

Liberalizing Ethiopia's Local Markets: Opportunities and Challenges for Local and Foreign Investors

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1. INTRODUCTION

Ethiopia has recently liberalized its market policy and opened up key sectors such as export, import, wholesale and retail to foreign companies. The new policy regulates foreign investment in these sectors and sets minimum thresholds for export volumes, import values and store sizes (Ashine, 2024). The aim of the new policy is to attract foreign investment while ensuring a level playing field for domestic companies. This creates new opportunities for foreign companies to engage in Ethiopia's growing economy, particularly in exporting commodities such as coffee and hides, importing a wide range of goods, participating in wholesale trade and investing in retail, provided they meet the set requirements. Market liberalization is seen as a positive “game changer” that boosts competition, improves access and helps exporters to reorient themselves (FDRE. Directive 1001/2024, 2024). However, balancing local and foreign interests remains a priority as reforms aim to open up opportunities while overcoming challenges such as regulatory barriers and underdeveloped logistics. The aim of this article is to provide a comprehensive analysis of the key opportunities and challenges associated with the recent liberalization of Ethiopia's local markets for both local and foreign investors. It also explains the key aspects of the new directive for South Korean investors.

2. THE CHANGING LANDSCAPE OF ETHIOPIA'S LOCAL MARKETS

Ethiopia has a long history of courting foreign direct investment, with foreign investors playing an important role in building the country's modern manufacturing industry since the 1920s. Under the regime of Haile Selassie (former Emperor of Ethiopia) in the 1950s and 1960s, the government enacted favorable investment incentives that led to a significant influx of foreign direct investment, particularly in the manufacturing sector. However, it was criticized that this gave foreigners a

disproportionate advantage over local investors. After the Dergue regime came to power in 1974, foreign investment declined as the state nationalized large companies. When the Ethiopian People's Revolutionary Democratic Front (EPRDF) came to power in 1991, it restructured its policies to encourage private sector growth and foreign direct investment by revising investment laws and creating incentives. As a result, FDI increased significantly, reaching USD 4.2 billion in 2021, with China being the largest investor (Ashine, 2024). Key sectors attracting FDI include manufacturing, real estate, agriculture and renewable energy. Indeed, Ethiopia has identified several priority sectors for investment and economic development, including agriculture, manufacturing, mining, ICT and tourism. The country also has other important sectors such as energy, health and transportation and logistics, which offer significant opportunities for growth. In addition, emerging sectors such as telecommunications, financial services and privatization initiatives, as well as the development of both public and private Special Economic Zones (SEZs) have been highlighted as priority areas. By strategically targeting these different sectors, Ethiopia aims to attract foreign direct investment, drive industrialization and promote sustainable economic growth (Ashine, 2024).

While agriculture dominated in the past, today the service sector makes the largest contribution to GDP, including the state-owned Ethiopian Airlines. Industry accounts for 29% of GDP, including manufacturing, construction and related activities (NBE, 2024, p. 11). Ethiopia has recently attracted significant foreign direct investment. According to the Ethiopian Investment Commissioner, Ethiopia received USD 3 billion in foreign direct investment in the first 10 months of fiscal year 2024 (FBC, 2024). Other promising sectors for foreign investors include infrastructure development, agribusiness, renewable energy, mining, textiles and digital transformation. Ethiopia's growth trajectory offers diverse investment opportunities in its expanding economy in the wake of political change and economic dynamism (Shkuri, 2023).

3. OPPORTUNITIES FOR LOCAL AND FOREIGN INVESTORS

The liberalization of Ethiopian markets offers important opportunities for local and foreign investors. It provides access to Ethiopia's large, growing consumer base and middle class, as well as favorable investment incentives such as tax exemptions and industrial parks. This can facilitate technology transfer, innovation and integration into global value chains. This also offers local

entrepreneurs and SMEs the opportunity to develop their skills, collaborate with larger companies and participate in multinational value chains. For example, allowing foreign banks in Ethiopia would help integrate the country into the global investment market, bring in capital and expertise, and encourage foreign direct investment, but with appropriate regulations to avoid financial instability (Shkuri, 2023). Overall, market liberalization is expected to increase the competitiveness of local businesses in the global market, provide access to new markets and promote Ethiopia's economic development and integration into the global trading system.

The new policy is expected to boost domestic production, exports and support Ethiopia's WTO accession. The global experience, capital and market access of foreign companies will benefit local businesses and consumers in the form of more competition and better quality products at competitive prices. The country has also attracted investors drawn by its large domestic market, well-educated labor force, industrial parks and investment incentives. However, the current level of foreign direct investment is still inadequate and the Ethiopian Investment Commission needs to further strengthen its institutional capacity as the lead agency for managing foreign direct investment.

The liberalization of the Ethiopian market offers South Korean companies new opportunities to expand their presence in Africa and diversify their trading partners. South Korean companies can utilize Ethiopia's diverse natural resources such as asbestos, bentonite, ceramic clay and kaolin to support the production of building materials, ceramics and other industrial products. The abundant coal, iron ore, copper, nickel and manganese reserves can be utilized to support the South Korean steel, energy and metal industries. In addition, the deposits of gemstones, gold and other valuable minerals offer opportunities for collaboration in the jewelry and luxury goods sectors. Companies can also explore Ethiopia's geothermal, limestone and gypsum resources for the development of renewable energy and construction materials (Ethiopian Geological Survey, 2016).

In addition, South Korean companies can participate in the huge Ethiopian market of automotive manufacturing (Hyundai, Tucson, Creta), electronic assembly including cell phones and TV screens (Samsung), automotive parts, electronics, semiconductors, chemical manufacturing, assembly, house construction and sales, pharmaceuticals, bridge building and creative arts industries. Ethiopia's large population and fast-growing economy provide significant opportunities

for South Korean companies to establish manufacturing facilities, utilize local talent and meet the growing demand in the country and region (PDC, 2020).

South Korean companies have also opportunities to participate in the development of a "Smart City" project in Ethiopia, which focuses on creating an eco-green city with initiatives in urban agriculture, healthcare, and electronic systems. Additionally, they can invest in vocational and higher education infrastructure, digitalize public services, support science and technology advancements, and contribute to health and urban development systems. They can also explore the textile and garment sectors by investing in Ethiopian industrial parks (PDC, 2020).

4. CHALLENGES FOR LOCAL AND FOREIGN INVESTORS

While Ethiopia's efforts to liberalize trade offer opportunities, the country's business environment continues to pose challenges for investors. Regulatory complexity, infrastructure gaps, limited access to finance, inconsistent Forex and investment regulations, peace and security issues hinder investment. Liberalization also raises concerns about the impact on domestic businesses, food security, and government revenues. The existing investment policy remains general, highlighting the need for a more targeted foreign direct investment (FDI) policy. Key obstacles include insufficient quality and quantity of FDI projects, limited export earnings, and employment not commensurate with approved investments. FDI is unevenly distributed, with over 83% concentrated in Addis Ababa and Oromia. Investors also report unpredictable, unclear, and rapidly changing laws and regulations, inconsistent implementation, weak government coordination, and logistical problems. Political stability, security, anti-corruption, and financial sector reforms are crucial to attract foreign investment and facilitate the participation of foreign companies in the Ethiopian market.

Ethiopia faces numerous obstacles in maximizing the benefits of foreign direct investment, including ineffective investment incentives and weak linkages between foreign and domestic firms. The financial sector also suffers from neglect of human capital management, leading to talent gaps. Local banks need to change their HR practices, invest in training and offer comprehensive compensation to build a competitive workforce, with the government supporting joint ventures to

gain access to foreign expertise (Etensa, 2023). For Ethiopia to fully realize the benefits of foreign investment, both the macroeconomic constraints to FDI and the microeconomic constraints to human capital need to be addressed.

Ethiopia's plans to liberalize the banking sector face major challenges against the backdrop of general economic instability, including high inflation, currency devaluation and an unpredictable exchange rate regime. Foreign banks are reluctant to enter the market due to the political and economic turmoil, while local banks fear losing customers to the new competition (Shkuri, 2023). Prioritizing short-term recovery and reconstruction while maintaining long-term development is crucial as the government faces the policy challenge of ensuring stability and implementing structural reforms, including privatization and the introduction of competition, which first requires adequate restructuring and improvement of state-owned enterprises. Despite progress in industrialization, Ethiopia faces persistent policy and implementation challenges that require careful sequencing of reforms, learning from global best practices and adapting strategies to the country's unique context in order to harness the country's potential for sustainable economic transformation, including the gradual liberalization of the retail and banking sectors while strengthening regulatory capacity (NBE, 2024).

5. STRATEGIES FOR FOREIGNERS' SUCCESSFUL MARKET ENTRY INTO ETHIOPIA'S LOCAL MARKETS

When considering entering the Ethiopian market, some strategies can increase the chances of success. A thorough market assessment, comprehensive due diligence, appointing experienced local representatives, investing in personal relationships, hiring legal counsel, and exploring government tenders are all critical elements for successful market entry in Ethiopia (Habte, 2023). Dealing with the unique cultural nuances, business practices and regulatory environment is crucial. Extensive market research, localization and adaptation, regulatory compliance, optimized logistics and supply chain management, and a patient and persistent approach are all critical elements for foreign companies looking to establish a sustainable presence in Ethiopia's dynamic and promising local markets.

For example, Safaricom, a leading Kenyan telecommunications company, has secured a 15-year telecommunications license to operate in Ethiopia through the Global Partnership for Ethiopia (GPE) consortium. While Safaricom brings extensive experience and expertise in the industry with its market entry in 2022, it also faces challenges such as political instability, government interference, potential subsidies/protectionist measures and foreign exchange risks. Nevertheless, Safaricom has taken proactive steps to overcome these obstacles. These include taking out appropriate risk insurance, negotiating a mobile money license and leveraging its experience in the Kenyan market. Despite the ongoing hurdles, Safaricom views its Ethiopia venture as a long-term investment opportunity and has already achieved remarkable success by surpassing 5 million subscribers in less than a year. The company aims to further expand its customer base by introducing its successful mobile money platform, M-Pesa, to the fast-growing Ethiopian telecom landscape.

In addition, Ethiopia should identify various policy intervention areas to attract FDI based on the global experience of successful FDI attraction strategies. These are regulatory framework, FDI administration/management, political and economic stability, FDI targeting and promotion, FDI services, investment incentives for FDI, linkages between FDI and domestic enterprises, maximizing the benefits of FDI, and mitigating the risks of FDI (Debebe, et.al. 2023). These recommendations provide a comprehensive framework that the Ethiopian government and the

Ethiopian Investment Commission can use to formulate an effective FDI policy. To implement these recommendations, the government needs to build institutional, human and financial capacity and prioritize the development of concrete action plans in these critical areas.

6. CONCLUSION

The liberalization of Ethiopia's local markets presents both opportunities and challenges for investors. The country's growing consumer base, investment incentives and the potential for technology transfer and localization are enticing. However, regulatory barriers, infrastructure gaps, forex regulations, limited access to finance and inconsistent laws present significant hurdles. To maximize the benefits of investing in Ethiopia, policy makers, local companies and international firms need to work together. This requires simplifying regulations, investing in infrastructure, strengthening the financial sector and promoting consistent investment laws. Political stability, peace and security are also crucial. While exchange rate volatility and corruption are a concern, it will be crucial to capitalize on Ethiopia's strengths while addressing the remaining reform priorities in the business environment to attract foreign companies, drive economic integration and achieve sustainable development.

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