopia](#)" 2018.

¹⁴ *World Bank Group*, "[Ethiopia Poverty Assessment 2014](#)," 2015.

¹⁵ *Ibid*, see note 11.