

**A joint roadmap between the Government of Ethiopia and DAG for  
the implementation of the Addis Ababa Action Agenda (AAAA)**

**Final**

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## Acronyms

AAAA	Addis Ababa Action Agenda
ADLI	Agricultural Development Led Industrialization
AfDB	African Development Bank
CAP	Common Africa Position
CRGE	Climate Resilient Green Economy
CSA	Central Statistical Agency
CSD	Council for Sustainable Development
DAG	Development Assistance Group
DFID	Department for International Development
DRM	Domestic Resource mobilization
ERCA	Ethiopian Revenues and Customs Authority
ETB	Ethiopian Birr
EU	European Union
FDI	Foreign Direct Investment
FDRE	Federal Democratic Republic of Ethiopia
FeMSEDA	Federal Micro and Small Enterprises Development Agency
FfD	Finance for Development
GCF	Green Climate Fund
GDP	Gross domestic product
GoE	Government of Ethiopia
GTP	Growth and Transformation Plan
IAIPs	Integrated agro-industrial parks
IPDC	Industrial Development Corporation
LDCs	Least Developed Countries
LPI	Logistics Performance Index
M&E	Monitoring and Evaluation
MFIs	Micro finance institutions
MoANR	Ministry of Agriculture and Natural Resources
MoFED	Ministry of Finance and Economic Development
MoH	Ministry of Health
MoI	Ministry of Implementation
MoCS	Ministry of Civil Services
MoST	Ministry of Science and Technology
MEFCC	Ministry of Environment, Forest and Climate Change
MoFEC	Ministry of Finance and Economic Cooperation
MoWIE	Ministry of Water, Irrigation and Electricity
NBE	National Bank of Ethiopia
NEBDCC	National Economic and Business Diplomacy Coordination Committee
NECC	National Export Coordinating Committee
NPC	National Planning Commission
NPSCSC	National Productive Sector Competitiveness Support Council
ODA	Official Development Assistance
PASDEP	Plan for Accelerated and Sustainable Development to End Poverty
PPP	Public-private partnership
SD	Sustainable Development
SDC	Sustainable Development Council
SDPRP	Sustainable Development and Poverty Reduction Plan
SDGs	Sustainable Development Goals
TOT	Turnover Tax
UNDAF	United Nations Assistance Framework
UNDP	United Nations Development Programme
UNDESA	United Nations Department of Economic and Social Affairs
UNIDO	United Nations Industrial Development Organization
USAID	United States Agency for International Development
VAT	Value added tax

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## Executive summary

The overriding development agenda of Ethiopia is to sustain the rapid and broad-based growth path witnessed during the past several years and eventually end poverty and achieve sustainable development goals (SDGs). It has set out a very ambitious goals to achieve economic, social and environmental transformation and achieve a lower middle income status by 2025.

The Government of Ethiopia has also expressed its commitment to ensure the effective implementations and achievement of regional and global agreements such as SDGs, Agenda 2063, Paris Agreement and Addis Ababa Action Agenda (AAAA). In particular, the realization of SDGs and targets crucially depends on the effective implementation of the Addis Ababa Action Agenda. The government of Ethiopia has adopted various aspects and principles of the AAAA in its national strategies to ensure the mobilization of the various means of implementation required for the achievement of national objectives and SDGs. In addition, meeting sustainable development objectives require increasing financing options through mobilizing additional domestic and foreign resources. Although the finance landscape in Ethiopia has broadened to include non-traditional development partners (e.g. China, India, Kuwait, Saudi Arabia and Turkey), there is a need for better allocation of existing resources, effective alignment of incentives, and additional funds from domestic and external sources. In addition, tapping into new partnerships and innovative sources of financing can also play a role in complementing public sources of financing for sustainable development.

The main objectives of this study were twofold: to identify priority areas for intervention by government and stakeholders from a resource mobilization perspective and develop a roadmap to guide the implementation of the Addis Ababa Action Agenda. Using the Development Finance Assessment (DFA) framework as the main framework, the study provided a detailed analysis of sources of development finance for Ethiopia. The study uses both primary and secondary data. Primary information was generated through key informant interviews held with relevant government sector ministries, development partners, and Ethiopian Chamber of Commerce and Sectoral Associations, while secondary information was collected from different sources including government financial statistics published by the Ministry of Finance and Economic Cooperation, development plans (e.g. GTP-II), and other sources such as review of development policies and strategies.

The Ethiopian government has made substantive strides in articulating sustainable development as reflected in its development policies, strategies and plans which incorporate sustainable development (SD) principles and objectives. The supreme law of the land, which was adopted in 1995, incorporated sustainability and has become the guiding framework for subsequent mainstreaming of SD into national and sectoral plans. Between 2005 and 2014, three medium-term development plans had been adopted and implemented which helped improve both economic and social indicators. The latest development plan is the second generation of growth and transformation plan (GTP-II) (2015/16-2019/20) which coincides with the beginning of SDGs. Ethiopia has well-articulated many of targets and indicators of SDGs in its latest growth and transformation plan and has also designed a detailed implementation strategies to address the objectives set out in the GTP-II. As part of the plan, GTP-II includes results framework covering the main goals, outputs, targets, and indicators, as well as responsible institutions to monitor and track sectoral progresses. However, some of the indicators in the GTP-II Policy Matrix could not be populated with baseline data, indicating a



paucity of baseline information to support results-oriented performance measurement and report across sectors. In addition, the Policy matrix needs to include additional targets and indicators related to the Addis Ababa Action Agenda. The plan lacks detailed indicators to monitor resource mobilization from different sources and needs to be supported by a detailed finance mobilization strategy.

The scale of resource requirements is huge to achieve the objectives and targets set in the economic, social and infrastructural development, environmental conservation, good governance and democratic system as articulated in the GTP-II. According to the budgetary financial plan, it is envisaged that domestic revenue and external grants would cover about 86 percent of government expenditure, with average overall deficit of 14 percent. Of this, external loans would cover close to 38.8 percent, while the remaining would be generated from domestic borrowing. The government allocates a large share of its budget to capital outlays which enable the government to provide basic services and infrastructure to the majority of the population.

Despite robust economic growth, the share of tax revenue in GDP has not shown significant improvement as tax revenue has remained low compared to the tax revenue generating capacity of the economy, the financing requirements of the development programs and the average performances of the sub-Saharan countries, indicating existence of some kind of inefficiency in tax administration and structural problems in the tax system. Tax compliance cost is high in Ethiopia (between 4.5 and 5.8 percent of total government revenue in 2012/13), and it is higher for small businesses compared with large business as measured by the share of tax compliance cost in turnover. There is also a wide gap between tax capacity and actual tax revenues raised due to tax-administration challenges. These suggest that there is a need for improving tax revenues by, among others, broadening the tax base (e.g. through identifying new tax bases), enhancing efficiency of tax administration (e.g. modernization) and awareness creation. The Ethiopian government has expressed its commitment to strengthening domestic tax revenue mobilization through various interventions as indicated in GTP-II. The establishment of a tax directorate with the Ministry of Finance and Economic Cooperation indicates government's commitment to enhance the tax revenue capacity.

Domestic revenue mobilization is also constrained by the preferential treatment granted to specific taxpayers through targeted tax deductions, credits, exclusions, or exemptions to attract private investment. Between 2005/06 and 2015/16, foregone revenue as a share of customs duty and taxes was on average 90 percent or 4 percent of gross domestic product (GDP). Although these incentives are meant to attract and stimulate private investment, there is a need to closely monitor and evaluate their benefits vis-à-vis the foregone revenue.

Although the financial sector has shown rapid expansion, the coverage is inadequate compared to the size of the country's population, with large unbanked population. Given that commercial banks and insurance companies are concentrated in cities and towns, the majority of rural population still have limited access to financial services. There is huge finance outside the formal financial sector. Between 2010/11 and 2015/16, currency outside banks grew on average by 14.5 percent, indicating a large potential to tap this finance for financing development activities.

Harnessing domestic private sector is crucial in speeding up the country's transformation process. However, the majority of domestic private investment projects registered with the federal and

regional offices have not been translated into actual investments as only a very small proportion of licensed projects have become operational. This requires close monitoring and follow up of licensed projects and facilitate their graduation from pre-implementation to implementation and operation phases.

Leveraging non-state resources through partnership with the private sector serves as an opportunity for the government to narrow the gaps caused by resource constraints. For instance, about USD 4 billion capital was raised in three PPP arrangements alone, namely, *Lebulu*, Addis Ababa Exhibition Center, and geothermal energy projects. However, the utilization public-private partnership in supporting development is limited despite existence of good practices in the country. Specific policy and legal framework governing PPP is yet to come, leading to an ad hoc undertaking of PP projects in the country. Implementation of PPPs has been a challenge due to weak technical and managerial capacity to execute PPP contractual arrangements, inadequate awareness about PPP, lack of specific legal frameworks, lack of a standardized PPP operating procedure, weak contract negotiation capacity, and financial constraints. There are ongoing efforts to establish PPP within the Ministry of Finance and Economic Cooperation, with a draft legal framework for PPP establishment has been prepared. The finalization of this legal framework helps establish a dedicated and functional institution for nurturing PPP to mobilize resources from the private sector. However, this needs to be followed by capacity building programme for public and private sector to successfully implement the PPP framework.

Private international finance sources, which include remittances and foreign direct investment, are important sources of development finance. International remittance forms the major share of development financing in Ethiopia, surpassing merchandise exports in recent years. The actual remittance inflows to Ethiopia could be higher than that reported by the National Bank of Ethiopia as people use informal ways of transferring money. The inflow of remittances could be enhanced through among others allowing additional operators to play a larger role in money transfers (e.g. microfinance institutions) and opening up bank branches or money transfer agents in areas where there is large concentration of Diaspora. Although the GTP-II recognizes the importance of remittance as a source of foreign exchange earnings, it does not explicitly address this with the same level of priority and does not provide any explicit operational linkages between national priorities.

Foreign direct investment (FDI) to Ethiopia increased sharply in the last 15 years, grew on average by about 29 percent per year between 2000 and 2015. However, FDI flows lack diversification across country of origin, with China, India, Turkey and others from Middle East account for a large proportion of FDI in Ethiopia.

Creating an enabling business environment in terms of stable and transparent regulatory systems, good investment climate and sound macro-economic and financial policies are essential to attract FDI in terms of both quality and diversity. However, Ethiopia's rank on ease of doing business deteriorated in 2017 (declined from 146 in 2016 to 159 in 2017). In particular, significant push is required in some specific ease of doing business indicators such as starting a business and getting credit. The country also performs badly in the World Bank's Logistics Performance Index (LPI) as its overall rank declined recently (deteriorated from 104<sup>th</sup> in 2014 to 126<sup>th</sup> in 2016). High logistics costs reduce the competitiveness of Ethiopian goods and services compared with its competitors. Cognizant of these problems, the government has initiated flagship programmes to curb the multiple problems constraining the private sector including Ethio-Djibouti railway project, integrated industrial development parks, and establishment of the Ethiopian Industrial Parks Development Corporation (IPDC). Rural transformation centers are also envisaged to accompany

integrated industrial parks. These grand initiatives are expected to attract private investment and boost private sector competitiveness.

Domestic resource mobilization effort is also hampered by illicit financial outflows. Studies indicate that the country loses on average USD 2.5 billion per year through illicit financial outflows. In particular, international trade through trade misinvoicing is a means of illicit financial outflows. The volume of illicit financial outflow through misinvoicing international trade transactions amounts to an average of USD 2 billion per year. In particular, import trade misinvoicing has remained the main driver of illicit financial outflows, while export under-invoicing is less of a concern.

Both grants and loans are important sources of development finance for Ethiopia, but grants as a share of GDP has shown a declining trend. Both grant commitment and disbursements declined in recent years, while loan commitment and disbursement improved, but the amount of loan disbursed fall short of commitments, indicating pledges have not been translated into actions. Ethiopia's disbursement rates for grants and loans have improved, from just 40 percent of commitments in 2010/11 to 67 percent in 2015/16. However, this still leaves a 33 percent shortfall of committed ODA that has not been used, due mainly to bottlenecks in the implementation of large infrastructure projects. This adversely affects the country's ability to repay its debt including the principal and interest (i.e. debt servicing), which in turn, depends on export performance. The present value of external debt to exports has been projected to be out of the threshold value of debt sustainability. However, the ongoing investments in transportation, power and other infrastructure, if completed on time, are, expected to enhance export competitiveness of the country which would help boost its capacity to repay its debt. Consultations with stakeholders indicate that there is a need to ensure effective utilization of external resources and improve project planning and management capacity to execute projects on time and with the required quality.

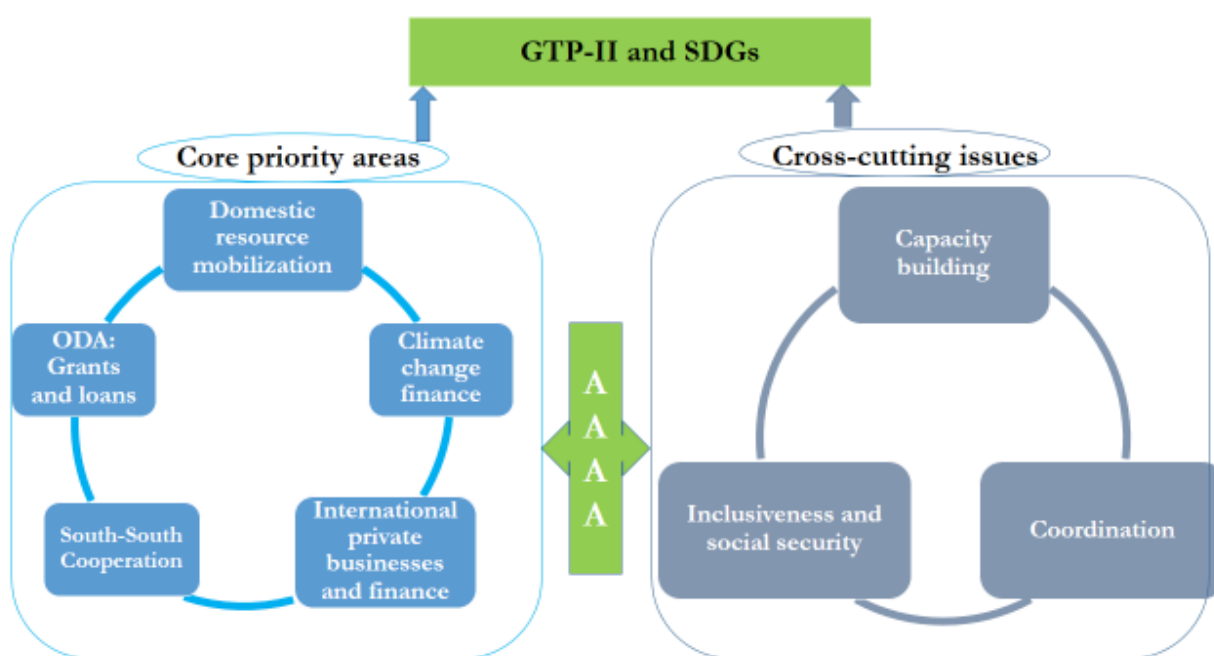
Despite robust economic growth in the past decades, generating employment for the expanding labour force has remained a challenge as reflected by high unemployment rate, especially in urban areas. Given the scale of unemployment in the country, a coordinated support is required to enhance youth employability through broad-based, inclusive, sustained growth, and productive and decent jobs. This requires a combination of growth enhancing interventions and social protection programmes. In particular, support in the expansion and growth of SMEs could help address the growing unemployment in the country through targeted interventions such as providing a more organized and handholding support in multiple fronts in the areas of finance, technology support, and continuous entrepreneurship training. This calls for establishing a dedicated finance institution catering the needs of SMEs or establishing a dedicated window for SMEs within the existing finance institutions, especially in commercial banks and Development Bank of Ethiopia.

Overall, the achievements of SDGs and GTP-II goals call for utilizing a combination of multiple sources and instruments of finance. Considering the revenue trends and the increasingly grim outlook for external resource inflows, there is a need to look for availability of potential 'non-traditional' financial resources that will help Ethiopia sustainably finance its development interventions. Additional financial resources can be tapped from climate funds (e.g. Green climate fund and adaptation fund), Diaspora bonds and social impact bonds, health and pension funds, public-private partnerships, charities and private foundations, and South-South cooperation (focusing on non-traditional development partners-China, India, Turkey, Brazil and countries in the Middle East). Among the list of non-traditional sources of finance, Diaspora and Social impact bonds, South-South cooperation and public-private partnership have high prospects to raise

significant amount of sustainable finance. Other sources such as blending arrangements, external borrowing, and insurance and pension funds can also hold promise of generating development finance, especially in the short and medium-term.

Based on detailed analysis of the different dimensions of the Addis Ababa Action Agenda, the national context, and regional and global perspectives, key priority areas has been identified which are grouped into two categories: Core and cross-cutting issues. These priority areas are building blocks of implementing the AAAA roadmap to achieve GTP-II and SDGs objectives. The core priority areas are anchored in five dimensions, while the cross-cutting issues are built around three dimensions. The individual dimensions that make up this roadmap are also supported by a matrix of interventions as well as monitoring and reporting mechanism.

**Figure E.1: Dimensions of the roadmap**



The details of individual dimensions that make up this roadmap are grouped around the following components.

**A. Core priority areas**

**Component 1: Enhance domestic resource mobilization:** Included in this components are enhancing domestic saving including both private and government savings through various instruments, raising domestic revenue through broaden the tax base, increase the tax coverage, reduce the costs of paying taxes and improve the enabling environment, introduce capital markets, and promote public-private partnerships (PPPs).

**Component 2: Attract international private business and finance:** with a focus on remittances and foreign direct investment (FDI). International remittances inflow can be facilitated by encouraging and allowing other institutions, such as post offices, cooperatives, microfinance institutions, or possibly telecom operators to play a larger role in money transfers and opening up bank branches or money transfer agents in areas where there is large concentration of Ethiopian

Diaspora, with certain incentives to reduce transfer fees. In addition to general improvement in business climate, strategic FDI marketing should specify concrete target countries and even companies for enhancing FDI diversification across countries and sectors. Fiscal incentives (such as tax exemptions and holidays) need to be attached to performance and monitored and evaluated on regular basis to ease fiscal burden on the government.

**Component 3: Maximizing ODA through enhanced cooperation:** Grants and loans tend to be volatile and pro-cyclical, as reflected by gaps between pledges and actual disbursements. Grant revenue has also been shrinking due to budget constraints in donor countries, indicating a need for tapping into new finance sources and instruments (e.g. blended finance) to complement domestic sources of financing. Development partners need to honor their Official Development Assistance (ODA) commitments in a timely and adequate manner, scale up their support in terms of capital, technology and capacity building. There is a need to improve allocation and disbursement of ODA through better management by MoFEC and line ministries. Manage the reduction in the time it takes to implement ODA projects through strengthening the monitoring and evaluation capacity of MoFEC, NPC and line ministries. There is also a need to improve effective utilization of external resources, improve project planning, and management capacity to execute projects on time and with the required quality. Strong domestic capacity needs to be built across sectors in project planning, management, monitoring, and contract administration.

**Component 4: Enhance South-South Cooperation (SSC):** There is a need to strengthen South-South Cooperation through bilateral, trilateral and interregional initiatives to support the country's development programmes. Currently, the scope and depth SSC is limited as a large share of SSC is originating from few countries and there is huge potential to leverage SSC. Efforts are also required to change composition of the financial linkages with SSC through designing projects with smart financing modalities (e.g. blended finance). There is also a need to diversify the quality of SSC by improving the current cooperation modality, facilitating regional integration and capturing more countries through bilateral negotiations. Developing a comprehensive database for SSC is required to effectively monitor and disseminate information to stakeholders.

**Component 5: Climate change finance:** The resource requirement for realization of addressing the climate change risks and the 2025 vision significantly exceeds the current capacity, which require additional resources to meet the envisaged targets. This requires tapping climate finance through bankable projects which in turn requires building strong local capacity in project preparation and negotiation. Specific interventions include support in the establishment project preparation fund within MoFEC, enhance coordination and harmonization of climate-related programmes from a variety of sources (public, private, community and non-governmental organization) to maximize synergies. Support is also required to comprehensively assess CRGE finance and investment needs, establish economy-wide baseline climate change relevant CRGE finance, and identify financing options. In addition, there is a need to develop a climate fiscal framework to track climate related financial flows and uses. Equally important is establishing a comprehensive database within MoFEC for tracking climate finance flows to Ethiopia and its uses.

## **B. Cross-cutting issues**

**Component 7: Strengthening capacity building** with a focus on improving good governance at all levels, strengthening and establishing a robust monitoring and evaluation (M&E) system, and human capacity development. At institutional level, there is a need to establish a well thought, forward looking and shared systems to accommodate current and future developments. This requires strengthening a

robust monitoring and evaluation (M&E) system at all levels (e.g. establishing a function M&E unit and developing monitoring and evaluation policy and guidelines). While there is an M&E framework for physical activities in GTP-II, there is no M&E for tracking financial targets under GTP-II, indicating the need for developing financial M&E and ensure its alignment with national development plan.

**Enhance coordination mechanism:** There is a need to strengthen inter-sector policy coordination through providing policy and legislative guidance for effective implementation, monitoring, evaluation and reporting. In particular, a strong coordination architecture is crucial to harmonize different development programmes, reduce duplication of efforts and enhance synergies across programmes. The current a three level dialogue Architecture between the government of Ethiopia and development partners can serve an entry point for enhancing coordination among development partners, sectors and the government. In this regard, strong monitoring and evaluation system shall be in place at all levels to enhance coordination and alignment of programmes, improve accountability, and to inform policy, planning, and programme development as well as budgeting decisions. In addition, efforts should be made to strengthen statistical capacity and improve the quality and timeliness of statistical data.

**Improve inclusiveness and social services:** Improvements in public service delivery system, including employment, education and health care, and ensure equal access to basic public services continue to be the primary focus of the country. In particular, promoting SMEs is crucial to ensure inclusiveness, especially as a means of employment creation for the growing labor force. SMEs are constrained by multiple problems including credit, market, technology, etc. The existing commercial banks don't have a special window for SMEs services nor are there specialized financial institution to cater the needs of SMEs. This calls for promoting SMEs through improving access to warehouses, relaxing credit constraints, and improving the macroeconomic and regulatory environment, the potential for SMEs for creating more jobs will be severely compromised. Key interventions include provide inclusive assistance for new businesses and encourage job creation through expansions and growth of small and medium enterprises (SMEs), and improve access and quality of education for all and at all levels. In addition, enhance social protection and security through expanding the coverage of social security, strengthening quality basic healthcare services. These interventions require substantial resources, strong coordination and alignment of programmes from different stakeholders to achieve the desired targets.

## 1. The context

### 1.1 Background

The Ethiopian government has increasingly become aware of and better informed about sustainable development (SD) more than a decade or so ago. The Supreme law of the land (or the Constitution) of the Federal Democratic Republic of Ethiopia (FDRE), which was enacted more than two decades ago, recognizes the importance of sustainable development. Guided by the principles of the supreme law of the land, the government of Ethiopia has made enormous strides in articulating sustainable development in its development policies, strategies and plans. National policies, strategies, plans and programs are geared towards achieving sustainable development and eradicating poverty.

Ethiopia is committed to address the many acute and co-mingled economic, social and environmental issues which stand in the way of sustainable development, the greening of the economy and improvements in human wellbeing, quality of life and happiness. It has set out very ambitious goals to achieve economic, social and environmental transformation and achieve a lower middle income status by 2025. Economic goals include raising productivity in agriculture, improving social services, promoting industrial development, and filling significant infrastructural gaps in power, transportation (both road and railway) and telecommunications. In doing so, the Government of Ethiopia has determined to deepen and enhance rapid growth and structural transformation, with net-zero GHG emission growth trajectory, while simultaneously building the resilience of the economy to climate shocks. The main planning instruments are a series of development plans including the first generation Growth and Transformation Plan (GTP-I) (2010/11-2014/15) (MoFED, 2010) and the second generation of Growth and Transformation Plan (GTP-II) (2015/16-2019/20) (NPC, 2015). Most of the measures mandated under the GTP-I and II require huge public sector fiscal resources (either in terms of spending requirements or the foregoing of revenue in the case of incentives).<sup>1</sup>

In 2015, the global community made three major international and transformative agreements including the Addis Ababa Action Agenda (AAAA) (or Addis Agenda) on Financing for Development (FfD), the 2030 Agenda for Sustainable Development (or sustainable development goals), and the Paris Agreement on Climate Change (Khan, 2016; OECD, 2016). The Government of Ethiopia has renewed its commitment to ensure the effective implementation and achievement of these agreements. The realization of the sustainable development goals (SDGs) and targets crucially depends on the effective implementation of the Addis Ababa Action Agenda (AAAA) and the Government of Ethiopia has adopted various aspects and principles of the AAAA in its national strategies to ensure the mobilization of the various means of implementation required for the achievement of SDGs.

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<sup>1</sup> Framed in terms of the developmental state model, the GTP-I draws on a wide range of tools requiring Government spending, including: targeted financial support (subsidies, bank loans, and equity participation); tariff exemptions for production inputs; tax incentives, including tax holidays, partial profit exemptions, and free trade zones to attract FDI and to promote priority sectors, particularly those facing handicaps such as inadequate specific infrastructure; strategic government procurement (e.g. assured profit margins for domestic pharmaceutical manufacturers in government health-care procurement); publicly financed infrastructure, particularly power, telecommunications and transportation, both internal expansion of the road and rail network and improving the trade corridors; and the creation of public corporations.

Reflecting the country's commitment to national, regional and global goals, Ethiopia has mainstreamed both SDGs and the climate resilient green economy (CRGE) strategy into its second generation growth and transformation plan (GTP-II). This ensures that SDGs and CRGE initiative are part of a comprehensive national plan for public investments as well as the legal and institutional reforms necessary to create an enabling environment for private sector and community engagement. It also provides essential prominence to measures designed to promote the three dimensions of sustainable development: economic, social and environment. As indicated in the CRGE strategy, Ethiopia requires expenditure of over USD150 billion in order to realize its vision of building a low-carbon and climate resilient a lower middle income country status by 2025. In other words, Ethiopia should invest over USD7.5 billion annually to make the economy climate smart and ensure the sustainability of economic growth.<sup>2</sup> This indicates that realizing SDGs requires much more resources than that indicated in the CRGE strategy and this calls for the need to identify current and future financing mechanisms for delivering SDGs. Implementing SDGs requires both significant increases in resources and changes in the way existing resources are used and prioritized, calling for more effective integrated approaches to managing public and private finance to achieve sustainable development.

The challenge, then, is how to mobilize and channel finance and technology towards sustainable development. A major task for policy-makers in financing SDGs is to devise financing solutions to attract and direct investments to areas where greater co-benefits and multiplier effects can be achieved.<sup>3</sup> A diverse financing “tool-box” may provide the country with new opportunities to leverage additional public and private resources for financing sustainable development and managing its vulnerability to climate change. This financing mechanisms need to be tailored to the specific needs and characteristics of the country. Of course, the extent of utilization of these financing instruments depends on country's capacity to use and manage these resources effectively to finance sustainable development and manage risks.

Following the adoption of the AAAA, development of a strong follow-up and review mechanism remains a high priority. At the 17<sup>th</sup> High Level Forum between the Government of Ethiopia and the Development Assistance Group (DAG), the Government of Ethiopia called for a joint action to implement the Addis Agenda for the achievement of the SDGs through its subsequent national development plans. To this end, the Forum agreed to jointly prepare a roadmap identifying actions to be taken by the GoE and its development partners to realize the country's national development plan through the effective implementation of the AAAA. The development of an integrated national financing strategy (INFS) is a key recommendation from the Addis Abba Action Agenda. Such strategy captures a diversity of financial flows, including both domestic and foreign sources of funding.

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<sup>2</sup> This USD 150 billion expenditure doesn't include the climate change resilience building requirements of specific sectors of the economy. According to the Climate Resilience Strategy of Ministry of Water, Irrigation and Electricity, it is anticipated that the sector requires about USD 895 million for climate resilience building actions. The climate change resilience building resource requirement of the Agriculture and Forest sector has been estimated at USD 1508 million.

<sup>3</sup>The Istanbul Programme of Action (IPoA) for the LDCs charts the international community's vision for the sustainable development of the LDCs for the decade 2011-2020. The IPoA also recognizes that the lack of access to financial resources represents one of the biggest development constraints facing LDCs.



## 1.2 Objectives

The overall objective of the study is to develop a comprehensive roadmap for the implementation of the Addis Agenda to be implemented by the government, members of DAG and other stakeholders. Using the Development Assessment Framework (DFA) as guide, this study intends to assess recent trends in development finance flows including public and private flows, external and domestic flows and examine policies and institutional capacity in government to manage such flows in a more coherent, complementary, and catalytic way. By doing so, the roadmap also intends to provide a framework that includes strategic partnerships for the mobilization and employment of ‘*New and Additional*’ resources for the achievement of the Sustainable Development Goals (SDGs) through Ethiopia’s second Growth and Transformation Plan (GTP-II).

The specific objectives include:

- Identify critical and immediate action to be taken by GoE and its development partners to implement AAAA ensuring ‘*new and additional*’ means of implementation for the SDGs during the GTP-II period,
- Assess opportunities and challenges for Ethiopia and its partners in the mobilization of ‘*new and additional*’ means of implementation for the SDGs as called for in the AAAA, and
- Define a coherent mechanism for the monitoring and reporting of the AAAA that could feed into the annual report of the global inter-agency workforce on the implementation of AAAA.

## 1.3 Methodology and Approach

### 1.3.1 Overall analytical approach

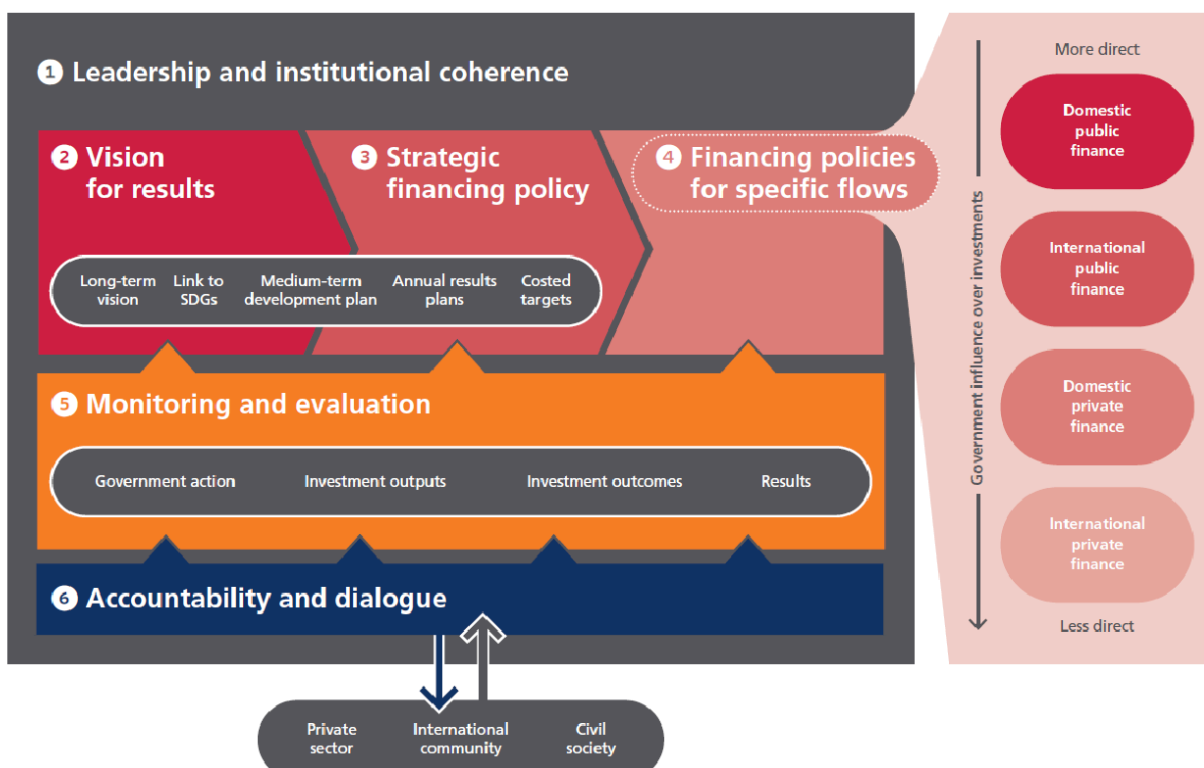
The overall methodological approach is based on the Development Finance Assessment (DFA) framework which requires a comprehensive mapping of past and current sources of development finance. The DFA framework provide an understanding of the potential sources of resources including domestic and external resources needed for implementing development initiatives (Figure 1). Domestic resources include public sources such as tax and non-tax revenue, and domestic private sources such as domestic private investment and domestic philanthropic organizations, while the external resources include official development assistance (ODA), climate finance and South-South cooperation (SSC) and external private sources (e.g. FDI and remittances).

In addition, the DFA framework includes an assessment of relevant policies, institutional arrangements, technical systems and tools and human resource capacity to mobilize, manage, deliver, monitor and report on existing and future flows, together with recommendations on the way forward.

A successful implementation of the Addis Agenda also depends on whether or not government is taking ownership for developing innovative policy frameworks as well as on a meaningful involvement and engagement of stakeholders from the private sector and civil society. In this regard, the framework helps to answer the following questions. Who are the key actors? And what is the balance between different forms of finance (e.g. public versus private resources? How does the sectoral composition of finance look like? The findings and recommendations of the DFA are also expected to inform the implementation of the GTP-II and will also inform the Development

Cooperation strategy, as well as the institutional arrangements necessary to implement the cooperation. Note that the Development Finance Assessment (DFA) provides both the baseline and the road map for implementing reforms needed for adopting and implementing an integrated national financing framework.

Figure 1: Development Finance Assessment (DFA) tool as an integrated financing framework



Source: AP-DEF and UNDP (2016)

Five strands of work are of particular relevance for the analysis: (i) Review of reports on Addis Agenda monitoring commitments and actions<sup>4</sup>; (ii) The UNDESA Briefing Note on AAAA<sup>5</sup>; (iii) recent research work on *financing the post-2015 sustainable development goals* (SDGs)<sup>6</sup>; (iv) recent research works on development finance framework<sup>7</sup>; *Country case study on integrated financing strategy*<sup>8</sup>; and (v) Government plans such as Growth Transformation Plan (GTP-II) and its policy matrix as well as other relevant strategies including the CRGE Strategy.

In analytical terms, the study is subdivided into five *analytical components*: (i) a general review of the Addis Agenda and SDGs (the ‘Review of Addis Agenda and SDGs’); (ii) a review of national policies, strategies, plans and institutional arrangements (‘Review of national policies, strategies, plans and institutions’); (iii) analysis of regional and global policies, strategies and plans related to the Addis

<sup>4</sup>UN (2016), *Addis Ababa Action Agenda commitments and actions*, Inaugural Report 2016, Inter-agency Task Force on Financing for Development.

<sup>5</sup>UNDESA (2016), *Financing sustainable development and developing sustainable finance: A DESA Briefing Note on the Addis Ababa Action Agenda*.

<sup>6</sup>Kharas, H., Prizzon, A. and Rogerson, A. (2014), *Financing the post-2015 sustainable development goals* (SDGs), Overseas Development Institute (ODI), UK.

<sup>7</sup>AP-DEF and UNDP (2016), *Achieving sustainable development goals in the era of the Addis Ababa Action Agenda: Progress on establishing integrated national financing frameworks in the Asia-Pacific region*.

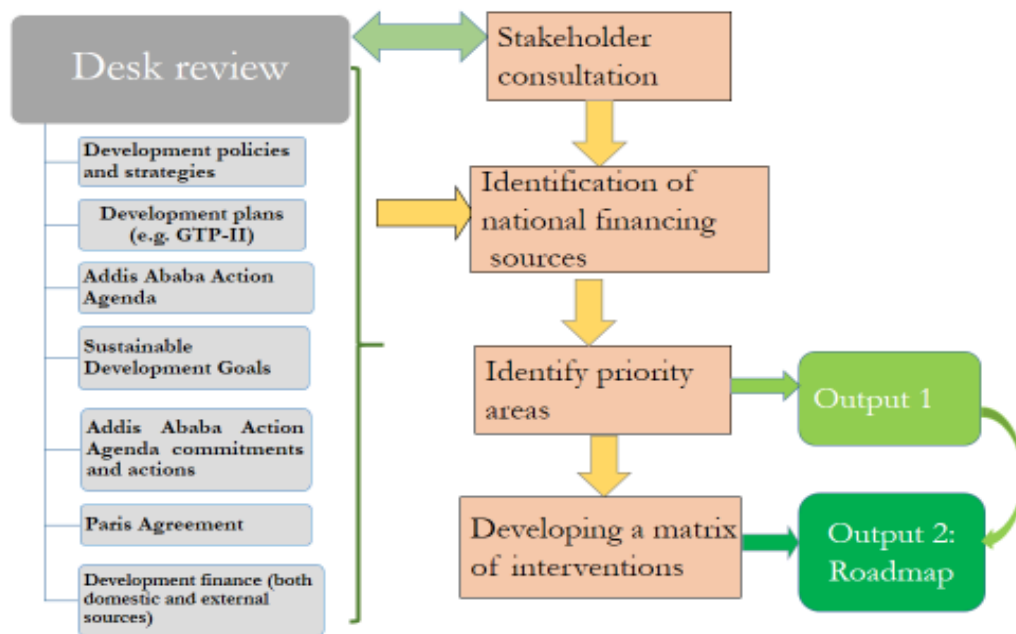
<sup>8</sup>Bjornestad, L., Hossain, J., Sinha, J. and Stratta, N. (2016), *Strengthening Finance for the 7th Five Year Plan and SDGs in Bangladesh: Findings from an Independent Development Finance Assessment*; UN, EU and Ministry of Planning and Investment of Viet Nam (2014), *Development Finance for sustainable development goals in the middle income Viet Nam: Financing Viet Nam’s Development: meeting the new challenges*.

Agenda (‘Review of regional and global policies, strategies and plans’); and (iv) assessment of domestic and external development financing strategies (‘Assessment of development finance’); (v) identification of priority areas and development of a matrix of interventions (‘Priority areas and matrix of interventions’).

### 1.3.2 Operational framework

From an operational point of view, the study is supported by a two pronged approach consisting of (i) desk review, aimed at reviewing relevant literature and consolidating the available information from secondary sources, (ii) stakeholder consultations, including government, private sector, development partners (including UN and DAG) and others such as bilateral development partners. Figure 2 presents a sequence of the operational framework used in this study.

Figure 2: Operational framework



Source: Own construction

## 2. An overview of the Addis Ababa Action Agenda

### 2.1 From Monterrey to Doha

The first international conference on Financing for Development, which was held in Monterrey, Mexico, in March 2002, marked a global consensus on forging partnership for financing sustainable development. The Monterrey Consensus addressed, at least in principle, the challenges of financing for development aimed at eradicating poverty, achieve sustained economic growth and promote sustainable development (UN, 2002, 2009). The Monterrey Consensus recognized the crucial role of all sources of financing for development including public and private, domestic and international, and this requires public policies and enhanced national and international enabling environment for resource mobilization (UN, 2016; Khan, 2016). Subsequently, the second international conference on Financing for Development was held in Doha, Qatar, in December 2008. The Doha Declaration was intended to achieve the objectives of the Monterrey Consensus through more concrete commitments.

A holistic approach is rooted in the FfD process, embodied in the 2002 Monterrey Consensus and the 2008 Doha Declaration on Financing for Development. Domestic policies need to be supported by an enabling international environment. Both national policies and regulations and international rules and agreements are thus linked to development finance and outcomes. The global partnerships for development emphasizes the central importance of development cooperation and concessional financing. Indeed, development cooperation, and the fora, remain a crucial part of the agenda. Although science, technology, innovation and capacity building had been part of the Monterrey Consensus and Doha Declaration on FfD, they lacked details regarding financing sustainable development including emerging issues.

### 2.2 From Monterrey to Addis Ababa: The Addis Ababa Action Agenda (AAAA)

The Heads of States, High Representatives and other global development community gathered in Addis Ababa for the Third International Conference on Financing for Development (FfD) in July 2015 and adopted the Addis Ababa Action Agenda (AAAA)<sup>9</sup> (or Addis Agenda) (UN, 2015a). The Addis Ababa conference on FfD was intended to assess the progress made in the implementation of the Monterrey Consensus and the Doha Declaration, address new and emerging issues on development financing, and strengthen the financing for development follow-up process (Khan, 2016). The Addis Agenda provides a holistic and coherent framework for financing sustainable development. In particular, the Addis Agenda is the intergovernmental-negotiated outcome document on mobilizing financial and technical resources for development from an increased number of actors to support the implementation of Sustainable Development Goals (SDGs) covering the period 2016-2030.

The Addis Agenda also consists of concrete actions that Member States of the United Nations pledged to undertake individually and collectively. Building on Monterrey and Doha Declarations, the Addis Agenda reaffirms that developing countries have primary responsibility for their own economic and social development. National sustainable development strategies are thus a core

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<sup>9</sup>The Addis Ababa Action Agenda is the outcome of the Third International Conference on Financing for Development, which took place in Addis Ababa, Ethiopia, in July 2015 (see the General Assembly resolution 69/313).

element of the Addis Agenda. The Addis Agenda sets out an ambitious agenda for raising the necessary resources to achieve an equally ambitious the 2030 Agenda including SDGs (Karoubi *et al.*, 2016). It should be noted that SDGs go beyond poverty reduction and now include targets in industrialization, employment, and economic growth and infrastructure development.

The Addis Agenda explicitly incorporates major non-financial means of implementation for delivering sustainable development along with the more traditional financial means, complementing and contextualizing them in a comprehensive framework. The Addis Agenda goes beyond Monterrey and Doha outcomes by taking into account policy requirements for realizing all the three dimensions of sustainable development (i.e. economic, social and environmental) in an integrated manner. It emphasizes the importance of incentives for private sector investment, as well as the quality of investment. It also focuses on sustainable consumption and production patterns globally. In doing so, it brings issues such as climate finance, protection of oceans and forests, and other environmental concerns, and incorporates these into the Monterrey global coherence agenda, along with issues of trade and global financial stability.

The Addis Agenda aims to mobilize public finance, set appropriate public policies and regulatory frameworks to unlock private finance, trade opportunities and technological development, and incentivize changes in consumption, production and investment patterns. It further seeks to align all resource flows and policies with economic, social and environmental priorities.

The commitments and action items in the Addis Agenda are organized in seven main action areas including issues on data, monitoring and follow-up (see Box 1). Member States also identified a number of cross-cutting thematic areas where policy actions harness the synergies that exist between many of the specific action items elaborated in the Addis Agenda.<sup>10</sup>

**Box 1: Action areas of the Addis Ababa Action Agenda**

- (i) Domestic public resources,
- (ii) Domestic and international private business and finance,
- (iii) International development cooperation,
- (iv) International trade as an engine for development,
- (v) Debt and debt sustainability,
- (vi) Addressing systemic issues, and
- (vii) Science, technology, innovation and capacity building

The Addis Agenda also includes several new commitments and initiatives including (UN, 2015):

- A new social compact to provide social protection and essential public services for all,
- A global infrastructure forum to bridge the infrastructure gap,
- An ‘LDC package’ to support the poorest countries,
- A Technology Facilitation Mechanism to advance to the SDGs,
- Enhanced international tax cooperation to assist in raising resources domestically, and
- Mainstreaming women’s empowerment into financing for development

Overall, the Addis Agenda provides guidance on three major areas. First, it provides a comprehensive set of policy actions by Member States, with a package of concrete measures to finance sustainable development, transform the global economy and achieve sustainable development goals. Second, it serves as a new global framework for financing sustainable

<sup>10</sup> On list of cross-cutting issues see UN (2015) and General Assembly resolution 69/313 of 27 July 2015.

development that aligns all financing flows and policies with economic, social and environmental priorities and ensures that financing is stable and sustainable. Third, unlike previous declarations, the Addis Agenda contains provisions for supporting Least Developed Countries (LDCs).

### **3. Development policies, strategies and plans and sustainable development frameworks**

This section provides pertinent analytical information on national and international development policies, strategies and plans. First, it looks at the global and regional development perspectives in the context of sustainable development, with a focus on current frameworks such as SDGs and Agenda 2063. The second part reviews the national context in terms of policies, strategies and plans. This is followed by assessing the linkage between SDGs and national development plans (i.e. GTP-II).

#### **3.1 Review international policies and strategies and initiatives/programs**

##### **3.1.1 Global sustainable development frameworks: The 2030 Agenda**

Although the transition from MDGs to SDGs needs to address particular opportunities and challenges of different national and local contexts, a number of key characteristics of sustainable development can be identified (GEC, 2012; OECD, 2012): economic growth, environment sustainability and social development. Despite some achievements under MDGs, significant challenges remain. The key lesson under MDGs is that there is a need to look beyond narrow economic and social measures of progress to consider all aspects of well-being and sustainable development.

On September 25, 2015, world leaders gathered in New York and adopted the Sustainable Development Goals (SDGs), which is a universal and transformative global development agenda (or the 2030 Agenda). The Sustainable Development Goals (SDGs) that succeeded the Millennium Development Goals (MDGs) are an integrated and indivisible set of global priorities that incorporate economic, social and environmental aspects and recognize their inter-linkages in achieving sustainable development (United Nations Development Group, 2015). The 2030 Agenda for Sustainable Development recognizes collaborative partnerships, and provides a useful universal framework to strengthen collective action towards common goals. The multi-sectoral and cross-cutting nature of sustainable development as well as the need to achieve a better balance between its diverse dimensions calls for policy coherence and integration.

The Rio+20 national preparations underscored the need for more coherent planning and decision-making at and between the national, sub-national, and local levels of government as well as across thematic sectors to meet SDGs. Unlike MDGs, SDGs are universal goals that apply to every nation (not just developing countries). In particular, SDGs consist of more goals (17) and targets (169) which balance the three dimensions of sustainable development compared with MDGs (Box 1). For each goal and target area, relevant indicators are developed to track progress; SDGs consist of about 230 indicators.

The Sustainable Development Goal 17 “Strengthen the means of implementation and revitalize the global partnership for sustainable development” includes “Institutional and Policy Coherence” as an integral part of the Means of Implementation (MoI). It also includes a cross-cutting target to “enhance policy coherence for sustainable development” which apply to the whole SDG framework (OECD, 2015). In achieving this target, governments need to ensure that their policies in all public domains are consistent with, and do not undermine the achievement of sustainable development goals.



<b>Box 1: Sustainable Development Goals</b>	
<b>Goal 1</b>	End poverty in all its forms everywhere
<b>Goal 2</b>	End hunger, achieve food security and improved nutrition and promote sustainable agriculture
<b>Goal 3</b>	Ensure healthy lives and promote well-being for all at all ages
<b>Goal 4</b>	Ensure inclusive and equitable quality education and promote lifelong learning opportunities for all
<b>Goal 5</b>	Achieve gender equality and empower all women and girls
<b>Goal 6</b>	Ensure availability and sustainable management of water and sanitation for all
<b>Goal 7</b>	Ensure access to affordable, reliable, sustainable and modern energy for all
<b>Goal 8</b>	Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all
<b>Goal 9</b>	Build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation
<b>Goal 10</b>	Reduce inequality within and among countries
<b>Goal 11</b>	Make cities and human settlements inclusive, safe, resilient and sustainable
<b>Goal 12</b>	Ensure sustainable consumption and production patterns
<b>Goal 13</b>	Take urgent action to combat climate change and its impacts <sup>11*</sup>
<b>Goal 14</b>	Conserve and sustainably use the oceans, seas and marine resources for sustainable development
<b>Goal 15</b>	Protect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification, and halt and reverse land degradation and halt biodiversity loss
<b>Goal 16</b>	Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels
<b>Goal 17</b>	Strengthen the means of implementation and revitalize the global partnership for sustainable development
	Source: UN (2015)

**3.1.2 Regional sustainable development frameworks: Agenda 2063**

African member states prioritized structural transformation as reflected in the continent’s blueprint for development (Agenda 2063) and the 2030 Agenda. The Common African Position (CAP) on the Post 2015 development agenda articulated the continent’s priorities for the global agenda and served as a unifying voice for the continent in the intergovernmental negotiations that culminated in the adoption of the Post 2015 development agenda in 2015. The sustainable development goals (SDGs) and Agenda 2063 provide the global and regional enabling environment required for Africa’s transformation, while agenda 2063 reflects the totality of Africa’s development priorities including region-specific transboundary priorities. Nevertheless, a shared objective of Agenda 2063 and the SDGs is the achievement of structural transformation underpinned by sustainable development in all its dimensions: economic, social and environmental. Implementing Agenda 2030 involves taking “transformational” actions that redirect investment flows within and across sectors.

The 2030 Agenda presents a unique opportunity for Africa in general and Ethiopia in particular in its effort for pursuing structural economic transformation for inclusive and people centred

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<sup>11</sup> Acknowledging that the United Nations Convention on Climate Change is the primary international, intergovernmental forum for negotiating the global response to climate change.

development (Africa Union Commission, 2015). This requires building productive capacities, especially in the areas of infrastructure, agriculture, industrial and services sectors development, science technology and innovation, value addition, youth development and engagement, women's empowerment, and sustainable natural resource management. It also requires addressing the challenges posed by climate change (e.g. desertification, land degradation, drought and loss of biodiversity), promoting peace and security, and implementing a responsive and accountable global governance architecture through, *inter alia*, the full and equitable representation of African countries in the international financial and economic institutions. Thus, there is a need to align Africa's development priorities with the global development agenda and the latter need to be customized to the context of Africa.

As indicated in the Common Africa Position (CAP), Africa's development priorities have been grouped into six pillars (Africa Union Commission, 2015): (i) structural economic transformation and inclusive growth; (ii) science, technology and innovation; (iii) people-centred development; (iv) environmental sustainability natural resources management, and disaster risk management; (v) peace and security; and (vi) finance and partnerships.

Agenda 2063, which is rooted in Pan Africanism and African Renaissance, provides a framework for addressing past injustices and the realization of the 21st Century as the African Century. The agenda 2063 is based on the Pan Africa vision of “*an integrated, prosperous and peaceful Africa, driven by its own citizens and representing a dynamic force in the international arena*” (Africa Union Commission, 2015). Agenda 2063 consists of seven aspirations, 20 goals, 39 priority areas, 256 targets and 248 indicators, while SDGs include 17 goals, 169 targets and 231 indicators. It appears that Agenda 2063 is more comprehensive than that of SDGs.

**Box 2: The African We Want Aspirations**

1. A prosperous Africa based on inclusive growth and sustainable development
2. An integrated continent, politically united and based on the ideals of Pan-Africanism and the vision of Africa's Renaissance
3. An Africa of good governance, democracy, respect for human rights, justice and the rule of law
4. A peaceful and secure Africa
5. An Africa with a strong cultural identity, common heritage, shared values and ethics
6. An Africa whose development is people-driven, relying on the potential of African people, especially its women and youth, and caring for children
7. Africa as a strong, united and influential global player and partner

Source: Africa Union Commission (2015)

### **3.2 Review of national development policies, strategies and plans**

#### **3.2.1 The Constitutional framework**

Ethiopia is multiethnic, multilingual and multicultural nation and officially named the Federal Democratic Republic of Ethiopia which comprises nine member states and two city administrations. The Constitution of the Federal Democratic Republic of Ethiopia (FDRE) is the supreme law of the land (FDRE, 1995).

The overriding objective of the government of Ethiopia is poverty eradication and sustainable development. For Ethiopia, lasting peace, political stability, democracy and good governance are fundamental conditions to achieve poverty eradication and sustainable development agenda. The context for sustainable development, planning, and implementation in Ethiopia has been framed in the supreme law of the land by the Nations, Nationalities and Peoples of Ethiopia. Guided by the principles of the supreme law of the land (i.e. the Constitution), all national policies, strategies, plans

and programmes are geared towards achieving sustainable development and eradicating poverty. The Constitution of the FDRE provides power to the Federal Government to formulate and implement national policies, strategies and plans in respect to overall economic, social and development matters. This ensures vertical consistency as regional governments follow the national development policy as a guiding framework and customize with their own context. In particular, the following are important provisions of the constitution:

- People have the right to improved living standards and to sustainable development,
- People have the right to full consultation and to the expression of views in the planning and implementations of environmental policies and projects that affect them directly,
- The people and the state have common responsibility/obligation to protect the environment
- The state endeavors to ensure all people live in a clean and healthy environment, and
- The state shall ensure that the design and implementation of development projects will not damage or destroy the environment.

Thus the supreme law of the land contains provisions which serve as a major springboard for subsequent legislations in the management of environment, as well as for mainstreaming environmental sustainability in the political, social and economic development sectors. Accordingly, any organ of the government shall in the formulation and implementation of development policies, strategies, plans and programs be guided by the constitutional principles.

### **3.2.2 The National Vision and Development Policy**

The National Development Policy of the FDRE is to build a market-oriented economy with the following objectives:

- Enhance the participation of all Ethiopian peoples both in the process and outcome,
- Ensure food security,
- Attain sustained economic growth and social development, and
- Ensure environmental sustainability.

Ethiopia's vision is:

“to become a country where democratic rule, good-governance and social justice reign, upon the involvement and free will of its peoples, and once extricating itself from poverty to reach the level of a middle-income economy as of 2025” (MoFED, 2010:21).

The country's long-term economic vision is:

“building an economy which has a modern and productive agricultural sector with enhanced technology and an industrial sector that plays a leading role in the economy, sustaining economic development and securing social justice and increasing per capita income of the citizens so as to reach the level of those in middle-income countries” (MoFED, 2010:21).

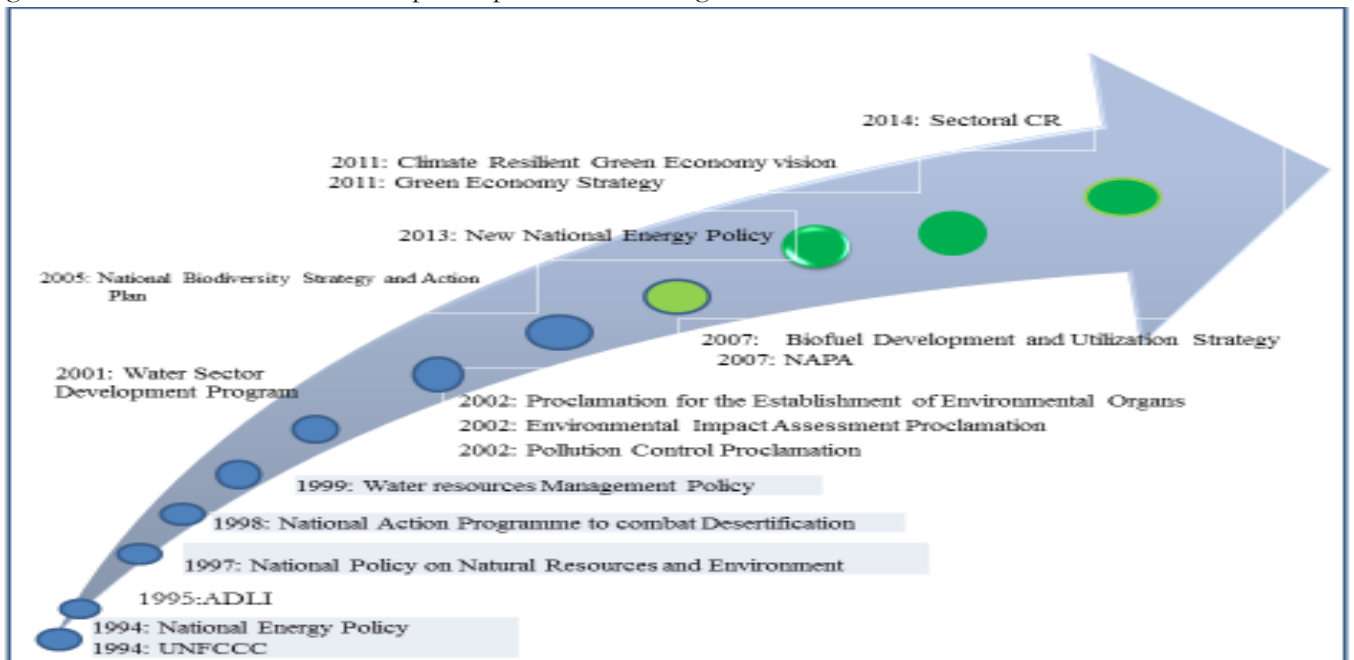
### **3.2.3 Development strategies**

Ethiopia has been a champion of sustainable development (SD) paradigm as reflected in landmark of SD-related policies and initiatives since the early 1990s (Figure 3). Agricultural Development Led Industrialization (ADLI) is a National Development Strategy that aims to achieve initial industrialization through robust agricultural growth and establishes close linkage between the agricultural and the industrial sectors (Walleligne, 2015). It envisages an economically transformed society within which agriculture will grow rapidly and sustainably and provides long-term

development framework for economic transformation. ADLI focuses on poverty reduction and sustainable development and gears towards sustainable use of the country’s resources such as land and water. ADLI is the basis of all sectoral development strategies and plans.

On the environmental front, the process of greening Ethiopia’s economy started as early as the 1990s. The introduction of regulations to manage pollution from the palm oil industry was one of the first greening steps taken by the government. The step-wise greening approach thus far, consisted of the formulation of supporting policies, mainly at sectoral level, for the transition to the green economy. To date, the most comprehensive and consolidated green economy framework is the Climate Resilient Green Economy (CRGE) Strategy (FDRE, 2011).

Figure 3: Evolution of sectoral development policies and strategies

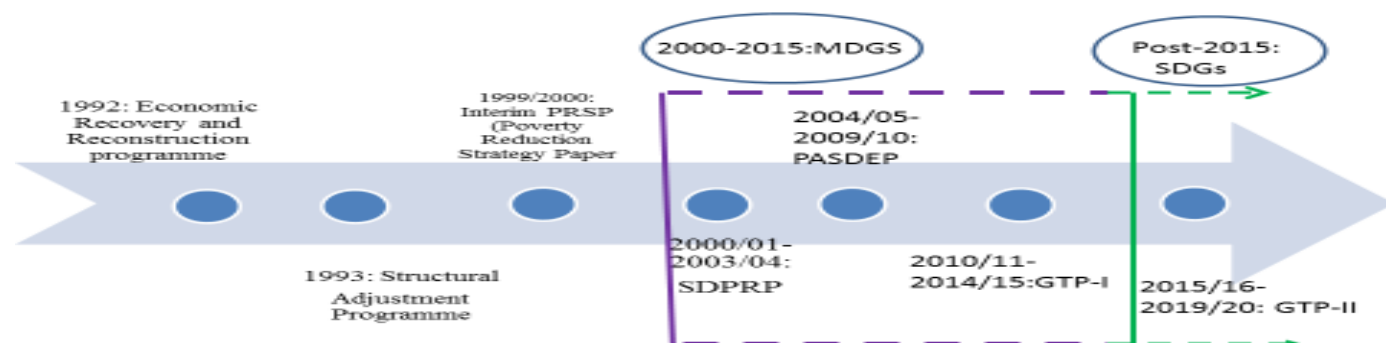


Source: UNECA (2015)

### 3.2.4 Development plans

The review of the macroeconomic environment follows the chronological order of development programs, strategies and policies since 1991. The various development plans and programmes include Emergency Recovery and Reconstruction Program (ERRP), Structural Adjustment Programme (SAP), and Poverty Reduction Strategy Papers (PRSPs) which have all substantial implications for sustainable development and rural resilience building. In particular, the PRSPs include interim PRSP plan, Sustainable Development and Poverty Reduction Plan (SDPRP), Plan for Accelerated and Sustainable Development to End Poverty (PASDEP), and Growth and Transformation Plans (GTP I and II).

Figure 4: Timelines of development plans



Source: Own construction

### 3.2.4.1 An overview of GTP-II and key priority areas

Ethiopia has prepared and is implementing the second growth and transformation plan (GTP-II) (2015/16-2019/20). This planning horizon coincides with end of MDGs and the beginning of SDGs. GTP-II takes into account national, regional and global perspectives including the following.

- The country's vision
- National Development Policies and Strategies
- Lessons from GTP-I
- Regional circumstances and outlook such as Common Africa Position and Agenda 2063
  - Global situations (e.g. Post-2015 development agenda such as SDGs and Global economic outlook)

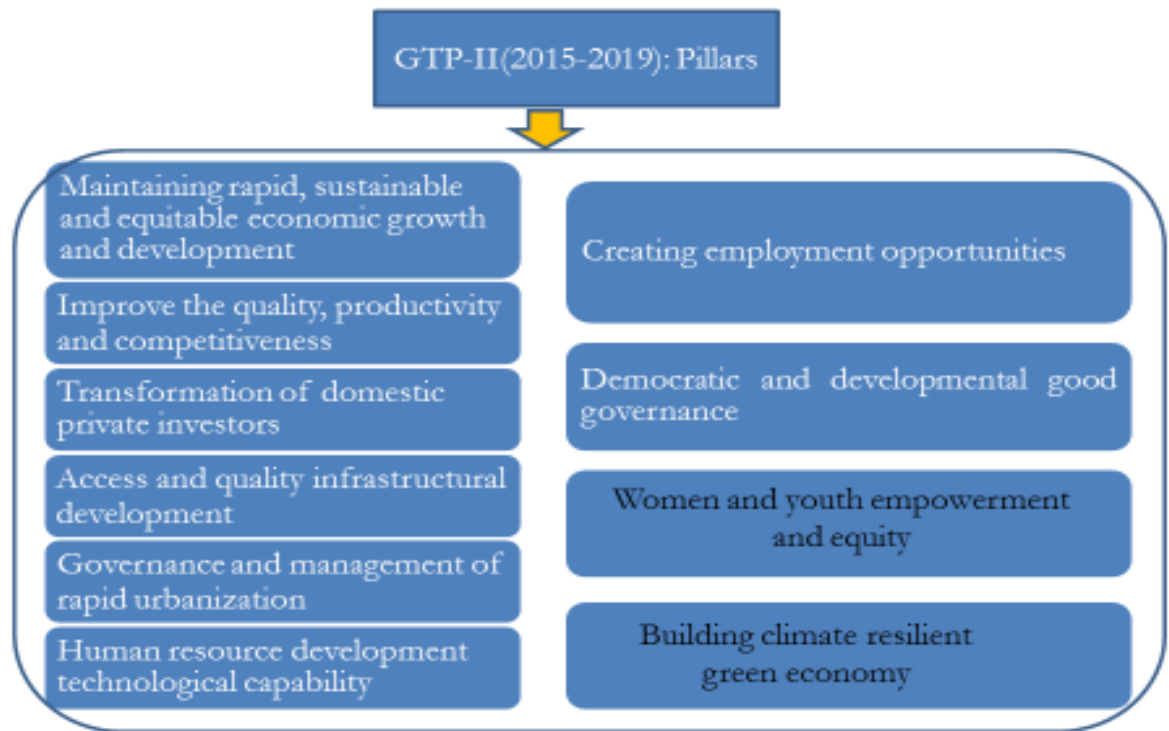
The main objective of GTP-II is to achieve the national vision of becoming a lower middle-income country by 2025. Specifically, GTP-II has the following objectives.

- Maintain at least an average real GDP growth rate of 11 percent in a stable macroeconomic environment;
- Develop the domestic engineering fabrication capacity and improve productivity, quality, and competitiveness of the domestic productive sectors to speed up structural transformation;
- Strengthen and develop existing infrastructures for social mobilization/developmental army to render citizens become owners of the development process and ultimately benefit from the outcomes; and
- Deepen developmental political economy by strengthening a stable democratic developmental state.

The second Growth and Transformation Plan consists of nine strategic pillars (Figure 5). The key departure of GTP-II from its predecessor (GTP-I) is the explicit focus on manufacturing industry, inclusion of the green economy and of SDGs to achieve sustainable structural transformation. Based

on the experience gained from the GTP-II-CRGE strategy integration, Ethiopia contextualizes relevant SDGs into its five-year development plan (i.e. GTP-II). In Ethiopia, the economy-wide integration of SDGs occurs both at macroeconomic and sectoral levels to ensure that adequate SDGs indicators and targets are included at both levels. Matching exercise between GTP-II and SDGs indicate that about 39.1 percent and 43.2 percent of SDGs targets have been fully and partially reflected in GTP-II, respectively.<sup>12</sup> Only 17.8 percent of SDGs targets do not have the corresponding targets in GTP-II, indicating that the Ethiopian five year development plan captures well SDGs targets. Similarly, about 43.3 percent of SDGs indicators have corresponding indicators in GTP-II.

Figure 5: Pillars of GTP-II



Source: NPC (2015)

### 3.2.4.2 GTP-II targets and indicators: An overview of GTP-II policy matrix

The design of GTP-II policy matrix covers the main goals and outputs indicated in the Second Growth and Transformation Plan. The results framework consists of two main components: goals

<sup>12</sup> See Ferde, T. (2016), Supporting African governments in development planning and the integration of globally agreed sustainable development frameworks into national development frameworks: An application of mainstreaming toolkit to Ethiopia, a research report prepared for the Macroeconomic Division of UNECA.

and priority areas and detailed policy matrix. The first component identifies priority areas along four clusters: macroeconomy, economic clusters, good governance and public service reform, and Social Affairs cluster. For each cluster, there are corresponding goals. The second component provides detailed targets and indicators as well as implementing institutions along the four clusters. The design of GTP-II policy matrix has benefited from previous similar experiences gained from the implementation of the National Monitoring and Evaluation System which has been in place since 1996. It is also based on previous experiences in the mainstreaming of the MDGs targets and indicators into the national plans of the country.

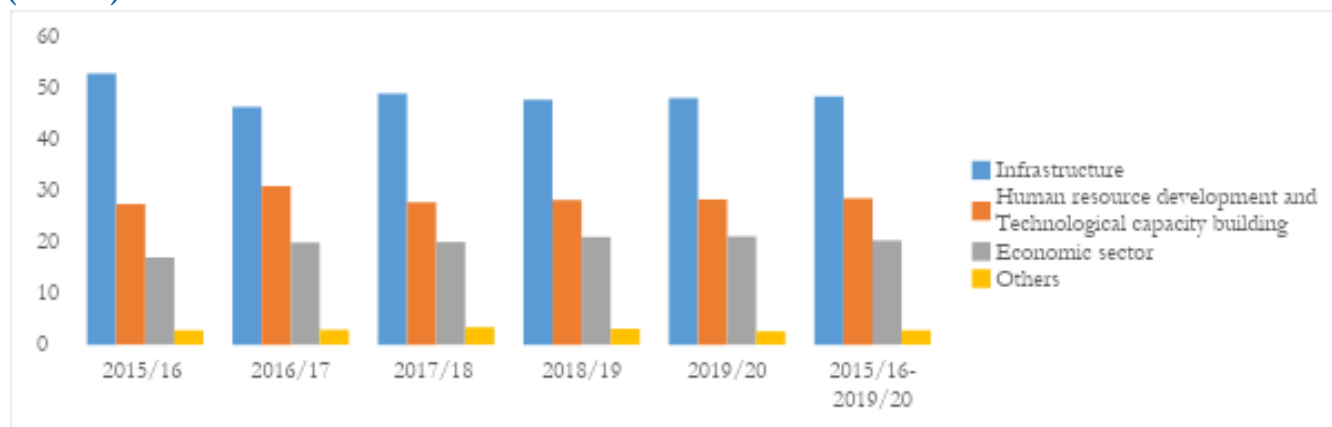
Although the GTP-II policy matrix has shown improvements over its predecessor in terms of data, some of the indicators in the GTP-II Policy Matrix could not be populated with data (e.g. some indicators from the agriculture and rural development). There are sectors with glaring problems with missing baseline data including industrial development, urban development and housing, science and technology development, and environment and climate resilient green development. This indicates a paucity of data to support results-oriented performance measurement across most sectors. The recent M&E Diagnostic study indicate that there are considerable data issues that have plagued the ability to measure and report on performance in Ethiopia, including the inability to populate many of the indicators of the GTP Policy Matrix (AfDB, 2014a). In addition, the Policy matrix needs to include additional targets and indicators related to the Addis Ababa Action Agenda.

### **3.2.4.3 An overview of expenditures during GTP-II period**

The main plan document includes not only activities and development interventions but also expenditures during the plan period. Given the planned activities and interventions both at macro and sectoral levels, total government expenditure is projected to ETB 2.3 trillion, with ETB 1.3 trillion for capital expenditure and ETB 0.99 trillion for recurrent expenditure during the plan period. Such allocation of expenditure reflects government's focus on investment in economic and social sectors. Capital expenditure on infrastructure sector accounts for 48.4 percent of total capital expenditure. Further breakdown of capital expenditure reflects that drinking water and irrigation and energy account for 44.9 percent of capital expenditure, while road, railway infrastructures account for 2 percent and 1.5 percent, respectively. Human resource development and technological capacity building sector account for 28.5 percent of total capital expenditure. Within this, education and training, health, and science and technology capacity building accounts for 16.6 percent, 10.6 percent and 1.3 percent, respectively.

The economic development sector consists of agriculture and rural transformation, manufacturing and other sectors. This sector is projected to account for 20.3 percent of total capital expenditure. Of this, the share of the manufacturing sector would account for a large proportion (15.2 percent), while agriculture and rural transformation accounts for 3.8 percent.

**Figure 6: Distribution of projected capital expenditure requirements by major socioeconomic sectors (Percent)**



Source: NPC (2016), volume II.

#### 4. Means of implementation of development plans: Institutions, planning, and budgeting

Achieving sustainable development and the 2025 vision of the country depends a great deal on high-level political commitment, well-functioning government institutions and overcoming co-ordination failures in public policies and implementation. The implementation of development plans requires more effective alignment of incentives, a better allocation of existing resources and additional funds from domestic, external and innovative sources.

##### 4.1 Institutional arrangement for plan preparation

Sustainable development is a shared responsibility of all levels of government, the private sector, and civil society. It should be noted that achieving sustainable development depends, among others, on strong political commitment, well-functioning government institutions and overcoming co-ordination failures both at policy and implementation levels (OECD, 2006).

A decade long experience in the implementation of MDGs shows that there are several government machineries that are involved in formulating and implementing policies, strategies and plans. Core institutions have been put in place to design sectoral policies and strategies and oversee their implementation. For instance, the Ministry of water, irrigation and Energy is in charge of water and energy issues, while the Ministry of Environment, Forestry and Climate Change (MEFCC) is for environment, forest and climate change related issues. In addition, MEFCC is the national institution providing technical backstopping for coordinating the CRGE strategy, while the Ministry of Finance and Economic Cooperation (MoFEC) for managing the CRGE fund.

The National Planning Commission (NPC), established in 2013, guides and coordinates the national development planning and prepares medium-term (five-year) development plans as a means to achieve a long-term vision of the country. These medium-term plans articulate government's economic, social and environmental priorities, and in turn influence the areas of cooperation and support provided by government partners including donors, intergovernmental institutions, UN organizations, the private sector and civil society.

The National Planning Commission (NPC) of Ethiopia combines both top-down and bottom-up planning processes. First, NPC prepares a macroeconomic framework which indicates the key policy



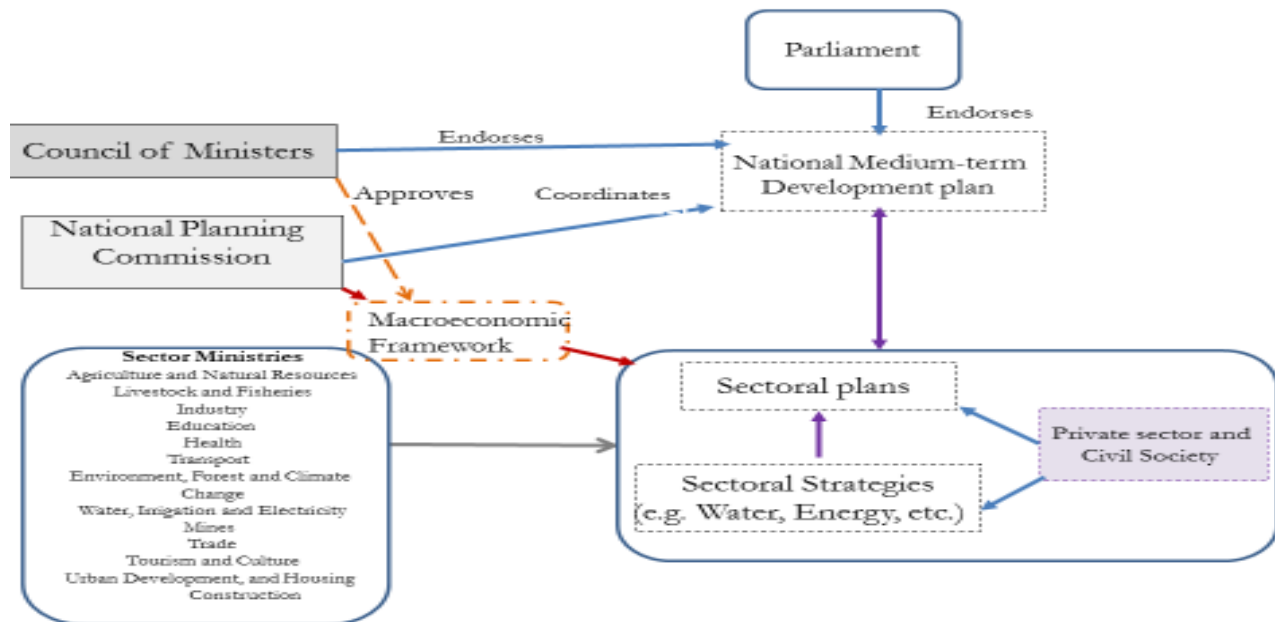
directions of the country during the plan period. This framework needs to get endorsed by the Council of Ministers which will serve as the basis for national development plan preparation. The approved framework is then communicated to sectoral ministries to guide their sectoral plan preparation.

National development plans are normally established through a cyclic process led by the National Planning Commission and involve the following steps:

- Performance review of latest five-year plans against targets,
- Elaboration of next five-year plan (e.g. macroeconomic framework),
- Preparation of sectoral plans (prepared by Sectoral Ministries),
- Development of national development plan (based on sectoral plans),
- Stakeholder consultation,
- Revision and preparation of final national development plan, and
- Approval by Parliament

Once the medium-term plan is endorsed by the parliament, the NPC follows its implementation, monitors and evaluates progress towards targets, and prepares annual progress reports. Ethiopia has already established the necessary institutions in line with the SD.

Figure 7: Institutional arrangement and planning processes in the preparation of medium term plan



Source: Own construction

## 4.2 Coordination and collaborative mechanisms

The cross-sectoral nature of development plans (and SDGs) calls for improved governance arrangements and practices to ensure vertical and horizontal collaboration. Mainstreaming as well as implementation of development plans necessitates strong horizontal collaboration between national coordination body and the different sectors of the economy (Urana *et al.*, 2014). Likewise, vertical interactions also exist between the national coordinating organization and lower levels institutions including the regional states, provinces, districts, cities and communities.

Sustaining cross-sectoral and integrated engagement of different stakeholders at the planning stage and during implementation of national development plans is critical in ensuring positive economic, social and environmental benefits. Although cross-sectoral coordination is achieved at the planning stage through NPC, it is not clear how the different sectors can be coordinated during implementation. The decade long experience in the implementation of MDGs indicates that achieving cross-sectoral coordination has been problematic as each sector ministries operate in silos. Breaking down sector silos at implementation stage is of paramount importance. The National Planning Commission needs to be supported in continuing the efforts of engaging with sectoral working groups to coordinate national development plan implementation across sectors at the national level, and through subnational administrations and their coordination focal points or regional planning commissions.

**Box 3: Coordination mechanism: Selected country experiences**

**Ethiopia:** Ethiopia has established a National Planning Commission in 2013 with the core mandate of coordinating and guiding national plan preparation (both medium and long-term plans) and monitoring and evaluation of national plans and programs. The National Planning Commission ensures coherence and effective planning and implementation of programs at the national and subnational levels. The Commission has also monitoring, evaluation and reporting systems that are implemented at all levels of government. Ethiopia has also established a Climate Resilient Green Economy (CRGE) Facility within the Ministry of Finance and Economic Cooperation to coordinate resource mobilization efforts of the country, with a focus on sustainable development related resources. Ethiopia has mainstreamed both the CRGE strategy and SDGs into its medium-term development plan (i.e. growth and transformation plan (GTP-II)).

**Mauritius:** Mauritius established a Council for Sustainable Development (CSD) to oversee the implementation of SD plans. The main functions of the Council includes coordination of SD programs at all levels, provide advice for the government on SD policies, and acting as the “watchdog” for SD in the country. Above the CSD, there is a strategic committee whose members are drawn from academia, government officials, the private sector, and civil society. The committee provides strategic advice to the CSD on emerging and compliance as well as legal issues.

Source: Urama *et al.* (2014)

The Environmental Council (EC), chaired by the Prime Minister, was established to oversee the implementation of the CRGE strategy. Members of the EC are drawn from Federal Ministries, Presidents of Regional States, and representatives of non-governmental bodies, the private sector and trade unions (see Ferede, 2014; UNDESA, 2012). EC can serve as an entry point to establish Sustainable Development Council (SDC) that oversees the implementation of SDGs in the country. The SDC will serve as an inter-ministerial coordinating committee for sustainable development, which provides an overarching policy direction for the implementation of SD agenda. The same committee can be reoriented to provide technical support to SDC.

### 4.3 National Framework for financing development: Planning and budget process

The Ministry of Finance and Economic Cooperation (MoFEC) plays the key role in public financial planning, budget preparation, execution and control. MoFEC follows an integrated planning and budget process in line with programme budgeting. The budget schedule involves two main processes: planning and budget processes. In the planning process, government forecast of resources defines the budget envelope and serve as the principal resource constraint. The macroeconomic fiscal framework (MEFF) preparation process is led by MoFEC and is completed in two phases: (i) preparation and (ii) approval. The first phase involves estimation of both supply of resources and expenditure needs. Essentially, it consists of three main building blocks.

- (i) **Macroeconomic forecast** includes gross forecast of domestic product (GDP), and balance of payments (BOPs), monetary aggregate and inflation forecasts,
- (ii) **Forecast of resources available** based on forecast of domestic revenues, direct budget support, and of project loans and assistance, and
- (iii) **Expenditure needs forecast** including forecast of resource requirements for recurrent and capital expenditures, regional requirements for project loans and assistance, and of the total regional expenditure requirements for the priority sectors in GTP-II.

The above three forms the building blocks of the MEFF which provides indicative planning figures for both recurrent and capital expenditures. The second phase involves approval of MEFF by the Council of Ministers as per the financial regulation No.190/2010. Once MEFF is approved by the Council of Ministers, MoFEC communicates to public institutions regarding MEFF together with the budget call letter to help them guide preparation of their annual budget on the basis of the five-year indicative planning figures. As part of the planning process, MoFEC prepares a three year regional general purpose subsidy which is allocated to regional states based regional general purpose grant formula.<sup>13</sup> The planning process is completed with the preparation of the annual fiscal framework. The planning phase brings together core macro institutions including National Planning Commission and National Bank of Ethiopia which provide pertinent inputs to the preparation of MEFF.

The budget process is built around the preparation of a five-year macroeconomic fiscal framework (MEFF) and is led by the Budget Preparation and Administration Directorate of MoFEC. The budget process consists of the following steps: (i) pre-budget preparation preparedness which relates to links between budget and policy, i.e. plan document (e.g. GTP-II), annual programme budget document including assessment of previous performance, and preparation of preliminary budget based on previous budget allocations; (ii) Announcement of annual regional general purpose grant to regions, (iii) Issuance of budget call (includes indicative budget ceiling which takes into account the updated MEFF and provides guidelines for sector public institutions), (iv) Budget request by public institutions, (v) Budget hearing, (vi) Budget preparation and consolidation, (vii) Approval by the Council of Ministers, and (viii) Endorsement by the House of Representatives.

Around February each year, Budget Preparation and Administration Directorate of MoFEC announces budget request call, providing guidelines for budget preparation and instructions for line ministries to allocate resources among various development programmes and projects detailing

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<sup>13</sup> With the exception of Addis Ababa, all regional states (ten in number) benefit from the federal government subsidy. The regional general purpose grant formula is prepared by the House of Federation.

sector priorities, alignment with the national development plan priorities. The guidelines are based on national plans and strategies and are informed by the budgetary ceilings and provisions established in the Budget call.

The budget, in particular the consolidated annual budget is a vehicle for attaining medium-term and long-term development aspirations of the country. But the links between the budget preparation process by MoFEC and the role of NPC is not clear. While the Budget Preparation and Administration Directorate of MoFEC directly interacts with sector ministries in the budget process, NPC, as a coordinator of the overall plan preparation and follow up, doesn't seem to play any significant role. For instance, sector ministries are requested to submit to MoFEC their previous year performance assessments together with subsequent plans. On the other hand, NPC prepares annual progress report (only physical activities), but this information seems to be of little use in the budget process.

The monitoring and evaluation (M&E) of budget utilization is built in the budget process as each beneficiary public institution is required to submit performance report (including quarterly and annual reports) that shows both physical performance and budget utilization. To maintain uniformity across public institutions, MoFEC has designed a reporting template that guides the preparation of performance reports. However, it is not clear to what extent MoFEC uses performance reports submitted by public institutions in its subsequent budget preparation efforts. Discussions with stakeholders indicate that there is a room for improving the operational efficiency of the budget, especially the execution of investment projects as they take more time than envisaged. There are also cost and delays which undermine the economic returns to investment and postpone the envisioned benefits further into the future. This requires strong monitoring and evaluation system and enforce accountability.

## 5. Domestic finance: Analysis of institutional and policy context

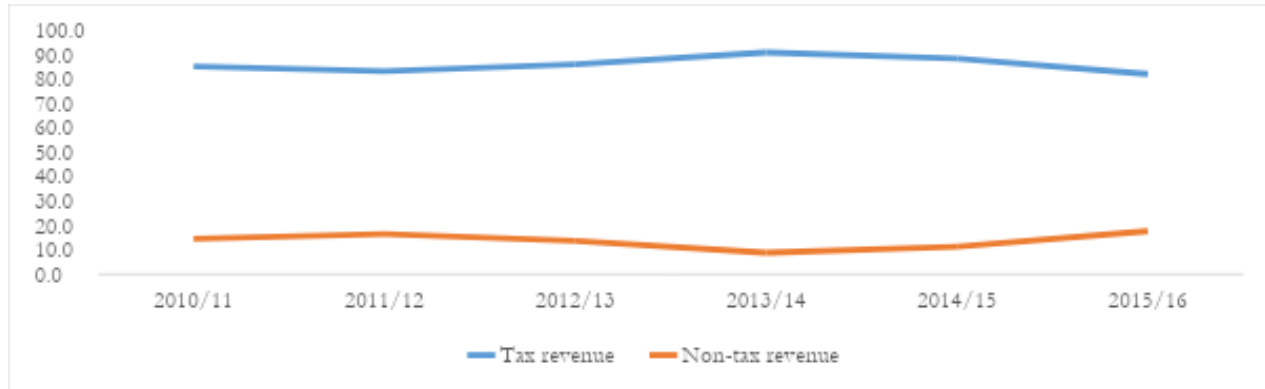
There is no doubt that financial and non-financial support remain crucial in successfully implementing sustainable development initiatives. In particular, achieving the 2030 Agenda will require commensurate financial and technological resources. The Addis Agenda outlines a comprehensive financing framework to implement the 2030 Agenda. Mobilizing domestic resources to increase financing for development through enhancing tax revenues, rationalizing subsidy programmes, developing deeper capital markets and preventing illicit capital flows are examples of improving the prospects of adequate availability of finance for development. The AAAA encourages countries to strengthening domestic resource mobilization, continuing international cooperation on tax, improving domestic tax policies administration systems and better collection of revenues and statistics, and combating illicit financial flows (SDG 17; AAAA paras 22, 23). Domestic resource mobilization needs to be a priority for Ethiopia in the context of the national integrated fiscal framework (NIFF) financing strategy as articulated in the AAAA. Given its low revenue as a share of GDP and uncertainty on external financial flows, increasing domestic resources is a key issue for Ethiopia. Note that achieving sustainable development will depend not just on the expansion of domestic finance but also on the achievement of substantial improvements in the efficiency of public expenditures.

This section focuses on the following issues: (i) Tax and non-tax revenues (ii) Supply of finance with banks and outside banks; (iii) Domestic private finance; (iv) Public-Private Partnerships (PPPs); (v) inclusive business finance; (vi) Domestic climate finance; and (vii) Domestic philanthropy and NGOs.

### 5.1 Tax and non-tax sources of finance

Tax revenue, which consists of direct and indirect taxes, as a share of total domestic revenue accounted for 82.2 percent of total revenue in 2015/16. Within tax revenue are direct and indirect taxes. Revenues from direct taxes as a share of total domestic revenue marginally increased from 29.3 percent in 2012/13 to 31 percent in 2015/16. Indirect tax revenue, which consists of domestic indirect taxes and import taxes and tariffs, accounts for a large share of total revenue: accounting for 51.2 percent in 2015/16. In absolute terms, revenue from indirect taxes increased from ETB 70.6 billion in 2012/13 to ETB 117 billion in 2015/16. In particular, revenue from import taxes and tariffs also increased from ETB 38.2 billion to ETB 59.3 billion.

Figure 8: Share of tax and non-tax revenues in total revenue excluding grants (Percent)



Source: Based on MoFEC data

#### Box 4: Types of tax and non-tax revenue sources

According to the Ethiopian fiscal data, tax revenue sources include both direct and indirect taxes.

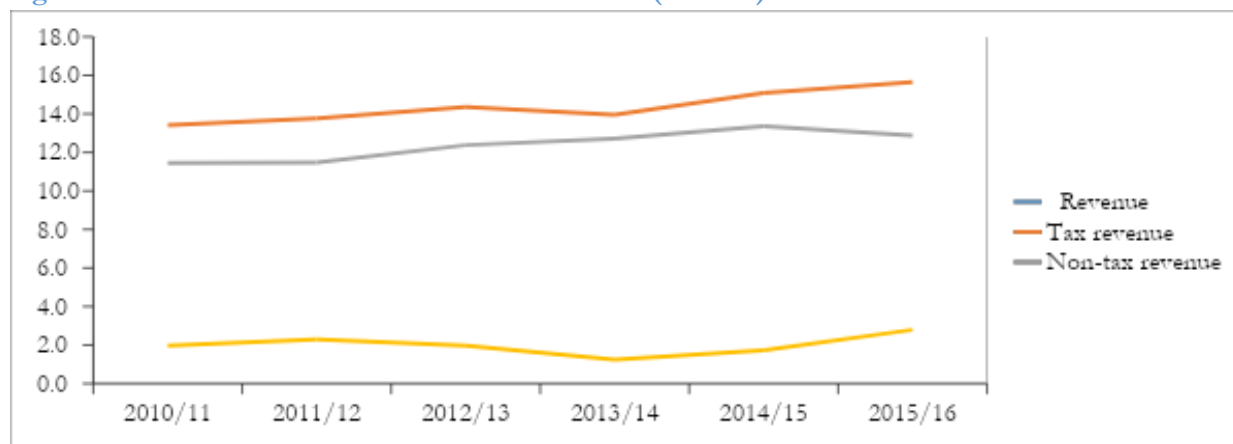
**Direct tax revenue sources:** include taxes on income and profit income which consist of personal income tax, rental income tax, business profits, withholding income tax on imports, other income/chance winning, and interest income tax. Tax on profits account for a large share of total direct tax revenue, accounting for about 76 percent of total direct tax revenue in 2015/16.

**Indirect tax revenue sources:** include two main sources, namely domestic indirect taxes and import duties and taxes. The former includes sales/value added (VAT)/turnover tax (TOT)/excise taxes (such as services sales tax/VAT/TOT, and stamp duties), while the latter includes custom duties, sales/VAT/excise taxes (on petroleum products, alcohol and tobacco, and other imports), and surtax on imports. The two main indirect tax sources are sales/VAT/excise taxes and customs duties. In 2015/16, these indirect tax sources accounted for about 28 percent and 20 percent of total indirect tax revenue, respectively.

**Non-tax finance sources:** The main elements of non-tax sources of finance includes charges and fees, sales of goods & services, residual surplus, capital charge, interest payments and state dividend, pension contributions, reimbursement & property sales, and miscellaneous. Of these, residual surplus, capital charge, interest payments and state dividend is the main source of non-tax source of government finance. For instance, this source of finance accounted for about 87 percent of non-tax revenue in 2015/16.

Despite robust economic growth, the share of tax revenue in GDP has not shown significant improvement; tax revenue as a share of GDP slightly increased from 11.5 percent in 2012/13 to 12.9 percent in 2015/16. Tax revenue has remained low compared to the tax revenue generating capacity of the economy, the financing requirements of the development programs and the average performances of the sub-Saharan countries (MoFED, 2013; World Bank, 2015). This indicates existence of some kind of inefficiency in tax administration and structural problems in the tax system.

Figure 9: Share of tax and non-tax revenues in GDP (Percent)



Source: Based on MoFEC data

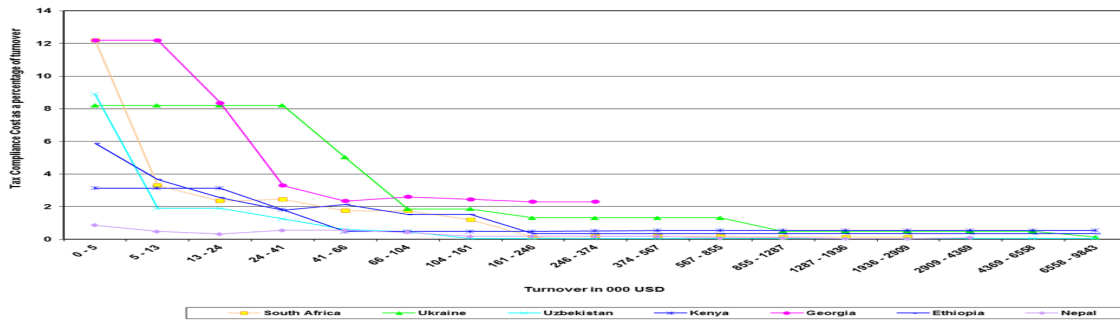
According to recent study by IFC (2016), the majority of tax payers indicated that the process of complying with taxation is perceived to be more burdensome than the actual tax due, indicating high tax compliance cost. The tax compliance cost, which consists of outsourcing and in-house costs, is high in Ethiopia. The total tax compliance cost was estimated to be between 4.5 and 5.8 percent of Ethiopia's total government revenue in 2012/13 and about one percent of GDP during the same year (IFC, 2016). The average tax compliance cost of a business as a share of turnover was in the range of 4.7-5.4 percent in 2012/13.<sup>14</sup> The tax compliance cost as a share of turnover is relatively high for small businesses compared with large businesses; tax compliance cost as a share of turnover tends to decrease with turnover, suggesting that it is regressive.<sup>15</sup> In absolute levels, large companies face large tax compliance cost. For instance, tax compliance cost for category A businesses is well over five times the cost for category C businesses.

Tax compliance cost in Ethiopia is high even compared with other countries such as Kenya, South Africa, Ukraine, Nepal and Georgia (Figure 15).

<sup>14</sup> In its 2016 study, the IFC estimated the tax compliance cost for Ethiopia in two ways: with and without acquisition and maintenance costs of software and hardware. If the acquisition and maintenance costs of software and hardware are included, the tax compliance cost a share of turnover would be 5.4 percent, otherwise 4.7 percent (i.e. without acquisition and maintenance costs of software and hardware).

<sup>15</sup> The income tax legislation classifies businesses into three categories based on turnover. Category A businesses are those that have annual turnover of ETB 500,000 or above and all incorporated entities, while Category B includes those that are not already classified as A and have annual turnover of more than ETB 100,000 but less than ETB500, 000. Category C taxpayers are those that are not already included in categories A and B and have annual turnover up to ETB 100,000 (See Income tax proclamation No. 286/2002 (as amended) and Council of Ministers regulations 78/2002 (as amended)).

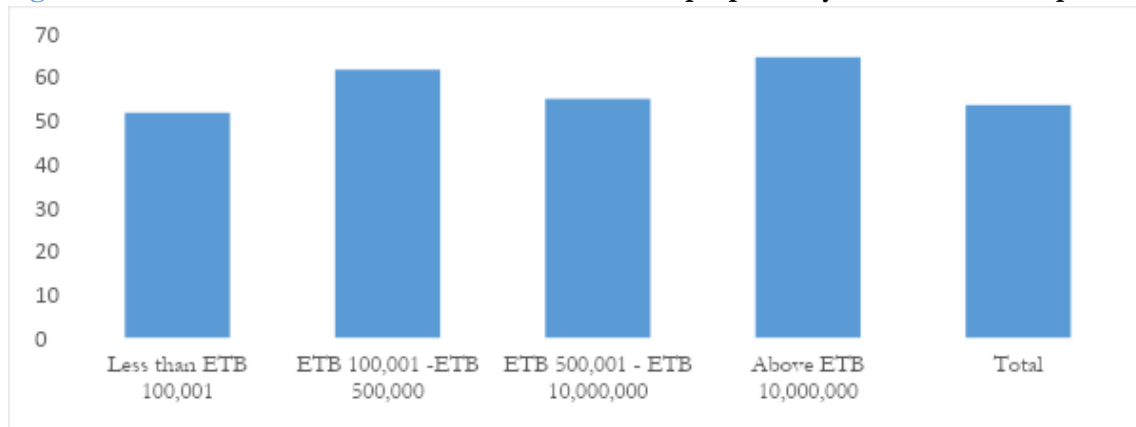
**Figure 10: International comparison of tax compliance costs**



Source: IFC (2016)

The main barriers for hindering businesses not registering for taxes include high tax burden and high tax rates. While about 34 percent of businesses perceived higher tax burden or high tax rates, close to 13 percent perceived complicated tax compliance procedures as the disadvantages of registering for taxes (IFC, 2016). Underreporting of taxable incomes or inflating expenditures are some of the methods used by firms to evade taxes. The recent study also indicates that business firms in Ethiopia declare on average 53 percent of their total annual sales for tax purposes. Similarly, businesses overstated by about 38.4 percent of their actual expenditures in tax returns. In particular, large taxpayers overstated their annual expenditures for tax purposes compared with small and medium size businesses. There is also a wide gap between tax capacity and actual tax revenues raised due to tax-administration challenges. Together, these findings suggest that there is a need for improving tax revenues through, among others, enhancing efficiency of tax administration (e.g. modernization) and awareness creation.

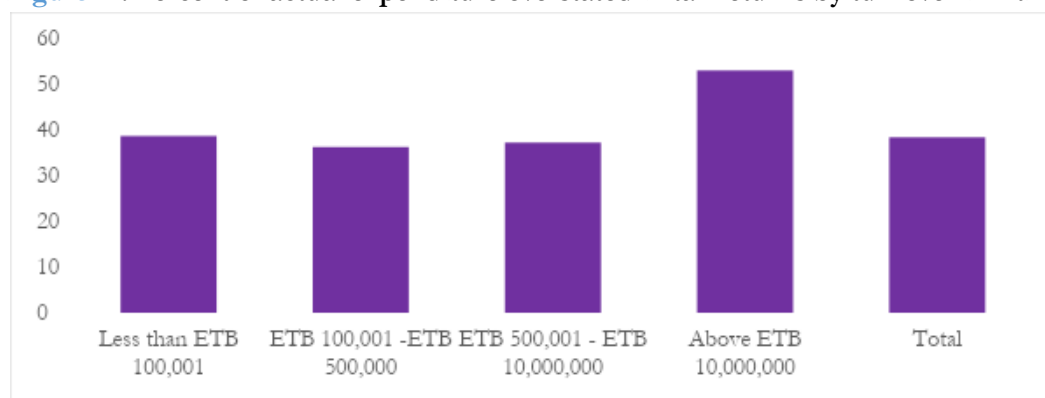
**Figure 11: Percent of total annual sales declared for tax purposes by turnover in Ethiopia**



Source: IFC (2016)



**Figure 12: Percent of actual expenditure overstated in tax returns by turnover in Ethiopia**



Source: IFC (2016)

Domestic revenue mobilization is also hampered by the preferential treatment granted to specific taxpayers through targeted tax deductions, credits, exclusions, or exemptions to attract investment and support growth. In 2015/16, revenue foregone was ETB 67 billion, representing 35.3 percent of total tax revenue or 4.4 percent of GDP during the same year. Between 2005/06 and 2015/16, revenue foregone as a share of customs duty and taxes was more than 90 percent. Although these incentives are meant to attract private investment, there is a need to closely monitor and evaluate their benefits vis-à-vis the foregone revenue.

**Figure 13: Revenue foregone (in Billion ETB)**



Source: ERCA

The Ethiopian government has expressed its commitment to strengthening domestic tax revenue mobilization. Key intervention areas include:

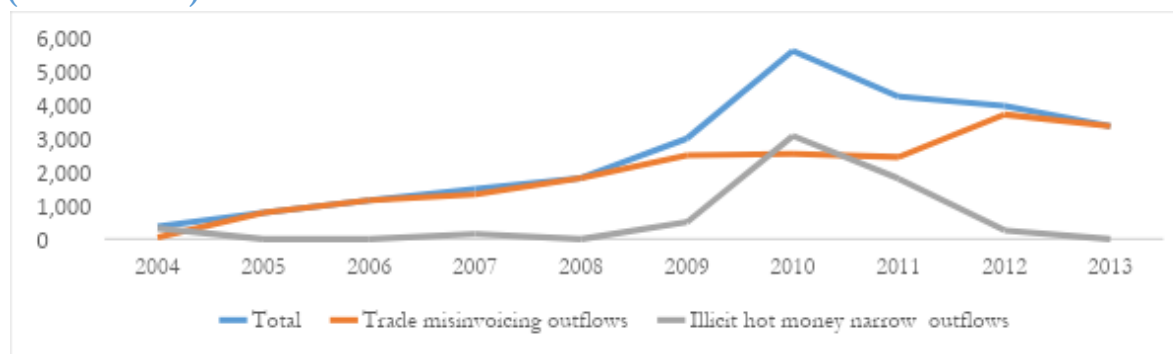
- expand the tax base through capturing new businesses into the tax net
- improve human resource development and management revenue offices;
- expand modern information system;
- improve customer relations and awareness creation among tax payers;
- customer service and support to improve the delivery system;
- improve tax collection efficiency by fully and fairly implementing the on-going tax and customs reforms;
- improve the presumptive tax system; and
- improve the administration of the tax system.

These interventions, if successfully implemented, will address some of the challenges in tax administration and improve the domestic tax revenue. In addition, efforts are in progress to establish a dedicated tax directorate within the Ministry of Finance and Economic Cooperation (MoFEC), which was under the macroeconomic policy and management directorate of MoFEC, indicating government's determination to enhance tax revenue mobilization. If strengthened, this institutional

set up can provide evidence-based and coordinated advice on issues related to tax policy, tax legislation, tax forecasting, analysis of revenue potential, and tax administration. Given that this is in the early stage, more support is required to establish a strong tax directorate in terms of human resources with the required expertise and skills as well as supporting infrastructure.

Also linked to the challenge of domestic resource mobilisation is capital flight and illicit financial flows. According to the 2015 Global Financial Integrity Report, illicit financial outflows through trade misinvoicing increased from USD 52 million in 2004 to USD 3.4 billion in 2013, grew on average by about 33 percent. The volume of illicit financial outflow through misinvoicing international trade transactions amounts to an average of USD 2 billion per year. In particular, import trade misinvoicing has remained the main driver of illicit financial outflows, while export under-invoicing is less of a concern. This indicates some kind of capacity weaknesses in terms of arresting abuses of transfer pricing, especially by multinational enterprises. This calls for building domestic capacity to implement the transfer pricing rules<sup>16</sup> and take proactive steps to narrow the information gap and obtain regular and correct information from relevant companies. This also requires strengthening the audit preparation capacity of tax administrations offices to make information requests to taxpayers more precise and explicit, and enforce reporting and disclosure obligations. Discussions with stakeholders indicate that the Ethiopian Revenues and Customs Authority (ERCA) has introduced the Ethiopian Customs Valuation System (ECVS) with the aim to improve information system, especially on generating up-to-date information on international prices of imports of goods. Although this system is expected to address price variation on imports and reduce malpractices, it is less applicable to exports. In addition, internal capacity problems with ERCA workers also limits the application of this system due to resistance and reluctance of using the technology, and this requires continuous capacity building and mindset change.

**Figure 14: Illicit financial outflows through misinvoicing international trade transactions (Million USD)**



Source: Global Financial Integrity Report (2015)

In terms of institutional set up, the Ethiopian Revenues and Customs Authority (ERCA) is responsible for administering federal and Addis Ababa City Administration domestic direct and indirect taxes and taxes on international trade under the supervision of the Prime Minister. The Ministry of Finance and Economic Cooperation (MoFEC) is in charge of fiscal policy design, while ERCA is responsible for implementing policies related to taxes. ERCA is led by the Director General and is supported by a management team comprising Deputy Director Generals (e.g. in charge of federal domestic tax division, Addis Ababa domestic tax division, Customs division,

<sup>16</sup> Ethiopia issued a transfer pricing rules in 2015 as part of its income tax proclamation. The explicit adoption of the transfer pricing rules provides guidance, especially for multinational enterprises wishing to do business in Ethiopia to arrange their businesses to comply with the 'arm's length' principle.

enforcement division, and modernization & corporate division), Bureaus, and Directorates. Domestic Tax Operations are carried out at 140 tax office administering the affairs of large, medium, small, and micro taxpayers. Recent performance assessment report of ERCA highlighted a number of institutional challenges (Muyangwa *et al.*, 2016). These include among others weak information technology administration system, inaccurate database, weak compliance risk management program, lack of electronic payment facility, weak internal audit function not providing oversight on all key operations, lack of impact assessment or evaluation of compliance activities, relies on use of manual operations (outside of SIGTAS), deficient VAT refund system, and weak coordination among key directorates and with branches.

Looking forward, the main sources of tax should be derived from domestic sources to ensure sustainability of finance for development. However, since there is a large informal economy, there is a need to focus on registering this part of the economy to bring them into the tax net. Expansion of the income tax base and bringing more individuals and companies under the tax net would help to drive revenue growth. In order to achieve this, there is a need to press ahead with further automation of the tax administration system, and strengthening ERCA through training and establishing robust systems at various levels. Specifically, key intervention areas include (NPC, 2016):

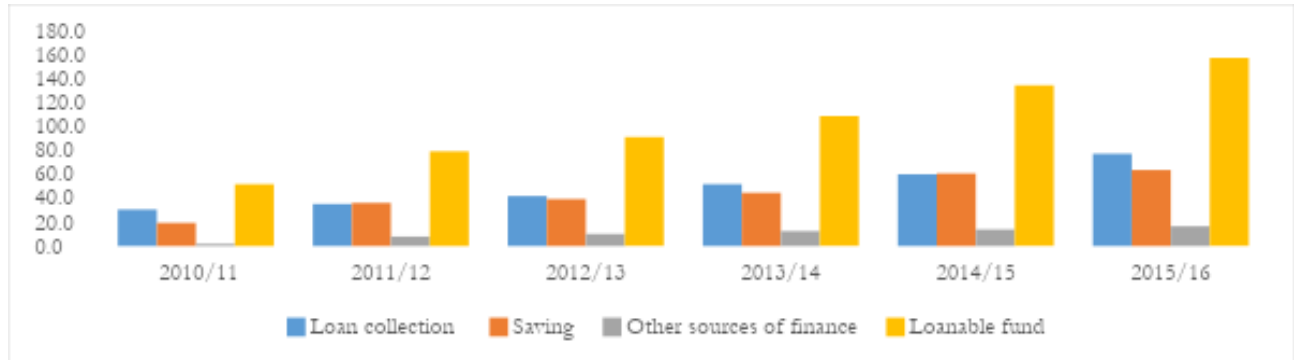
- strengthening system and institutional capacity development of the sector,
- establishing a modern and reliable trade information system,
- building integrated information network (by linking sectoral implementing institutions, regional states and city administrations),
- establishing Trade Development Academy for building sustainable trade capacity,
- developing a harmonized national trade policy, and
- expanding trade registration and licensing services to enhance a modern, fair and competitive trade system and support the trade registration and licensing system with modern technology.

## 5.2 Supply of finance with banks and outside banks

### (i) Supply of finance from banks

The total number of banks (including government and private banks) reached 19 and there were 2,868 bank branches in 2014/15. One of the indicators of access to bank services is the ratio of population to bank branch which is low in Ethiopia, indicating large unbanked population. In 2014/15, a bank branch served about 30,334 people (NPC, 2016). The total loanable fund with the financial institutions, especially in banks consists of loan collection, savings/deposits, and other sources of finance. The total loanable fund increased from ETB 51.7 billion in 2010/11 to ETB 157.3 billion in 2015/16, increased on average by about 20.9 percent per year (Figure 15). Saving and loan collection are the main sources of loanable fund. In particular, deposits have increased from ETB 19.3 billion to ETB 63.6 billion in 2015/16, grew by about 21.8 percent.

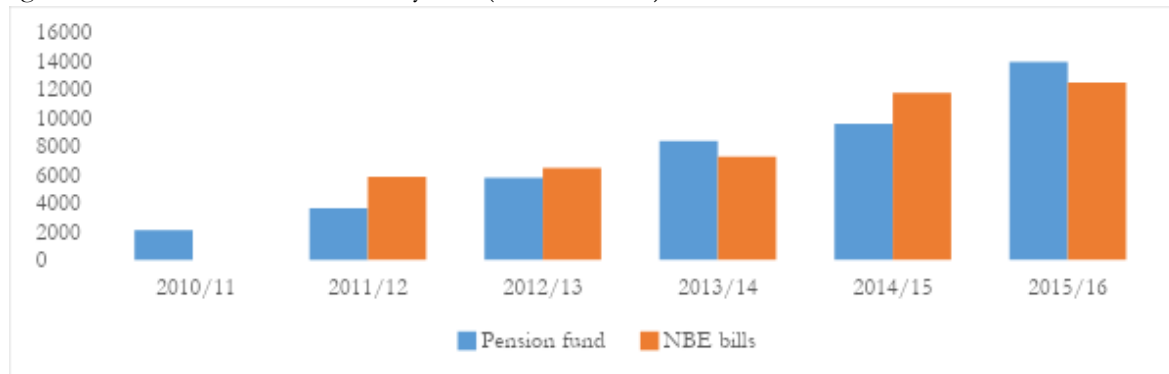
Figure 15: Composition of loanable fund from banks (In billion birr)



Source: NBE, Development Bank of Ethiopia and Commercial Banks

Pension fund and government treasury bills (T-bills) are also other sources of finance in Ethiopia. In 2011, the Government of Ethiopia introduced a proclamation to make pension contribution compulsory for employees in private enterprises. Pension fund has increased from ETB 2.1 billion in 2010/11 to ETB 13.9 billion in 2015/16, grew by about 36.4 percent per year. Likewise, T-bills have increasingly become an important source of finance; increased from ETB 5.8 billion in 2011/12 to ETB 12.5 billion in 2015/16, representing a growth rate of 21.2 percent per year.

Figure 16: Pension fund and Treasury bills (In million birr)

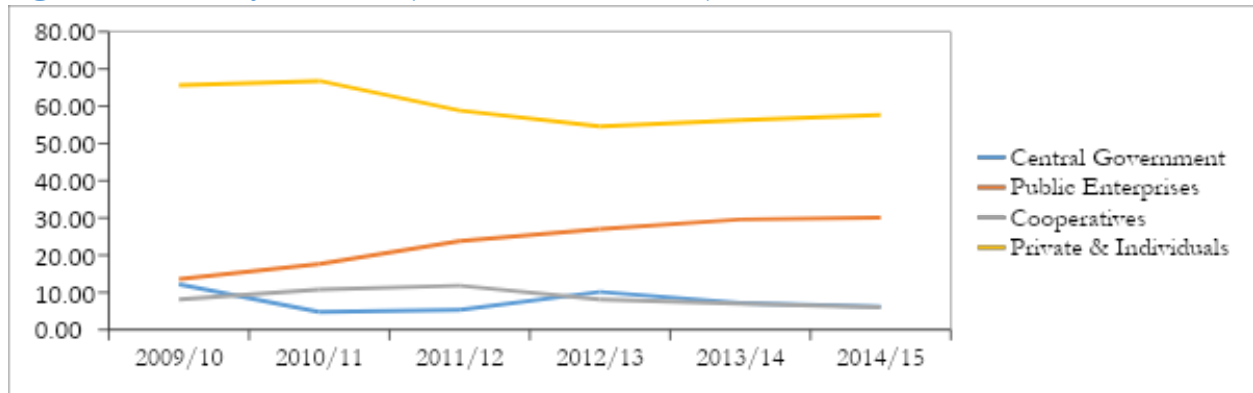


Source: NBE

Note that loanable fund, pension fund and T-bills serve as sources of finance for the government and private sector. A look at government statistics reveals two types of domestic borrowing: bank and non-bank. In 2015/16, domestic bank borrowing by the government accounted for 1.5 percent of GDP and other sources of domestic finance for the government includes privatization and other sources, but these are of small magnitude. A review of credits by institutions indicates that the share of public enterprises in total credit increased, while that of private sector and central government has shown a declining trend between 2009/10 and 2014/15.

Given that government saving is inadequate to finance development interventions, there is a need to raise government saving through effective administration of the tax policies to increase tax revenue, and prioritize government expenditure to capital investment, efficient and effective use of budget, focus on sectors that accelerate capital accumulation, economic growth and poverty reduction, and reducing wastage and improving transparency on expenditure.

**Figure 17: Credit by borrower (Percent of total credit)**



Source: NBE

**(ii) Supply of finance outside banks**

Although the financial sector has shown rapid expansion, the coverage is inadequate compared to the size of the country’s population. Given that commercial banks and insurance companies are concentrated in cities and towns, the majority of rural population still have limited access to financial services. There is huge finance outside the formal banking sector. Recent statistics from the National Bank of Ethiopia indicate a large magnitude of currency outside banks. In 2015/16, currency outside banks was about ETB 66.7 billion, equivalent to 40 percent of total loanable fund available in banks. Between 2010/11 and 2015/16, currency outside banks grew on average by 14.5 percent, indicating a large potential to tap this finance for financing development activities. This could be done through, among others, expanding bank branches, introducing capital markets, and financial literacy.

**Figure 18: Currency outside banks (In billion ETB)**



Source: NBE

In order to mobilize this finance outside the formal banking sector, the main intervention areas, as articulated in the GTP-II, shall include:

- public education and mobilization around domestic savings,
- maintain positive real interest rate,
- expand and improving financial institutions including microfinance institutions, and

- deploy saving instruments including contractual savings and services such as saving for housing program, saving for investment equipment scheme, bonds, social security saving, and health insurance saving.

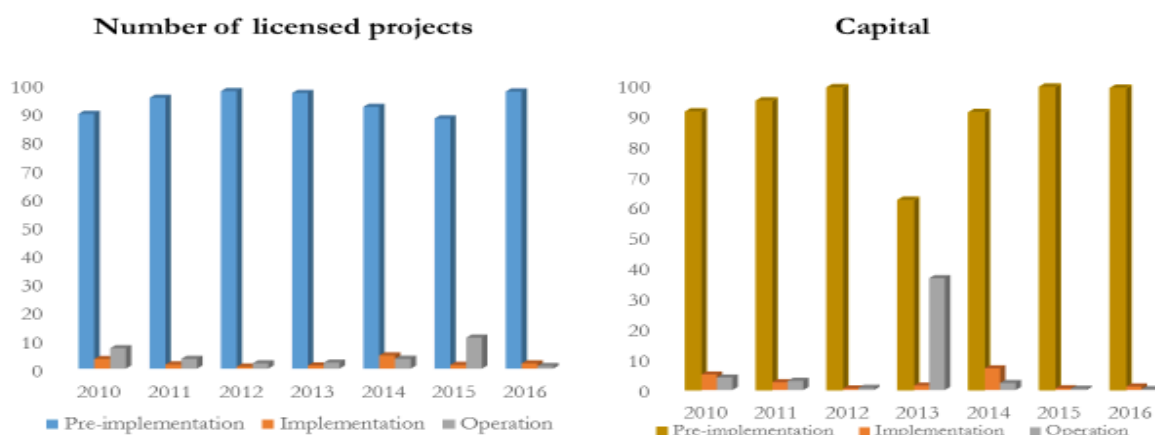
### 5.3 Domestic private business and finance

The AAAA recognizes the growing roles of private finance and business activity as major drivers of inclusive economic growth and job creation and help reduce poverty and inequality (SDG 1, 10) and foster inclusive growth (SDG 8; AAAA paras 35-37).

An increase government spending is indispensable to spearhead the country's development. But financing increased expenditure requires expanding prudent financing modalities such as harnessing both domestic and foreign private sources of finance. One of the main advantages of engaging with the private sector relates to the possibility of attracting new financial resources. In the short term, this could either be additional to the efforts to scale up public investment expenditures, or allow significant 'savings' of public funds. Accordingly, the Ethiopian government has designed different incentive schemes to promote private sector investment. The Investment Proclamation No.769/2012 is the main legal framework for guiding and promoting private sector development in the country. The Ethiopian Investment Commission (EIC) is the main institution responsible for promoting private sector investment through various incentives. The investment proclamation also provides various incentives including provision of land at reduced land lease value, building industrial zones with developed infrastructure, import duty exemption up to 100 percent, income tax holiday based on investment type and location of the investment, zero tax on export goods, export promotion schemes like voucher system, duty and tax drawback, bonded manufacturing warehouse, export guarantee scheme (except for coffee exporters), foreign currency retention, remittance of capital and the like.

Harnessing domestic private sector is crucial in speeding the country's transformation process. Between 2010 and 2016, of the 39,771 licensed domestic private investment projects, a large proportion of these investments were under pre-implementation. In 2010, the share of investment projects in operation was only four percent and this figure declined to 0.20 percent in 2016. During the GTP-I period, of the total 22,097 licensed domestic investors with a total capital of ETB 212.74 billion, only 0.84 percent (186 projects with a total capital of ETB 4 billion) were under construction, while 1.2 percent (262 projects with a total capital of ETB 3.948 billion) started operation (NPC, 2016). This indicates that the majority of domestic private investment projects registered with the federal and regional offices have not been translated into actual investments on the ground. In terms of sectoral distribution, a large proportion of domestic private investors were engaged in the services sector compared with agriculture and industry. This requires close monitoring and follow up of licensed projects and facilitate their graduation from pre-implementation to implementation and operation phases.

Figure 19: Trends in licensed domestic private investment (Percent share)



Source: Based on Ethiopian Investment Commission Data

### 5.3 Public-private partnership in Ethiopia

The conventional public finance approach of paying to achieve public policy purposes mainly from public revenue will not help achieve multiple objectives of the government as this approach often leaves many goals underfunded. New approaches and financing technologies are emerging that could help pursue public policy goals more efficiently at lower cost and with higher welfare gains.<sup>17</sup> To mobilize the private sector for sustainable development involves combining public financing, regulation, and private market participation into an effective public-private partnership (PPP). Public-private partnership refers to a collaborative arrangement between government or the public sector, and a private entity for better provision of public infrastructure and services. In PPP framework, some of the services that fall under the responsibilities of the public sector are provided by the private sector, with clear agreement on shared objectives for delivery of public infrastructure and/or public services (KDI, 2015). The Addis Agenda also recognizes the need for harnessing public-private partnerships as source of blended finance to lower investment-specific risks and incentivize additional private sector finance across key sectors (AAAA, para.48).

The PPP arrangement exists in Ethiopia since the 2000s. The Ethiopian government introduced the PPP arrangement in its 2009 Procurement and Property Administration Proclamation No.649/2009 which led to awarding contracts to the private sector. In addition, the Supreme Law of the land provides the legal framework for PPP. However, specific policy and legal framework governing PPP is yet to come, leading to an ad hoc undertaking of PP projects. Having a separate legal framework for PPP helps facilitate establishment of a specialized institution to support operationalization of PPPs in the country. Efforts have been made to tap on PPP initiatives in Ethiopia. Early examples

<sup>17</sup> See <http://web.undp.org/thenewpublicfinance/index.html>

of PP projects include a unifying utility billing system (*Lebulu*) (Build-Operate-Transfer, BOT), Corbetti geothermal energy (Build-Lease-Transfer, BLT), management of the Addis Ababa Exhibition Center (management contract/lease), urban housing (e.g. design and construction), and waste management and recycling<sup>18</sup> (KDI, 2015; Asubonteng, 2011). These projects involve both domestic and foreign companies as well as development partners.<sup>19</sup> In Ethiopia, PPP arrangements involve a mix of concession agreements (e.g. BOT and BLT) and management contracts with full private financing and in-kind contribution by the government. The existing PPP initiatives are limited to selected sectors, focusing on energy generation and services delivery.

**Box 7: A unified payment system for utility services**

In 2013, a unified utility billing system known as “*Lebulu*”<sup>20</sup> started operating in Addis Ababa, which help service users pay different utility bills at a single service window at convenient times and locations. This service payment system was established by the Ministry of Communication and Information Technology (MoCIT) and the Kifiya Private Limited Company. Before the introduction of the *Lebulu*, service users had to pay electricity, water and telephone bills in three different centers, at nearby branch offices. Moreover, payment centers for Ethiopian Electric Power Corporation (EEPCO), Addis Ababa Water and Sewage Authority (AAWSA) and Ethio-Telecom used to have different payment schedules. Paying utility bills was a challenge for households, and it was not uncommon to see long queues of customers waiting patiently to pay utility bills. Customers of the three services used to take up to three different days as payments had to be paid in three different or overlapping schedules at different locations.

The key lesson is that Public-Private Partnership can be used to deliver infrastructural services. It has also demonstrated the transformational impacts of ICT on city infrastructure and services delivery. Joint planning, design, building and maintenance of infrastructure continue to be some of the challenges facing Ethiopian cities. The experience of *Lebulu* demonstrates how PPP arrangements can enhance efficiency in service delivery and this type of model can also be used in other sectors.

Source: Ministry of Urban Development, Housing and Construction and Ethiopian Civil Service University (ECSU), 2015

As indicated in the GTP-II, the government recognizes the importance of enhancing public-private partnership to narrow the gap between public service delivery and public service demand, thereby improving the quality of social services. In particular, the government envisages use of the PPP model in selected infrastructure delivery such as roads, railway, education, health, energy, telecommunications, and transport. In the service sector, potential PPP arrangement include, among others, parks and recreational facilities, information communication and technology (ICT) centres, solid waste management and recycling, exhibition centres and unified billing. A similar framework can be applied to agricultural and industrial infrastructure development. Leveraging non-state resources through partnership with the private sector serves as an opportunity for the government to narrow the gaps caused by resource constraints (MoH, HEPCAPS2 Project, 2015; Asubonteng, 2011). For instance, about USD 4 billion capital was raised in three PPP arrangements alone, namely, *Lebulu*, Addis Ababa Exhibition Center, and geothermal energy projects.

<sup>18</sup> For example, Dream Light Plc for solid waste management and recycling in Bahir Dar with partnership involving Dream Light Plc, Bahir Dar City Administration, UNDP, UNEP, GIZ, and Bureaus for Health and Environment Protection of the region (see Asubonteng, 2011).

<sup>19</sup> There are different models of public-private partnership including service contracts, management contracts, lease agreement, franchise, joint venture, concession, BOT (Build-operate-transfer) and BOOT (Build-own-operate-transfer) (UNDP, 2015). Under the BOT model, private sector builds and operates a public service company (e.g. waste treatment plant) for a specified time after which ownership reverts to the government, while the BOOT model involves a private sector company finances, constructs, owns and operates the infrastructure for a fixed term.

<sup>20</sup> The literal English translation of ‘*Lebulu*’ is “for every one”.



Despite the potential of PPP in Ethiopia, challenges remain in implementing PPP including, among others, weak technical and managerial capacity to execute PPP contractual arrangements, inadequate awareness about PPP, lack of specific legal frameworks, lack of a standardized PPP operating procedure, weak contract negotiation capacity, and financial constraints.

Discussions with stakeholders indicate that efforts are being made to establish PPP, with draft legal framework for PPP establishment has been prepared, with the Ministry of Finance and Economic Cooperation taking the lead. The finalization of this legal framework helps establish a dedicated and functional institution for nurturing PPP to mobilize resources from the private sector. However, this needs to be followed by capacity building programme for public and private sector to successfully implement the PPP framework.

**Box 8: Ethiopia’s experience in PPP in the health sector**

Different models of PPP exist in the health sector including contracting, leasing, franchising, and social marketing. In Ethiopia, the PPP arrangement financing, service delivery, capacity building, participation in policy, guideline, and standards development and support in the formation of health professional associations. Examples of existing public-private (profit and nonprofit organizations) collaboration include among others in the delivery of comprehensive human immunodeficiency virus (HIV)/Antiretroviral therapy (ART) and Tuberculosis (TB). Contracting partnerships for the provision of non-clinical services are also notable. Such examples include Mizan Aman Hospital’s outsourcing of daily cash collection and patient registration) and clinical diagnostic services (e.g. Debre Berhan hospital outsourcing of advanced clinical laboratory services). These partnerships demonstrate examples of outsourcing practices by public hospitals.

Infrastructure-based hospital PPP arrangements refers to the establishment of specialized medical care services (e.g. Meles Zenawi Dialysis Center in Mekelle) and eye care (OIC eye care center at Zewditu Memorial Hospital in Addis Ababa) within public hospitals were found to create opportunity for providing services. PPP in social marketing (e.g. Family planning and child health commodities by DKT-Ethiopia) and franchising (Marie Stopes “BlueStar”) also improve access to sexual and reproductive health services.

Source: MoH, HEPCAPS2 Project, 2015

## 5.4 Inclusive Business Finance

Inclusive business finance refers to capital that supports the creation, growth, and sustainability of entrepreneurs, small holders, and small enterprises that were previously excluded from the financial markets. There are many microfinance institutions, with a significant total volume of lending. Non-bank financial institutions are relatively modest players. The economic importance of non-formal sectors and small and micro enterprises (SMEs) is well recognised in Ethiopia. The SME financing is receiving increased attention given the importance of small and medium enterprises (SMEs) in the economy, especially in employment generation.

The AAAA acknowledges the centrality of full and productive employment and decent work for all as a central objective of development strategies. For sustainable growth to be inclusive and job-rich, it needs to be supported by a comprehensive and coordinated approach which places employment promotion as the priority in national economic and social development strategies. This will enhance employability, promote quality apprenticeship and entrepreneurship through practical actions (SDG 10; AAAA paras 16, 37 and 41).

Despite robust economic growth in the past decades, generating employment for the expanding labour force has remained a challenge as reflected by high unemployment rate in urban areas (about 16.5 percent in 2013). This requires a combination of growth enhancing interventions and social protection programs. The Ethiopian government has initiated about ETB10 billion revolving fund for the youth.<sup>21</sup> Likewise, regional government also established youth fund to ease the growing

<sup>21</sup> See <http://www.ena.gov.et/en/index.php/economy/item/2073-gov-t-to-establish-10-billion-birr-mobile-youth-fund>

unemployment problem. Given the scale of unemployment in the country, a coordinated support is required to enhance youth employability through productive and decent jobs. The Ethiopian government has put a strong emphasis to achieve full and productive employment and decent work for all (SDG 8). In particular, efforts have been made to substantially increase the number of youth and adults who have relevant technical and vocational skills for employment and promote full and productive employment and decent work, entrepreneurship, and social protection. In this regard, key intervention areas include:

- Expand SMEs,
- promotion of private investment,
- Provide the necessary support to the development of SMEs including availing adequate (finance) credit, creating market linkages/networks, and training on entrepreneurship,
- Establish occupational safety and health service system,
- Establish labour affairs administrative information system, and
- Strengthening working conditions monitoring service.

There are microfinance institutions (MFIs) operating in Ethiopia that provide financial services to low income group. The Micro Finance Business Proclamation No. 626/2009 provide the legal framework for MFIs business operation in the country.<sup>22</sup> This legal framework allows MFIs to provide financial services to rural farmers and people engaged in other similar activities as well as micro and small-scale rural and urban entrepreneurs.

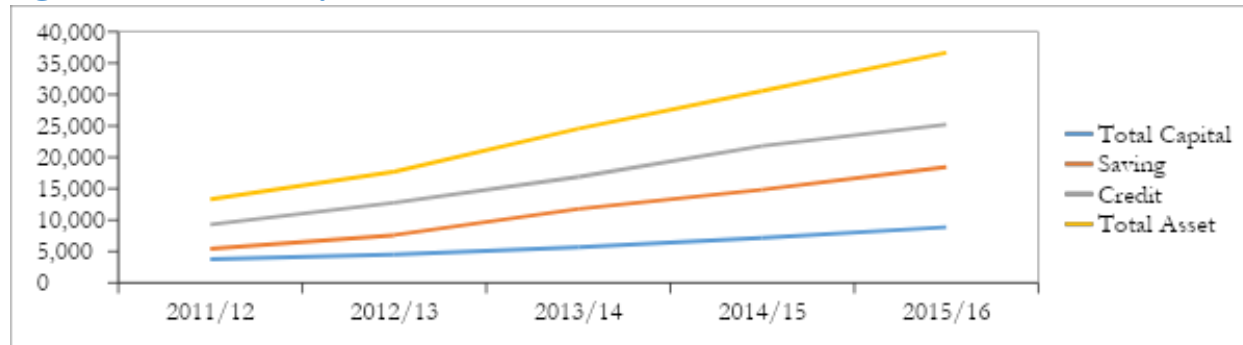
There are about 35 MFIs, with 1,593 branches across the country in 2015/16. As a result, the number of clients served by MFIs reached 4.3 million. These MFIs mobilised a total saving deposit of around Birr 18.4 billion and outstanding credit of the MFIs reached Birr 25.2 billion. As a result, their total assets increased to Birr 36.7 billion in 2015/16 (NBE, 2016). All the MFIs provide mostly small and short-term loans for small and microenterprises (SMEs) and other purposes. However, access to finance appears to be a major obstacle for micro and small enterprises and the problem is more severe for small enterprises compared with micro enterprise.<sup>23</sup> In the case of small enterprises, they are too big for MFIs in terms of the amount of loan they require, but they are too small for commercial banks in loan size, reflecting the missing middle financial intermediary that cater the needs of small enterprises. Note that the existing commercial banks don't have a special window for SMEs services nor there are specialized financial institution to cater the needs of SMEs. Hence without renewed focus on promoting SMEs through improving access to warehouses, relaxing credit constraints, and improving the macroeconomic and regulatory environment, the potential for SMEs for creating more jobs will be severely compromised.

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<sup>22</sup> Federal Democratic Republic of Ethiopia (FDRE), Micro Finance Business Proclamation No.626/2009, Federal Negarit Gazeta 15<sup>th</sup> year No.33.

<sup>23</sup> Tarfassa, S., Ferede, T., Kebede, S. and Behailu, D. (2016), Determinants of growth of Micro and Small Enterprises: Empirical evidence from Ethiopia, Research report for the Swiss Programme for Research on Global Issues, Switzerland.

Figure 20: Trends in key indicators of MFIs



Source: NBE reports

### 5.5 Domestic climate finance

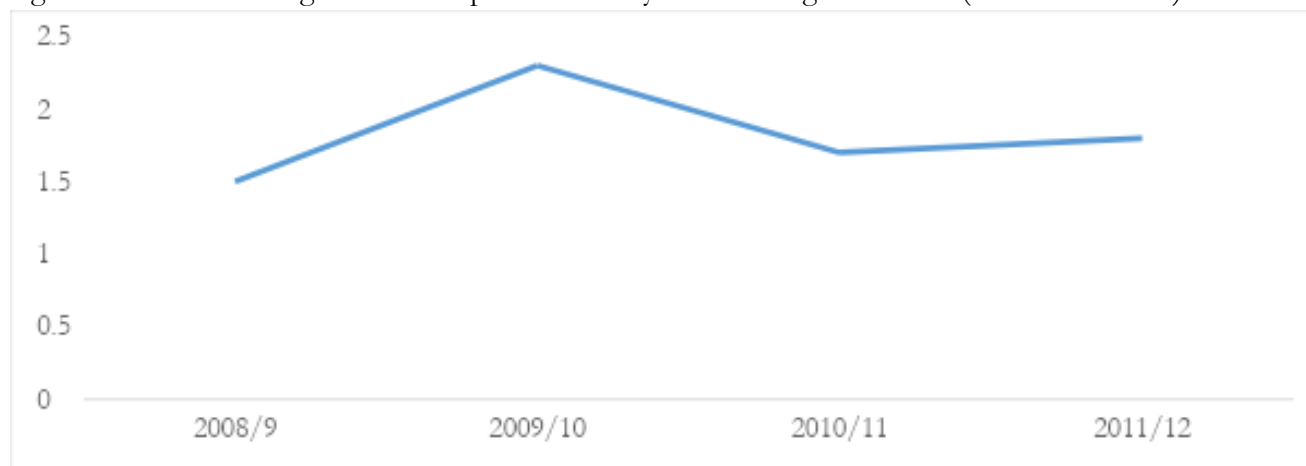
The AAAA attaches strong importance on protecting and preserving planet and natural resources, biodiversity and climate (SDGs 13, 14, 15; AAAA para 17). This requires a coherent policy, financing, trade and technology frameworks to protect, manage and restore ecosystems, including marine and terrestrial ecosystems, and to promote their sustainable use, build resilience, reduce pollution and combat climate change, desertification and land degradation.

Ethiopia also accords special emphasis on protecting the environment, manage and preserve ecosystems, sustainable use of natural resources, build resilience and address climate change. The legal context for public responses to climate change are provided in the National Environmental Policy (NEP) and the Environmental Protection Organs Establishment Proclamation of 2002 (No. 295/2002). Ethiopia is a front-runner in building an inclusive climate resilient green economy and adopted a climate resilient green economy (CRGE) strategy in 2011. The goal of the CRGE is to transform the economy from low-income country status to a lower middle-income status in rapid economic growth path that at the same time reduces greenhouse gases emission, and improves resilience to climate change. This strategy has been mainstreamed into the second Growth and Transformation Plan. In addition, in mobilizing the required resources for implementing this strategy, the Ethiopian government has established a CRGE Facility and managed by inter-ministerial steering committee. Institutional arrangements for coordinating and implementing public policy responses for CRGE are outlined in the National Environmental Policy (NEP) and CRGE Vision document. The Ministry of Environment, Forests and Climate Change (MEFCC) is in charge of coordinating CRGE planning, while the Ministry of Finance and Economic Cooperation (MoFEC) is responsible for financial aspects of the CRGE process. The CRGE Inter-Ministerial Steering Committee provides oversight of the CRGE process.

The green economy strategy takes an economy-wide approach to achieving development goals whilst limiting greenhouse gas emissions in 2030 to 2010 levels, which are estimated at 150Mt CO<sub>2</sub>e (FDRE 2011). The financing requirements of building a green economy are huge: it requires around USD 150 billion to implement green economy initiatives for 20 years, i.e. it requires on average USD 7.5 billion per year. Note that this amount does not include sectoral climate resilient investment requirements. Part of this financial requirement is to be mobilized from domestic including government budget and domestic private sector. Data on domestic climate finance is hard to identify in the country, but domestic climate finance is likely to be large. Recent study estimated that the level of climate relevant spending by federal government was on average about 15 percent of total

government expenditure or 1.8 percent of GDP between 2008/9 and 2011/12 (Eshetu *et al.*, 2014).<sup>24</sup> This figure is likely to be higher if spending by domestic private sector and regional governments is included. This requires supporting investment in data generation on climate change spending by the government and domestic private sector. In particular, support is required in establishing modern database centre for planning, implementing and monitoring climate change interventions. In addition, there is a need to conduct a comprehensive Climate Public Expenditure and Institutional Review (CPEIR) and develop a Climate Fiscal Framework (CFF) to ensure the effective use of domestic and international climate finance within the national budget process.

Figure 21: Climate change relevant expenditure at by the federal government (Percent of GDP)



Source: Eshetu *et al.* (2014)

### 5.6 Domestic philanthropy and non-governmental organizations (NGOs)

Ethiopia has a long tradition of partnership with domestic NGOs that have been supporting the government in the delivery of a wide range of services including education, health, training, women’s empowerment, microcredit, agriculture, climate change and social protection. Current data constraints do not allow estimations of the volume of investment made by philanthropic and other domestic sources. However, discussions with stakeholders indicate that domestic funding for national NGOs is limited.

Although GTP-II recognizes the roles of non-government charity organizations in the country’s development, the plan lacks details regarding strategic areas for which the government seeks partnerships with NGOs. To enhance the contribution of NGOs to help achieve the goals of GTP-II, a number of issues must be addressed including among others establishing a comprehensive database for monitoring and follow up domestic NGOs and their activities, and address the fund constraints of national NGOs. This will also help align NGOs activities with the priorities of the national development.

<sup>24</sup> Note the source of finance for climate relevant spending has not been indicated. But it is likely that government budget accounted for a large share of total climate relevant spending. According to Eshetu *et al* (2014), about government budget accounted for about 80 percent of total climate relevant spending in 2011/12.

## 6. External Finance: Analysis of institutional and policy context

The 2030 Agenda for Sustainable Development will place significant demands on public budgets and capacities, which require scaling up and more effective international support, including both concessional and non-concessional financing. To mobilize this support, the Addis Agenda contains a range of commitments and actions on official development assistance (ODA) (SDG 17; AAAA paras 50-58). It also contains commitments and actions on South-South cooperation, lending by multilateral development banks (MDBs) and other international development cooperation efforts.

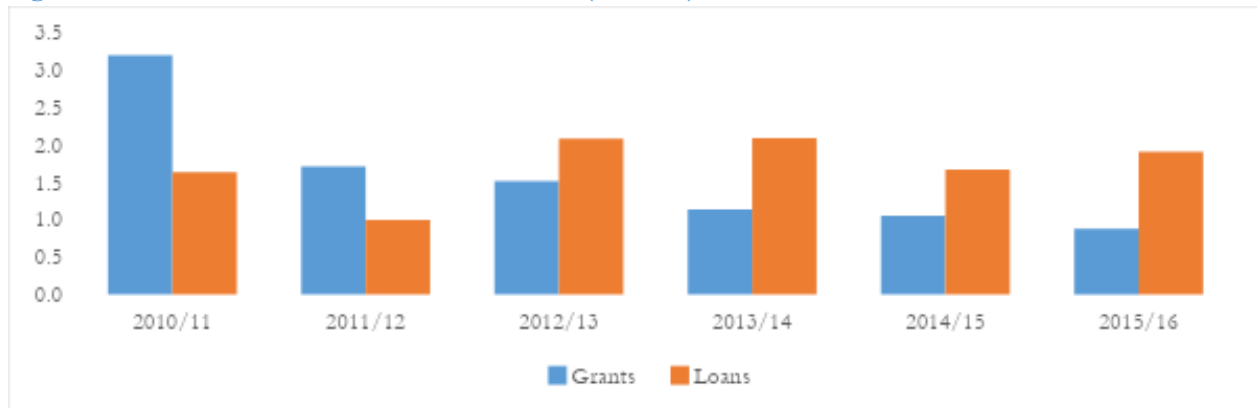
### 6.1 Official Development Assistance (ODA)

The AAAA reaffirms the ODA goals of 0.7 percent of gross national income (GNI) for all developed countries and 0.15-0.20 percent of GNI for Least Developed Countries (LDCs). These targets have not been met so far and there is nothing in the AAAA that would drive countries to meet those targets.<sup>25</sup> There are a few notable European countries that have met the targets. International public finance, including official development assistance plays an important role in complementing efforts to mobilize public resources domestically, especially in developing countries with limited domestic resources. Tapping into new partnerships and innovative sources of financing can also play a role in complementing public sources of financing sustainable development.

In the case of external sources of finance, two categories can be identified: grants and loans and the latter can be concessional or non-concessional. While the federal government is allowed to borrow from external financial institutions, State owned enterprises (SOEs) are also eligible to borrow from external financial institutions through government guarantee.

Although grants are important sources of finance in Ethiopia, their share in GDP has shown a declining trend. For instance, grants as a share of GDP declined from 3.2 percent in 2010/11 to 0.9 percent in 2015/16. On the other hand, loans as a share of GDP slightly increased from 1.6 percent to 1.9 percent. In absolute level, loans increased from ETB 8.4 billion to ETB 28.2 billion. It appears that loans have become an important source of government finance in Ethiopia.

**Figure 22: Grants and loans as a share of GDP (Percent)**



Source: Based on MoFEC data

Note that both grant commitment and disbursements declined between 2010/11 and 2015/16. For instance, grant commitment declined from USD 3.7 billion in 2010/11 to USD 1.4 billion in

<sup>25</sup> The share of ODA allocated to LDCs has declined in recent years. For example, total ODA to LDCs amounted to US\$ 41 billion in 2014, equivalent to 0.09 percent of donor countries' Gross National Income (GNI), well below the UN target of allocating at least 0.15 percent of GNI to the LDCs as ODA (UNDP and AFD, 2016).

2015/6. Grant disbursed as a share of commitment was 80 percent in 2015/16. Although loan commitment and disbursement improved, the amount of loan disbursed fall short of commitments. In 2015/16, loan disbursed as a share of commitment was only 60 percent regardless of the type of loan provider (Figure 23). Between 2010/11 and 2015/6, loan disbursed accounted for about 54 percent of the committed fund, indicating pledges have not been translated into actions. Discussions with stakeholders indicate that part of the delay in fund disbursement is due to weak performance of implementing development projects. Reliance on international assistance is problematic in a structural sense, since grant and loans come with their own problems: it tends to be fragmented (due to existence of multilateral and bilateral programs), which raises coordination issues and places administrative demands on Ethiopia’s public services; these often come with strings attached (e.g. tied to procurement requirements); and more importantly, grants and loans tends to be volatile and pro-cyclical, reflecting cyclical fiscal pressures in donor countries (Derk *et al.*, 2014).

**Table 1: Grant and loan commitment and disbursement (Million USD)**

	Grants		Loan	
	Commitmen	Disbursement	Commitmen	Disbursemen
	t		t	t
2010/11	3737.4	1894.7	1310.1	214.9
2011/12	1867.4	1590.4	1468.2	986.7
2012/13	1362.3	1576.8	2562.6	1417.3
2013/14	1050.8	1984.1	2351.6	1300.3
2014/15	658.9	1544.9	1697.3	1167.5
2015/16	1435.4	1160.0	2646.6	1597.8

Source: MoFEC (Aid platform database)

**Figure 23: Loans disbursed as a share of commitment by type of loan provider (Percent)**



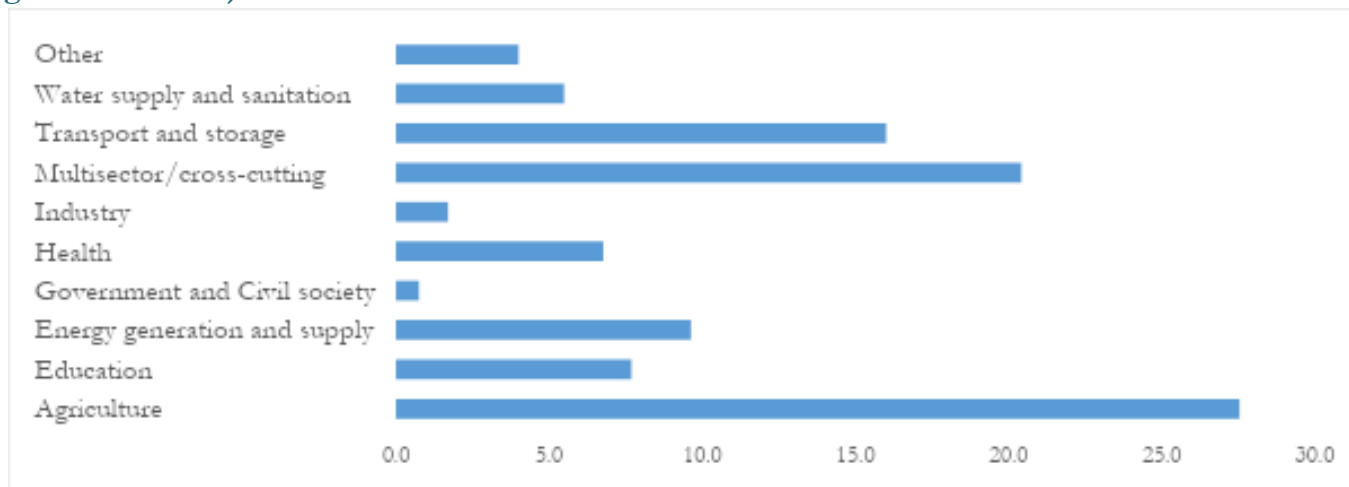
Source: MoFEC (Aid platform database)

The major sources of credit include bilateral (international and regional organizations), and multilateral (governments). Particularly, the international financial institutions such as the World Bank, IMF, the African Development Bank, the European Union, Arab Bank for Economic Development for Africa, OPEC Fund for International Development and others have been the major sources of credit. Bilateral sources consist of the country’s long time development partners mostly the Paris Club members, including United Kingdom, France, Italy, USA, Japan, and other non-Paris Club countries. Furthermore, Ethiopia has been benefiting from Asian and Middle East countries. Between 2011/12 and 2015/16, about 71 percent of the country’s external loan originated from official creditors (i.e. bilateral and multilaterals). Of this, about 41 percent was from multilateral and 30 percent from bilateral creditors. The rest (about 29 percent) was in the form of trade and other credit linked to external commercial operations of internationally active public corporations

(e.g. Ethiopian Airlines and Ethio-Telecom). This indicates that official development assistance in the form of concessional terms account for a large proportion of total loans.

In terms of sectoral distribution, ODA supports a wide variety of sectors; agriculture is the largest recipient of ODA, followed by cross-cutting and transport and storage. Energy generation and supply and education also together accounted for about 17.3 percent of total ODA between 2010/11 and 2015/16.

**Figure 24: Breakdown of ODA commitments by sector 2010/11–2015/16 (Percent of total grants and loans)**



Source: Based on MoFEC (Aid platform database)

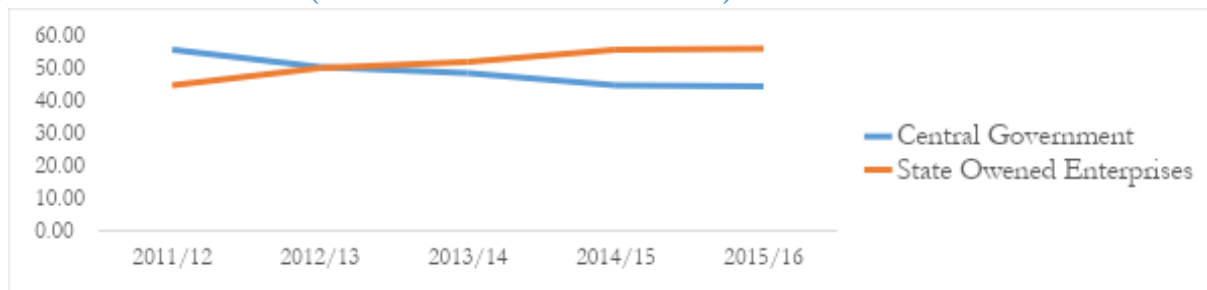
## 6.2 Debt and debt sustainability

The AAAA devotes considerable space on debt and debt sustainability. The extent to which countries borrow from external sources depend largely on their ability to repay their debt including the principle and interest (i.e. debt servicing), which in turn, depends on its export performance. Debt servicing takes resources away by (i) having less resources for public expenditure (ii) debt overhang can deter private investment and (iii) hinder new and more productive borrowing. In particular, external debt management has close links with the management of fiscal budget, foreign exchange reserves and the overall balance of payments.

### (i) Domestic debt

The share of domestic debt in total domestic debt owed by the central government declined over time: from 55.5 percent in 2011/12 to 44.4 percent in 2015/16, while that of state owned enterprises increased. This reflects a large size of domestic borrowing by public enterprises to finance infrastructural projects such as energy, railway and other infrastructural projects.

**Figure 25: Domestic debt (Percent of total domestic debt)**

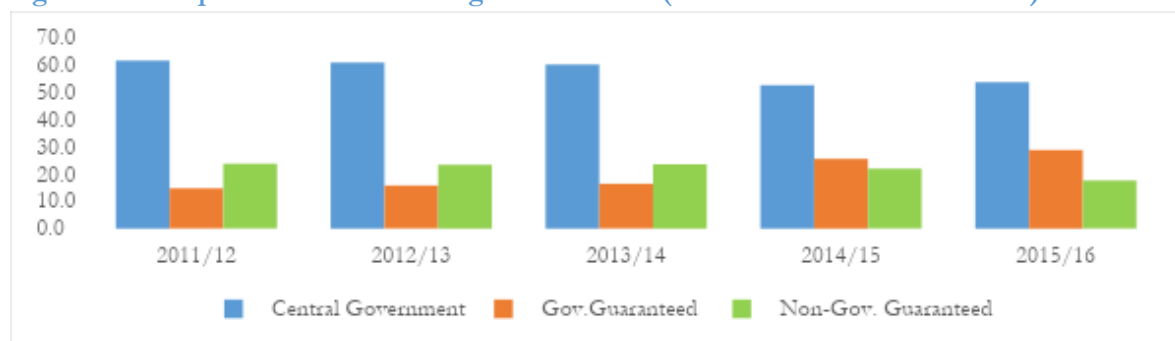


Source: Public sector debt Statistical Bulletin No.18, Debt Management Directorate of MoFEC

### (ii) External debt

In Ethiopia, aggregate public external debt includes the central government external debt (includes all external loans contracted between external creditors and MoFEC), (ii) the government-guaranteed external debt (comprises loans and suppliers credits contracted by public enterprises<sup>26</sup> guaranteed by MoFEC and the Commercial Bank of Ethiopia (CBE)), (iii) the non-guaranteed external debt including loans contracted by public enterprises (mainly Ethiopian Airlines (EAL) and Ethio-Telecom) without government or government owned bank guarantee. Total external debt increased from ETB159.2 billion in 2011/12 to ETB 470 billion in 2015/16, grew on average by about 28 percent. Total external debt as a share of GDP increased from 21.3 percent to 31.8 percent. Both the central government and public enterprises owed a large share of external debt.

Figure 26: Components of outstanding external debt (Percent of total external debt)



Source: Public sector debt Statistical Bulletin No.18, Debt Management Directorate of MoFEC

The sectoral distribution of public external debt indicates that three sectors, namely transport and communication, highway transport and electricity, gas and steam accounted for two-third of total public external debt between 2011/12 and 2015/16. Public external money goes to financing infrastructure, a small share goes to financing agriculture (6.9 percent) and industry (including tourism) (9.7 percent).

<sup>26</sup> These public enterprise include the Ethiopian Electric Power (EEP), Ethiopian Electric Utility (EEU), Ethiopian Sugar Corporation, Ethiopian Railways Corporation, and Ethiopian Shipping Lines.

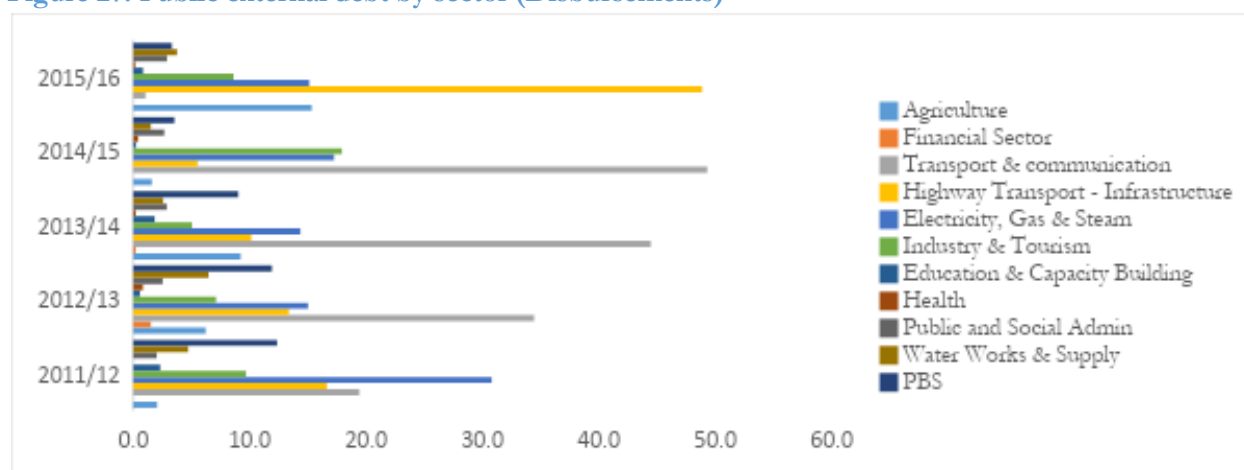


Table 2: Sources of public external debt (Percent of total external debt)

	2011/12	2012/13	2013/14	2014/15	2015/16
<b>Multilateral</b>	45.4	44.8	43.9	34.0	35.9
<b>Bilateral</b>	25.7	28.4	32.2	30.9	33.1
Paris Club	4.6	3.6	2.8	2.1	1.8
Non-Paris Club	21.1	24.9	29.4	28.8	31.3
<b>Private creditors</b>	28.9	26.7	23.9	35.1	31.0
Commercial Banks	13.7	14.6	14.5	13.6	12.0
Suppliers	15.3	12.2	9.4	16.3	14.4
Bond and Notes Holders (Eurobond)	0.0	0.0	0.0	5.2	4.6

Source: Public sector debt Statistical Bulletin No.18, Debt Management Directorate of MoFEC

Figure 27: Public external debt by sector (Disbursements)



Source: Public sector debt Statistical Bulletin No.18, Debt Management Directorate of MoFEC

The AAAA recognizes the IMF and World Bank debt sustainability analysis framework. Key debt sustainability indicators include debt-to-GDP ratio, debt-to-revenue ratio and debt-to-export ratio and these indicate the capacity to contract loans and repay them. All indicators show increasing trend between 2011/12 and 2015/16 (Table 3).

Table 3: Key indicators of public external debt

	2011/12	2012/13	2013/14	2014/15	2015/16
Public external debt as % of GDP	21.3	24.2	26.2	31.7	31.8
Public external debt as % of revenue	154.7	168.7	187.6	210.4	202.8
Public external debt as % of revenue and grants	137.6	152.5	173.5	196.7	192.0
Debt service as % of exports	7.0	9.7	10.4	16.5	
Debt service as % of GDP	1.0	1.2	1.2	1.6	1.4
Debt service as % of revenue	7.0	8.4	8.8	10.7	9.0
Debt service as % of revenue and grants	6.3	7.6	8.1	10.0	8.5

Source: Based on MoFEC data

The International Monetary Fund (IMF) ranks countries as high, medium and low risk based on their external debt burden. According to the 2015 Country Policy and Institutional Assessment (CPIA) score (3.4), Ethiopia is classified as a medium performer (IMF, 2016). So, the thresholds for debt burden for the medium performer are 150, 40, and 250 percent for the present value (PV) of debt to exports, GDP, and revenue ratios, respectively. Both the PV of public external debt to GDP

and revenue ratio are projected to within the threshold. Only the PV of debt to exports is projected to be out of the threshold during the GTP-II period. The disappointing performance of the export sector has become a real concern and affects the borrowing capacity of the country. The ongoing investments in transportation, power and other infrastructure are expected to enhance export competitiveness of the country which would help boost its capacity to repay its debt. The government remains committed to sustain a healthy external debt through allocating the borrowed money to infrastructural and energy projects that enhance the productive capacity of the economy, promote export and industrial development. Consultations with stakeholders indicate that there is a need to ensure effective utilization of external resources and improve project planning and management capacity to execute projects on time and with the required quality.

**Table 4: External public debt sustainability indicators outlook**

	Threshold	2016	2017	2018	2019
PV of Debt to Exports Ratio	150	255.6	250.9	243.9	226.0
PV of Debt to GDP Ratio	40	21.9	22.4	22.3	21.3
PV of Debt to Revenue Ratio	250	127	129.3	126.7	117.6

Source: IMF (2016)

Looking to the future, external financing, primarily in the form of concessional loans from official multilateral and bilateral sources, but increasingly loans on non-concessional terms will continue to supplement public investment needs of the country.

### 6.3 Remittances

The level of international migrants stock increased by 7.9 percent per year between 2010 and 2013. During this period, some 45,876 migrants were added annually, with 24741 male and 21135 female migrants.<sup>27</sup> International remittance forms the major share of development financing in Ethiopia. Remittances have been growing rapidly by about 25.9 percent per annum and reached close to ETB 126.7 billion in 2015/16, higher than the value of merchandise exports during the same period. Note that actual remittance inflows to Ethiopia could be higher than that reported by the National Bank of Ethiopia as people use informal ways of transferring money.<sup>28</sup> Remittances have become an important source of foreign exchange in Ethiopia and helped narrow the deficit in the balance of payments.

There are different factors affecting the inflow of remittances including among others remittance fees for transferring remittances, size of Diaspora, and accessibility of money transfer agents. At global level, fees are expensive, at average 8 percent and the figure for sub-Saharan Africa is even more expensive at 12 percent.<sup>29</sup> Improving access to formal banking services shall be a key step forward to reduce the cost of remittances and this could also facilitate savings, future access to microcredit for productive activities and to extend access and improve monitoring of a variety of social protection services. In addition, the cost of transferring remittances can also be reduced by fostering competition through encouraging other institutions, such as post offices, cooperatives, microfinance institutions, or possibly telecom operators to play a larger role in money transfer. By these means the use of remittances could be used to boost greater financial inclusion. International

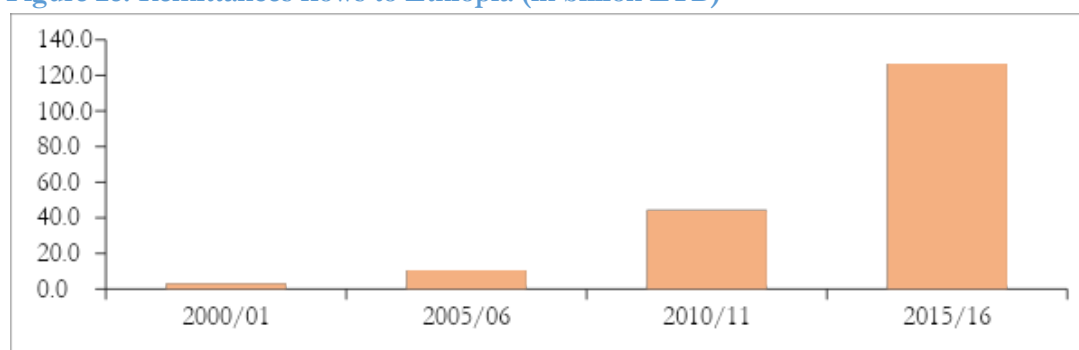
<sup>27</sup> UN, Population Division; POP/DB/MIG/Stock/Rev. 2013

<sup>28</sup> For instance, close to 46 percent of remittances were channeled through informal ways in 2008/09 (Assaminew *et al.*, 2010).

<sup>29</sup> Schmidt-Traub, G. and Sachs, D.S. (2015), The roles of public and private development finance, Issue Brief, Sustainable Development Solutions Network.

remittances inflow can also be facilitated by opening up bank branches or money transfer agents in areas where there is large concentration of Diaspora, with certain incentives to reduce transfer fees. Although the medium-term development plan (GTP-II) recognizes the role of remittances as a source of foreign exchange, it does not explicitly address this with the same level of priority and does not provide any explicit operational linkages between national priorities. For instance, there are no indicators to monitor remittances and promote remittance flow and utilization.

**Figure 28: Remittances flows to Ethiopia (in billion ETB)**



Source: NBE (2016)

The Ministry of Labour and Social Affairs (MoLSA) is responsible for formulating policies, plans, enacting laws, rules and regulations, and monitoring relating to the management of overseas employment as well as overall welfare of expatriate workers. There seems to be ample room for improving the impact of remittances on savings and productive activities. Remittances are mostly directed to support consumption in Ethiopia and are not fully used to develop productive activities.<sup>30</sup>

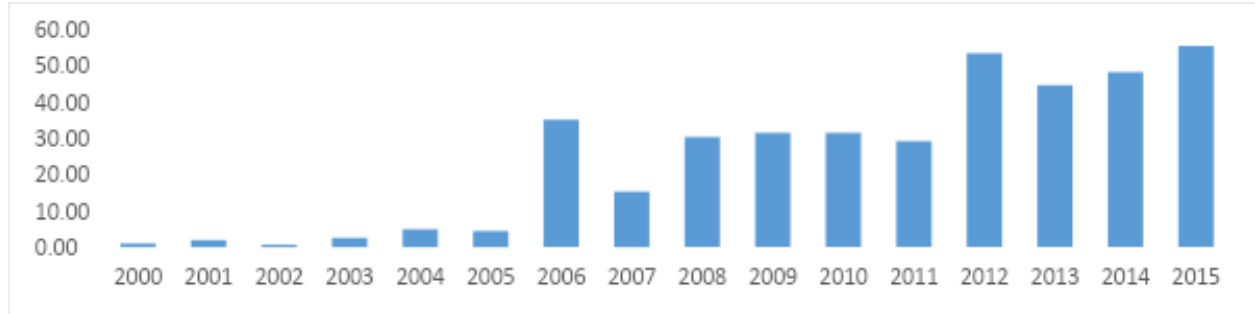
## 6.4 Foreign direct investment (FDI)

Foreign direct investment (FDI) is also regulated by the investment Proclamation No.769/2012. The investment proclamation also identifies priority sectors including light manufacturing (e.g. textiles, leather, agro-processing, agriculture, etc.). Foreign investors who wish to invest in the priority sectors are also entitled to get incentives as indicated in the proclamation. These incentives include export promotion (e.g. zero tax on exports, duty drawback scheme and bonded warehouse), investment tax incentives (e.g. tax holidays and duty free import of capital goods), and non-tax incentives (e.g. foreign exchange retention and export guarantee).

The various incentives mechanisms seem to have stimulated FDI flow to Ethiopia which has increased sharply in the last 15 years from less than one billion birr in 2000 to over ETB 55 billion in 2015. FDI grew on average by about 29 percent per year between 2000 and 2015. Of the total FDI, wholly foreign origin accounted for about two-third of total FDI, while joint venture accounted for the rest. However, FDI flows lack diversification across country of origin, with China, India, Turkey and others from Middle East account for a large proportion of FDI in Ethiopia.

<sup>30</sup> See Ferede, T., Admassie and Nuru, S. (2015), Migration and forced labour of workers from selected regions of Ethiopia, research report prepared for ILO.

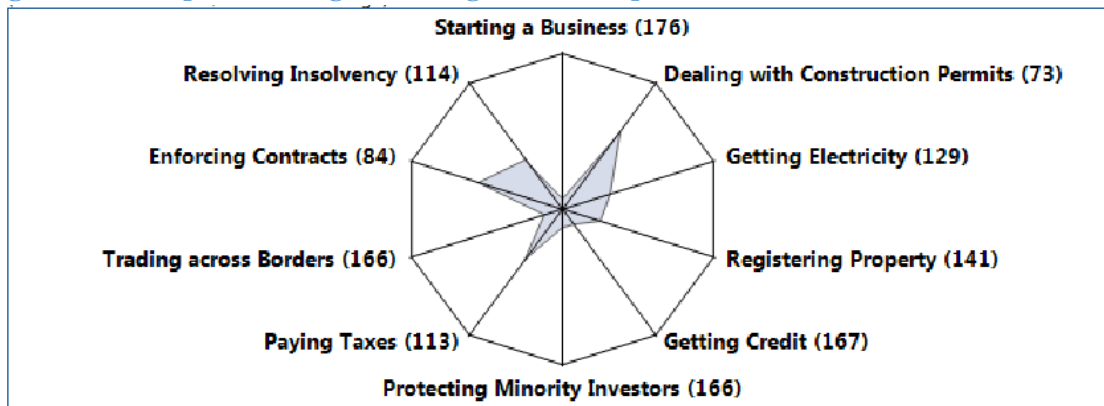
**Figure 29: Foreign direct investment (in billion ETB)**



Source: Ethiopian Investment Commission

Creating an enabling business environment in terms of stable and transparent regulatory systems, good investment climate and sound macro-economic and financial policies are essential to attract FDI and improve diversification through targeted interventions to enhance quality FDI. The World Bank Ease of Doing Business Index can be used to judge a country’s investment climate situation. Ethiopia ranked 146 out of 189 in 2016 on ease of doing business in 2016 and its score is slightly above the regional average but lower than other African countries such as Kenya, Rwanda, Uganda and Egypt. In 2017, Ethiopia’s rank in ease of doing business deteriorated: it ranked 159 out of 190 countries (World Bank, 2017). Ethiopia also lags behind in some specific ease of doing business indicators such as starting a business and getting credit, which the country ranked 176 and 167 out of 189, respectively, which is far below the SSA average ranking and other well-performing peers such as Rwanda (World Bank, 2017). Firms that are credit constrained exhibit poorer performance, productivity and competitiveness.

**Figure 30: Ethiopia’s rankings on Doing Business topics, 2016**

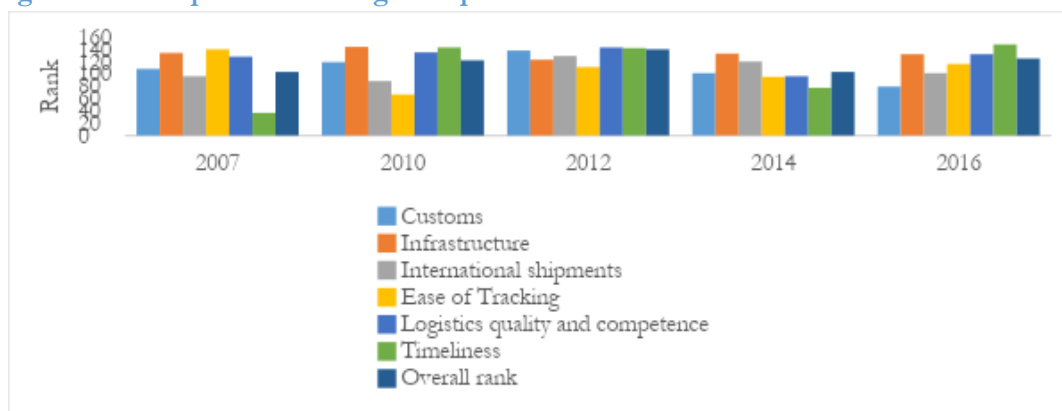


Source: World Bank (2017)

The Ethiopian government sets a target of improving logistics services to enhance competitiveness from 104<sup>th</sup> in 2014 to 57<sup>th</sup> by the end of plan period. However, the early signs are not encouraging. The country performs badly in the World Bank’s Logistics Performance Index (LPI): its overall rank in LPI deteriorated from 104<sup>th</sup> in 2014 to 126<sup>th</sup> in 2016. High logistics costs reduce the competitiveness of Ethiopian goods and services compared with its competitors. In particular, the country lags behind in simplifying customs procedures, logistics competence, and tracking and tracing. Poor trade logistics tends to erode the benefits of lower labour cost and increases transaction costs, thereby adversely affecting competitiveness of private firms (AfDB, 2014b). Discussions with stakeholders indicate that investments are being made to improve logistics efficiency including

investments in building infrastructure for cargo tracking and mobile scanning, but the application of these technologies, especially tracking technologies is hampered by high initial costs for private sector as tracking technologies need to be installed in each transport car.<sup>31</sup> In addition, weak coordination among different actors involved in the logistics services has remained a challenge since there is no coordination mechanism in place, and this calls for interfacing the different actors to improve efficiency in logistics services and information.

**Figure 31: Ethiopia's rank in logistics performance index**



Source: World Bank (various reports)

Barriers to private sector involvement in sustainable development investment include higher up-front costs (most sustainable investments impose higher up-front costs), greater technological risks, especially under local conditions as most climate-related technologies have not penetrated local markets, lack of awareness regarding options for addressing sustainable development challenges, limited relevant expertise/capacity among the actors involved in delivering sustainable development actions, limited capital market instruments due to underdeveloped capital markets, regulatory uncertainty, and inadequate institutional capacity (both technical and financial).

As articulated in the GTP-II, the following interventions are envisaged to enhance the domestic private sector and attract FDI.

- expansion of special economic zones or specialized industrial parks with the required infrastructure and streamlined public procedures as well as fiscal and trade policy incentives
- provide more efficient trade logistics and transport services and energy supply,
- supply of land mainly through industrial parks approach,
- trade and customs facilitations; and
- priority supply of credit and foreign exchange

There are notable initiative by the government to curb the multiple problems constraining the private sector. The completion of the Ethio-Djibouti railway project, which is currently in the final stage, would help reduce transportation costs, and enhance logistics efficiency. There are also similar investments in the railway sector to connect different areas of the country. The impact of these investments on industry and export growth is expected to be large as railway transport is cost effective compared to road transport.

The establishment of integrated industrial development parks across the country is also another initiative by the government which will ease not only the logistics hurdles but also other constraints as these parks are expected to avail the necessary infrastructure including one-stop-shop services for

<sup>31</sup> Initial investment cost in installing tracking technologies in private transporters is high, which is more than USD 2,000 per machine per car. Companies with many transport cars need to invest a large amount to install tracking technologies in each car. High upfront cost hinders the application of tracking technologies (Discussion with ERCA representative).

investors investing in designated industrial parks. Recently two industrial parks have become operational including Bole Lemi I and Hawassa. There are also a number of upcoming industrial parks in Ethiopia including Bole Lemi II, Kilinto, Adama, Dire Dawa, Kombolcha, Mekelle, Arerti, and Debre Berhan industrial parks.<sup>32</sup> These parks are dedicated for specific sectors such as textile & apparel, leather & leather products, pharmaceuticals, agro-processing etc. The government of Ethiopia established the Ethiopian Industrial Parks Development Corporation (IPDC) in 2014 to accelerate economic transformation, promote and attract both domestic and foreign investors. Development of industrial parks enjoys strong government support and investment policy, and these parks are located along key economic corridors and connected to ports surrounded by infrastructures such as airports, railway lines, dry ports, universities, etc. There is a need to deepen these initiatives to trigger further transformation.

**Box 6: Integrated industrial parks development in Ethiopia**

The government has already built two industrial parks on the outskirts of Addis Ababa, Bole Lemi and Kilinto and another in Hawassa town. The Ethiopian government also plans to establish additional industrial parks to boost manufacturing industries. The industrial parks will be located Bahir Dar, Jimma, Adama, Kombolcha and Mekelle. The government of Ethiopia with support from UNIDO has also developed a master plan for integrated agro-industrial parks (IAIPs) in four regions, namely Bure (Amhara), Baeker (Tigray), Bulbula (Oromia), and Yirgalem (SNNPR) to advance inclusive and sustainable industrialization and rural transformation. The feasibility study has identified 17 agro-industrial corridors, and a phased approach to be followed in the development of IAIPs and RTCs. In the first phase, four IAIP and 28 RTCs are being piloted in four regions mentioned above and these have been selected based on agricultural production potential of strategic commodities, infrastructure, potential inter-industry linkages and triggering effects, market potential, access to commercial and support services, and enterprise concentration and attractiveness (UNIDO, 2016).

Medium- and large-scale food processing companies in Ethiopia are constrained by shortage of raw material inputs (both in quantity and quality). This is due to two interrelated factors: poor quality inputs, and collection inefficiencies due to the large number of smallholder farmers scattered over large areas. Addressing these challenges helps the agricultural sector to drive agro-industrial development and underpin future economic growth. Recognizing this, the government of Ethiopia has developed a master plan for rural transformation centres (RTCs) which serve as raw material aggregation points in the catchment areas (100 km radius) of each IAIP. Rural transformation centers provide several functions including warehouses, input supply, sorting, grading, extension services, pre-processing activities and microfinance.

Source: UNIDO (2016)

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<sup>32</sup> See

<http://www.investethiopia.gov.et/investment-opportunities/strategic-sectors/industry-zone-development>

## 6.5 External climate change finance

External climate finance in Ethiopia refers to flow of funds toward adaptation and mitigation measures. Ethiopia has set Intended Nationally Determined Contributions (INDC) of emission reduction to 64 percent compared with the business as usual scenario by 2030. The Ministry of Finance and Economic Cooperation (MOFEC) has been accredited by the Green Climate Fund (GCF) in 2016 to directly access external resources of small size projects with a total project of up to USD 50 million. MoFEC has submitted two investment projects to Adaptation Fund (USD 10 million) and GCF (USD 50 million). There are also other projects under preparation to be submitted to GCF.

The Ministry of Finance and Economic Cooperation (MOFEC) in collaboration with relevant institutions has the responsibility to mobilize finance from domestic and international sources, allocate to key CRGE sectors and ensure effective and efficient use thereof. Between 2010 and 2014, the government of Ethiopia has mobilized over USD 450 million from bilateral and multilateral development partners. In addition, the UN-REDD Readiness Programme (United Nations Programme on Reducing Emissions from Deforestation and Forest Degradation) is also a funding source for climate change mitigation through forestry and land use change. Ethiopia is a participant country of the World Bank Forest Carbon Partnership Facility (FCPF) and the national REDD+ programme is funded through the FCPF Readiness Fund. In October 2012, the FCPF approved a Readiness preparation grant of USD 3.6 million. Recently, Ethiopia received about USD 118 million through REDD+ programme from the World Bank and Norway to support investment in forest. Note that external climate finance flow to the country is likely to be large, but data is difficult to gather as a comprehensive database is lacking to track climate related external finance flow in the country.

The government of Ethiopia will need to continue its scaling-up of public expenditures to deliver transformational changes and to meet SDGs targets. The achievement of these calls for utilizing a combination of multiple sources and instruments of finance. Considering the revenue trends and the increasingly grim outlook for external resource inflows, there is a need to look for availability of potential ‘non-traditional’ financial resources that will help Ethiopia sustainably finance its development interventions. In light of this, it is necessary for Ethiopia to examine its financing framework and consider other sources of financing to deliver its development aspirations.

## 6.6 South-South Cooperation (SSC)

Ethiopia maintains strong development cooperation with many non-traditional donors such as China, India, Kuwait, Brazil, Saudi Arabia, Turkey and United Arab Emirates. It has also developed strong relations from traditional donors, namely Japan and Republic of Korea. Since 2011/12, Ethiopia has mobilized USD 1.75 billion through official assistance from China, India, Kuwait and Saudi Arabia. The financial linkage with these countries is mainly in the form of loans (1.74 billion) with small grant element (USD 8.2 million).

The Ministry of Finance and Economic Cooperation through its Economic Cooperation wing maintains external economic relations and resources, including with countries from the Global South. Ethiopia is pursuing SSC through the following mechanisms:

### (i) Regional trading Arrangements

Ethiopia is a member of different regional blocs which have, sometimes, different objectives. Due to its geographical location, Ethiopia is one of the signatories to the Common Market for Eastern and Southern Africa (COMESA). Ethiopia is also a member of Inter- Governmental Authority for Development (IGAD) and the Sana’a Forum for Co-operation (SFC). The Ethiopian

government is engaged with multilateral and regional trade negotiations. These negotiations are accession to the World Trade Organization (WTO), the New Economic Partnership Agreement (EPA) with the European Union, Common Market for Southern and Eastern Africa (COMESA) Free Trade Agreement (FTA), and Continental free trade area (CFTA). Note that while TFTA, COMESA-FTA, IGAD and SFC are all Sub-Saharan regional economic integration agreements (i.e. South-South cooperation), the Economic Partnership Agreement with the European Union is a North-South agreement. Ethiopia enjoys quota- and duty free access to European market under the Everything But Arms trade agreement and the USA market under Africa Growth Opportunity Act (AGOA).

The impacts of regional trade agreements can be assessed in terms of trade flows. In particular, studies indicate trade flow with COMESA member countries is limited. The share of intra-COMESA exports accounted for on average 10.9 percent of total merchandise exports between 2001/2 to 2012/13. Ethiopia’s trade relationship is relatively strong, especially with Asian and European countries.

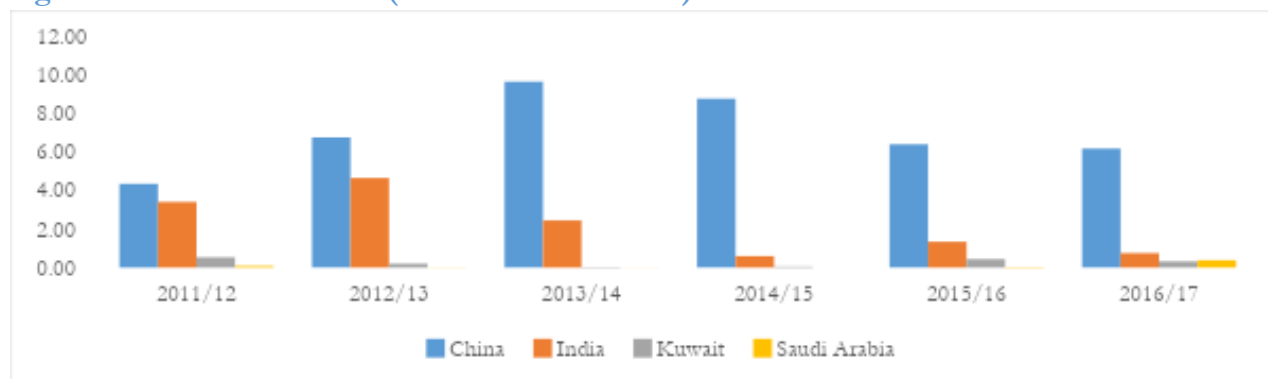
### (ii) Bilateral trade relations

Ethiopia has engaged with a number of bilateral trade agreements, and has entered into bilateral trade agreements with a number of countries. Among the list of countries which Ethiopia has bilateral trade agreements, the country has relatively strong trade ties with Djibouti, India, Sudan<sup>33</sup>, China, and Malaysia. Ethiopia’s trade with India, China, Russia, Turkey and Malaysia has increased. For instance, exports to India increased from about 0.99 percent of total merchandize exports in 2005/6 to 1.2 percent in 2012/13. Likewise, imports from India increased.

### (iii) Bilateral Financial Assistance

Top partners from the Global South for bilateral financial assistance include China, India, Kuwait, and Saudi Arabia. The financial assistance is largely in the form of loans, with small grant element. China is the main source of financial assistance to Ethiopia (with USD 1.3 billion loan and 8.2 million grant between 2011/12 and 2016/17).

**Figure 32: Grants and loans (Percent of total ODA)**



Source: Based on MoFEC (Aid platform database)

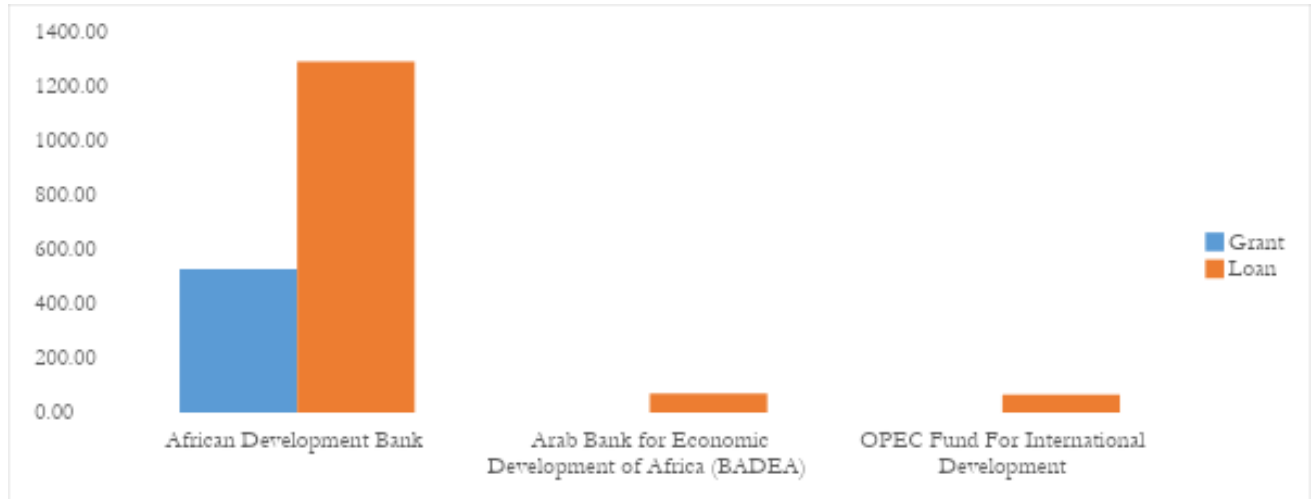
### (iv) Multilateral Financial Institutions from the South

<sup>33</sup> Ethiopia has also signed a free trade agreement with Sudan to foster free trade by eliminating barriers to trade and promoting free competition.



Ethiopia receives concessional loans and grants from Southern multilateral institutions, mainly from African Development Bank (AfDB), Arab Bank for Economic Development of Africa (BADEA) and others. The Africa Development Bank has remained the main source of financial support (both in the form of grants and loans).

**Figure 33: Total fund flow (In million USD)**



Source: MoFEC (Aid platform database)

The overall picture from SSC is encouraging as this emerging source of finance has great potential for Ethiopia to meet its development aspirations. A large proportion of SSC focuses on priority sectors, an indication that such cooperation is demand driven. In fact, most of the investment focus on agriculture, infrastructure development and manufacturing. Other key national development goals, like education, skill development, health and others need to get supported by the SSC framework. There is also a need to establish systematic database for SSC for effective monitoring and evaluation of SSC.

## 7. Key findings, priorities areas and matrix of interventions

The Ethiopia has shown substantive strides in articulating sustainable development as reflected in its development policies, strategies and plans which incorporate sustainable development (SD) principles and objectives. Economic goals include raising productivity in agriculture, improving social services, promoting industrial development, and filling significant infrastructural gaps in power, transportation (both road and railway) and telecommunications. Specific targets include to achieve a lower middle-income status by 2025 and to meet the sustainable development goals (SDGs) by 2030. The scale of resource requirement is very large; budgetary government spending and public enterprise off-budget spending are projected to increase significantly during the GTP-II period and beyond. The 2030 Agenda requires both significant increases in resources and changes in the way existing resources are used and prioritized, calling for more effective integrated approaches to managing public and private finance to achieve sustainable development priorities. This also requires adoption of Integrated National Financing Frameworks (INFFs) to mobilize resources to achieve GTP-II and SDGs. In the section, we provide a snapshot of development finance assessment findings and identify priority areas for intervention.

### 7.1 Key findings based on the development finance assessment (DFA)

The Ethiopian government has already developed a comprehensive medium-term development plan (GTP-II) for 2015/16-2019/20 with similarly aggregate indicative cost estimates. The plan lacks detailed indicators and targets for minor financial flows from sources, indicating a need for an integrated financing strategy and plan.

Tax revenue has remained low compared to the tax revenue generating capacity of the economy, the financing requirements of the development programs and the average performances of the sub-Saharan countries. This indicates existence of some kind of inefficiency in tax administration and structural problems in the tax system including among others weak information technology administration system, inaccurate database, weak compliance risk management program, lack of electronic payment facility, weak internal audit function not providing oversight on all key operations, lack of impact assessment or evaluation of compliance activities, relies on use of manual operations (outside of SIGTAS), deficient VAT refund system, and weak coordination among key directorates and with branches. Support is required to improve the transparency, efficiency and effectiveness of the tax system, by broadening the tax base and continuing efforts to integrate the informal sector into the formal economy and to develop modernised, progressive tax systems that encourage private sector development, and reduce the volume of illicit flows leaving the country.

Although the financial sector has shown rapid expansion, the coverage is inadequate compared to the size of the country's population and there is huge finance outside the banking sector. This can be mobilized through public education and mobilization around domestic savings, maintaining positive real interest rate, expanding and improving financial institutions including microfinance institutions, and deploying saving instruments including contractual savings and services such as saving for housing program, saving for investment equipment scheme, bonds, social security saving, and health insurance saving.

Public-private partnership (PPP) can help to narrow the gap between public service delivery and public service demand, thereby improving the quality of social services, but challenges remain

including weak technical and managerial capacity to execute PPP contractual arrangements, inadequate awareness about PPP, lack of specific legal frameworks, lack of a standardized PPP operating procedure, weak contract negotiation capacity, and financial constraints. The PPPs are needed to improve national infrastructure limitations that are hindering private sector investment.

Despite robust economic growth in the past decades, ensuring inclusiveness has remained a problem. This requires a combination of growth enhancing interventions and social protection programs. Expansion of SMEs has been identified the main entry point for enhancing inclusiveness, but SMEs face a number of challenges related to finance, technical, market, premises and other. The existing commercial banks don't have a special window for SMEs services nor are there specialized financial institution to cater the needs of SMEs. This calls for promoting SMEs through improving access to warehouses, relaxing credit constraints, and improving the macroeconomic and regulatory environment, the potential for SMEs for creating more jobs will be severely compromised.

A more strategic and innovative management of ODA, SSC and CCF is required. ODA, South-South Cooperation (SSC) and climate change finance (CCF) are key resources from which to begin to build an integrated financing strategy. They are all linked with international public flows of finance and have some relationship with national budgets. It is necessary to further exploit the synergies between ODA and CCF and advocate availability and additionality of resources. In this regard, a coherent framework is needed to ensure that climate finance is new and additional to existing ODA commitments and there is also a need to ensure integration of climate funding within the overall national development strategy.

Remittances have become an important source of foreign exchange in Ethiopia and helped narrow the deficit in the balance of payments. Remittances are potentially important for promoting inclusive finance and promoting expansion of SMEs, but GTP-II does not explicitly provide details about remittances nor any explicit operational linkages between national priorities. There is a potential to increase remittances through encouraging other institutions, such as post offices, cooperatives, microfinance institutions, or possibly telecom operators to play a larger role in money transfer. There could also help increase remittance-related investment directed to investment in owned/partnership farms/business, agricultural machinery purchase or in other types of SME investment.

Despite efforts by the government to improve the business environment, bottlenecks still remain. Private investment is beset by a number of challenges including high logistics cost, limited credit access, weak coordination among public service providers, and other infrastructural bottlenecks. Interventions are required to enhance the domestic private sector and attract FDI including expansion of special economic zones or specialized industrial parks with the required infrastructure, streamlined public procedures as well as fiscal and trade policy incentives, provide more efficient trade logistics and transport services and energy supply, supply of land mainly through industrial parks approach, trade and customs facilitations, and priority supply of credit and foreign exchange.

Availability and quality data and information remain a challenge. Improvement of national data, information and knowledge availability is also needed. While the availability of data has improved, there is still scope to build and improve the quality of existing statistical and management information Systems. Domestic and external climate finance needs to be tracked across ministries, using climate fiscal framework. There are also several other areas (e.g. PPPs, NGOs, and domestic climate finance, and philanthropy) where key data is not systematically collected. Overall, the

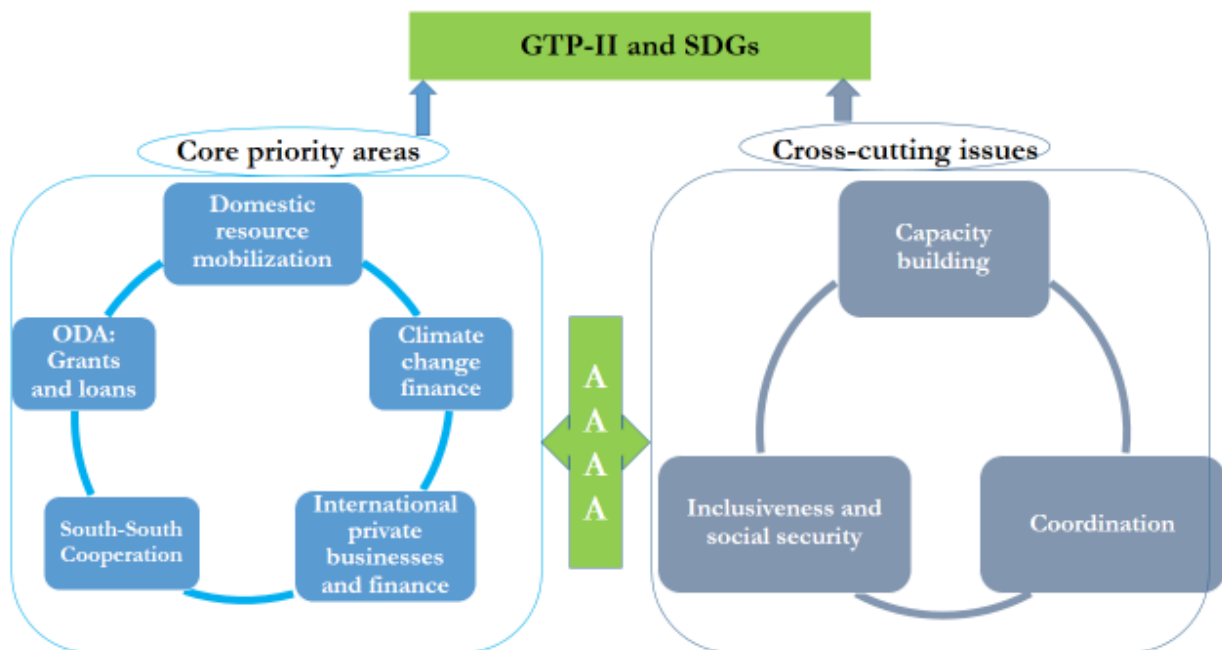
production of knowledge needs to be improved through investment, which could add value to the management of financial flows.

## 7.2 Priority areas

The DFA indicates that mobilisation of the wider variety of resources are needed to achieve the objectives of GTP-II and SDGs. The development finance assessment (DFA) also identifies a range of financial flows including ODA, FDI, PPPs, SSC, climate change finance and remittances that could be instrumental to achieve development objectives of Ethiopia. Based on thorough analysis of the different dimensions of the Addis Ababa Action Agenda, the national context, and findings from the DFA, key priority areas have been identified which are grouped into two categories: Core and cross-cutting issues, with each priority area has specific dimensions. These priority areas are building blocks of implementing the AAAA roadmap to achieve GTP-II and SDGs objectives. The core priority areas are anchored in five dimensions, while the cross-cutting issues are built around three dimensions. The details of the individual dimensions that make up this roadmap are presented subsequently.

This roadmap shall aim to achieve the following objectives: (i) expanding domestic resource mobilization; and (ii), diversifying external resources, (iii) capturing and scaling up private sector investment; (iv) strengthening coordination and improving the quality of finance, including the efficiency and effectiveness of expenditures and their alignment with national priorities.

**Figure 34: Dimensions of the roadmap**



Source: Own construction

### 7.2.1 Core priority areas

Considering the magnitude of the financing needs for meeting sustainable development targets, further sources of finance are required to maintain the growth momentum and continue pursuing public investment programmes. In particular, the non-traditional financing sources, which if tapped, would augment the traditional financial resources of the country and thereby providing additional fiscal space for the government to finance its development programmes. Based on the national vision, development policies and priorities, regional and global perspectives, and stakeholder consultations, core priority intervention areas are identified. The core priority areas consists of four broad dimensions, namely domestic resources, grants and loans, international private finance, and climate finance.

a. **Enhance domestic resource mobilization**

Ethiopia has challenges in terms of development financing and requires a significant boost to its domestic resource mobilization programme to maintain the pace of development achieved in recent years, deepen structural transformation, achieve the GTP goals, and to achieve its longer-term aims in terms of the SDGs and reaching a lower middle-income status by 2025.

**(i) Enhancing domestic saving:** Ethiopia's resource gap (the difference between domestic saving and domestic investment) has remained large at 17.1 percent of GDP in 2014/15, indicating dependence on international savings to finance its investment. Two areas worth mentioning to boost the domestic saving including enhance private and government savings. The former can be enhanced through financial inclusion (e.g. through improved access to financial services), financial literacy, creating decent work opportunities, etc. There is also a need to raise government saving through effective administration of tax policies, broaden tax coverage, prioritize government expenditure to capital investment, efficient and utilization of budget (through improved service delivery, project management and planning), focus on sectors that accelerate capital accumulation, and reducing wastage and improving transparency on expenditure. In particular, strengthen and expand saving instruments including contractual savings and services such as saving for housing program, saving for investment equipment scheme, social security saving, and health insurance saving.

**(ii) Raising domestic revenue:** Domestic revenue, which consists of both tax and non-tax revenues, forms a key source for financing development interventions. There is a wide gap between tax capacity and actual tax revenues raised due to among others limited tax base, narrow tax coverage, high compliance cost, and tax administration challenges.

- **Broadening the tax base:** Although Ethiopia's tax system has been modestly buoyant, its share in GDP remained low. The tax base of the country is confined to a limited number of tax items, suggesting the need for broadening the tax base through introducing new taxes (e.g. property tax) and charges (e.g. Charges for drainage services on building owners). There is also a need to assess the tax potential of the country to identify promising and feasible tax bases which help design a national resource mobilization strategy to guide future strategic interventions.
- **Reduce the cost of paying taxes:** Give the relatively high tax compliance cost in Ethiopia, efforts are required to reduce this cost through introducing reforms. From a business cost perspective, tax compliance with the documentation requirements needs substantially more time, a factor which has increased the difficulty of doing business in Ethiopia. There is a need to develop a comprehensive programme to improve voluntary tax compliance through tax education, revisit the tax system and administration, establishing a modern and reliable trade information system, providing continuous capacity building for exporters, raising the efficiency of trade registration and licensing system and promote use of electronic payment

system. Strengthening the SIGTAS (Standard Integrated Government Tax Administration System) for self-help services such as online registration, filing, payment and reports to considerably reduce the time costs and the overall tax compliance costs for businesses. Introduce a simplified presumptive tax for small, informal businesses, in part to drive activity into formal enterprises. In addition, ERCA in collaboration with relevant institutions (e.g. financial institutions such as banks) could also explore the option of using mobile filing and payment. This needs to be supported by educating and training businesses, including training in general tax compliance and how to complete electronic filing systems. In addition, there is a need to encourage business to use technologies (e.g. computers and softwares) not only for business and bookkeeping but also tax accounting purposes through providing inclusive training.

- **Increase tax coverage:** There is a need for expanding the tax coverage by capturing new businesses into the tax net through education, awareness creation, and collecting relevant information to provide tax identification number (TIN) for each potential taxpayer. Establish a robust communication between various agencies for better tax coverage, specifically with branches of the Revenue Authority, Investment Commissions, Transport Office, Chamber of Commerce, and Trade and Industry offices.
- **Introduce capital markets:** New ways of looking at development finance are required including the use of capital markets to leverage the resources needed to implement sustainable development interventions. Ethiopia has successfully established a commodities exchange market but does not have a securities exchange market to mobilize the necessary financial resources. There is no bond market or secondary market in the country; shares have been traded openly, but people face problems of liquidation when the need arises. Absence of an organized secondary market puts a straightjacket to domestic resources mobilization efforts. This calls for establishing a secondary market to raise finance domestically which will also be the basis for establishing a full-fledged stock market. The establishment of this market could also help attract finance outside the formal banking sector and help mobilize the necessary finance for development by facilitating efficiency in resource allocation and contribute to market discipline through price signals, information production, and takeover activities.<sup>34</sup>
- **Reducing the cost of doing businesses:** Ethiopia lags behind on the ease of doing business indicators and other competitiveness indicators (such as logistics services), which retard not only the formation of new businesses but also limit expansion of existing ones. Thus reducing the cost of entry into the formal sector by improving business environment (e.g. credit access, starting a business, and other services), thus enabling the expansion of small and medium sized enterprises which help stimulate diversification and expansion of the economy.

**Enhance Public-Private Partnership (PPP):** Public-private partnership can be a source of finance for delivering development goals and targets. Anecdotal evidence indicates that PPP can provide tremendous opportunities to enhance investments in the key sectors that generate transformational impacts by reducing burden on government and offering alternative for affordable public services that could otherwise be provided by the government. But lack of a standardized PPP operating

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<sup>34</sup> See World Bank (2015).

procedure was reported as a major limitation in the implementation of PPPs. It is recommended to strengthening PPP through a supportive and national regulatory system and establishing a unit dedicated to PPP at national and possibly at regional levels to guide PPP in systematized and organized way. Government needs to complete its legal framework for public-private partnerships. Development partners can provide support on developing the legal framework and helping the responsible agencies develop the technical expertise to design and negotiate PPPs. They could support the development of a central PPP unit, able to provide technical support across government. In addition, government and stakeholders need to invest in building capacity of the private sector and government sector offices on PPP with particular attention to the design, management, monitoring, evaluation and review of contractual agreements and other types of public-private modalities.

- b. **Attracting domestic and international private business and finance:** International remittances and foreign direct investment have become important sources of development financing in Ethiopia. Remittances inflow can be enhanced by encouraging other institutions, such as post offices, cooperatives, microfinance institutions, or possibly telecom operators to play a larger role in money transfer and opening up bank branches or money transfer agents in areas where there is large concentration of Ethiopian Diaspora, with certain incentives to reduce transfer fees. Likewise, there is also a need to improve business obstacles to attract quality FDI including expansion of special economic zones or specialized industrial parks, streamlined and speedy service procedures, provide fiscal incentive packages, provide more efficient trade logistics and transport services, supply of land mainly through industrial parks approach, trade and customs facilitations, and priority supply of credit and foreign exchange. In particular, fiscal incentives (such as tax exemptions and holidays) need to be attached to performance and monitored and evaluated on regular basis to ease fiscal burden on the government.
- c. **Maximizing ODA through enhanced cooperation:** International finance including official development assistance plays an important role in complementing additional resources from the public and private sectors. However, grants and loans tend to be volatile and pro-cyclical, as reflected by gaps between pledges and actual disbursements. Grant revenue has also been shrinking due to budget constraints in donor countries, indicating a need for tapping into new finance sources and instruments (e.g. blended finance) to complement domestic sources of financing. Development partners need to honor their Official Development Assistance (ODA) commitments in a timely and adequate manner, scale up their support in terms of capital, technology and capacity building. There is a need to improve allocation and disbursement of ODA through better management by MoFEC and line ministries. Manage the reduction in the time it takes to implement ODA projects through strengthening the monitoring and evaluation capacity of MoFEC, NPC and line ministries. There is also a need to improve effective utilization of external resources through improving project planning, and management capacity to execute projects on time and with the required quality. Strong domestic capacity needs to be built across sectors in project planning, management, monitoring, and contract administration.
- d. **Enhance South-South Cooperation (SSC):** There is a need to strengthen South-South Cooperation through bilateral, trilateral and interregional initiatives to support the country's development programmes. Currently, the scope and depth SSC is limited as a large share of SSC is originating from few countries and there is huge potential to leverage SSC. Efforts are also required to change composition of the financial linkages with SSC through designing projects with smart financing modalities (e.g. blended finance). There is also a need to diversify the

quality of SSC by improving the current cooperation modality, facilitating regional integration and capturing more countries through bilateral negotiations. Developing a comprehensive database for SSC is required to effectively monitor and disseminate information to stakeholders.

- e. **Climate change finance:** The resource requirement for realization of addressing the climate change risks and the 2025 vision significantly exceeds the current capacity, which require additional resources to meet the envisaged targets. This requires tapping climate finance through bankable projects which in turn requires building strong local capacity in project preparation and negotiation. Specific interventions include support in the establishment project preparation fund within MoFEC, enhance coordination and harmonization of climate-related programmes from a variety of sources (public, private, community and non-governmental organization) to maximize synergies. Support is also required to comprehensively assess CRGE finance and investment needs, establish economy-wide baseline climate change relevant CRGE finance, and identify financing options. In addition, there is a need to develop a climate fiscal framework to track climate related financial flows and uses. Equally important is establishing a comprehensive database within MoFEC for tracking climate finance flows to Ethiopia and its uses.

### 7.2.2 Cross-cutting issues

**Strengthening capacity building:** Capacity challenges at different levels remain a bottleneck for effective implementation of development programmes in the country. Capacity development needs to focus on institutional building and human development across all levels, especially in public institutions. This requires minimizing bad governance through capacity building with focus on land administration, tax administration, government finance and procurement, trade licensing and registration as well as improving the justice system. At institutional level, there is a need to establish a well thought, forward looking and shared systems to accommodate current and future developments. This requires strengthening a robust monitoring and evaluation (M&E) system at all levels (e.g. establishing a function M&E unit and developing monitoring and evaluation policy and guidelines). While there is an M&E framework for physical activities in GTP-II, there is no M&E for tracking financial targets under GTP-II, indicating the need for developing financial M&E and ensure its alignment with national development plan.

There is also a need to beef up the enforcement capacity through appropriate infrastructure (e.g. enhance ERCA's enforcement capacity to better detect international trade misinvoicing), and develop a comprehensive management information system including strengthening the statistical system. Strong institutions and systems need to be supported by a comprehensive human development programme through on-job training, short-term and long-term training. This requires interfacing public institutions with higher education, TVETs and research institutes.

**Enhance coordination mechanism:** There is a need to strengthen inter-sector policy coordination through providing policy and legislative guidance for effective implementation, monitoring, evaluation and reporting. In particular, a strong coordination architecture is crucial to harmonize different development programmes, reduce duplication of efforts and enhance synergies across programmes. The current a three level dialogue Architecture between the government of Ethiopia and development partners can serve an entry point for enhancing coordination among development partners, sectors and the government. In this regard, strong monitoring and evaluation system shall be in place at all levels to enhance coordination and alignment of programmes, improve accountability, and to inform policy, planning, and



programme development as well as budgeting decisions. In addition, efforts should be made to strengthen statistical capacity and improve the quality and timeliness of statistical data.

**Improve inclusiveness and social services:** Improvements in public service delivery system, including employment, education and health care, and ensure equal access to basic public services continue to be the primary focus of the country. In particular, promoting SMEs is crucial to ensure inclusiveness, especially as a means of employment creation for the growing labour force. The potential for SMEs for creating more jobs will be severely compromised SMEs due to multiple problems related to inadequate access to credit, market, technology, etc. The existing commercial banks don't have a special window for SMEs services nor are there specialized financial institution to cater the needs of SMEs. This calls for promoting new businesses and encourage job creation through expansions and growth of small and medium enterprises (SMEs) through improving access to warehouses, relaxing credit constraints, and improving the macroeconomic and regulatory environment. Key interventions include provide inclusive assistance for new businesses by strengthening the capacity of the existing institutions in charge of SMEs (e.g. FeMSEDA and SMEs bureaus ), encourage the existing commercial banks and Development Bank of Ethiopia to have a dedicated window for SMEs and establish a separate finance institution for SMEs (e.g. SMEs bank). In addition, enhance social protection and security through expanding the coverage of social security, strengthening quality basic healthcare services. These interventions require substantial resources to implement, enhanced coordination and alignment of programmes from different stakeholders to achieve the desired targets.

## 7.3 Matrix of interventions and monitoring and reporting

### 7.3.1 Matrix of interventions

Ethiopia, although growing faster than many of its Sub-Saharan African peers, has not managed to substantially raise the fiscal revenue share of GDP. Supportive macroeconomic and structural economic reforms can endogenously drive revenue mobilization through the revenue-generating institutions that Ethiopia has already put in place. Optimizing the efficiency of these institutions will allow the country to make the most of the new opportunities for revenue mobilization. With its newfound international credit rating, Ethiopia could also conceivably fill part of its financing needs by tapping into the demand for higher-yielding bonds from investors in advanced and emerging countries. In addition, forging partnership with non-traditional development partners will help mobilize finance for large-scale development projects which are crucial for achieving development targets. The private sector also offers a significant scope for increased public-private partnerships to finance developments. Together, these present opportunities for mobilizing resources, but there are also challenges such as inadequate internal knowledge base in accessing international finance and how new funding modalities work, absence of organized legal framework, especially for PPP, and changing nature of international financing priorities.

For Ethiopia to advance to the next level of development, there is a need to resolve the basic revenue mobilization constraints through a set of forward looking interventions which could boost the revenue generating capacity of the economy. After a thorough review of national, regional and global perspectives and situations on resource mobilization, a package of interventions have been identified to support the country's resource mobilization efforts which are envisaged to be implemented during the GTP-II period. The implementation of these interventions involves the participation of different stakeholders, which the government needs to play a leading role in terms of coordination and creating an enabling environment.

The proposed matrix of interventions includes key pillars, outcomes, outputs, indicators and time frame (Table 7). In addition, it also identifies relevant responsible stakeholders for implementation, monitoring and reporting. Note that some of the priority interventions are aligned with those indicated in the second Growth and Transformation Plan (GTP-II) of the country. But there is no a one to one correspondence between the result matrix of GTP-II and the AAAA matrix of interventions as the latter provides detailed information and milestones on resource mobilization mechanisms. If one wishes to track the progress of the roadmap both quantitatively and qualitatively over time, indicators need to be populated with baseline information and there is also a need to set targets across the years.

Getting baseline information including setting targets for the identified indicators is difficult to gather. Further assessment is required to generate baseline information and set targets for the various indicators.

### 7.3.2 Monitoring and reporting

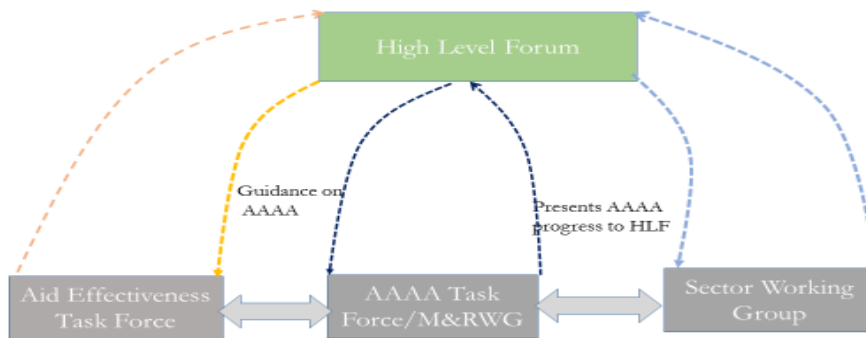
The Government of Ethiopia and Development Assistance Group (DAG) have established dialogue architecture to facilitate dialogue and deepen partnership. The joint government-donor coordination structure consists of the High Level Forum (focuses on policy, strategic and cross-cutting issues), the Development Effectiveness Taskforce (targets aid effectiveness), and Sector

Working Group (deals with sectoral strategic and implementation issues). However, the participation of private foundations in the government-donor coordination structure is so far limited. It will be useful to introduce a similar arrangement for private foundations to enhance coordination and ensure alignment of programmes.

The monitoring and reporting (M&R) of implementing the AAAA roadmap shall follow the standard requirements and procedures to ensure accountability, transparency and monitoring of progress and achievements. Note that monitoring and reporting of the AAAA roadmap is the responsibility of all partners involved in its implementation. To this end, there is a need to establish the AAAA Task Force as part of the dialogue architecture between the government of Ethiopia and development partners. The AAAA task force needs to establish a Monitoring and Reporting (M&R) Working Group (M&RWG) to provide advisory and capacity development support for effective implementation of the roadmap. The M&RWG shall comprise of specialists with relevant skills in resource mobilization. The M&RWG reports to the High Level Forum on the progress and status of the implementation of the Addis Agenda.

Progress will be measured through the annual joint monitoring report. In accordance with the existing practices, activities such as the joint annual review/progress report and evaluation will be undertaken in the course of the joint roadmap implementation period. The annual reviews and reports shall provide information on results achieved, challenges and lessons learned.

**Figure 35: Incorporating the AAAA task force into the Government-development partner’s dialogue architecture**



Source: Own construction

Table 5: Matrix of intervention

Matrix of interventions									
No	Key results and interventions by pillar	Indicators	Implementation period				Responsible institutions		
			2017	2018	2019	2020			
			1	<b>Outcome 1:</b> Domestic resource mobilization system strengthened at all levels (federal, regional and Woreda) and supported the national development efforts	Number of relevant policies revised, strengthened/developed and enforced				
Revenue administration systems revised									
Resources mobilization strategy developed and approved									
A functioning capital market system observed									
Proportion of domestic budget funded by domestic taxes									
	<b>Output 1.1:</b> Domestic savings increased	Share of domestic saving in GDP	24.6						
		Share of private saving in GDP	16.2						
		Share of government saving in GDP	8.4						
		Share of tax revenue in GDP	15.2						
		Share of non-tax revenue in GDP	1.9						
		Number of new saving schemes adopted							
1.1	<b>Key interventions:</b>								
1.1.1	Enhance private sector through financial inclusion such as improved access to financial services, and financial literacy						MoFEC, National Bank of Ethiopia (NBE), Development Bank of Ethiopia (DBE), Commercial Banks, Microfinance institutions, and insurance companies		
1.1.2	Enhance government savings through effective administration of tax policies, efficient and utilization of budget, and reducing wastage and improving transparency on expenditure						MoFEC, ERCA, NPC		
	Broadening the tax base through identifying and introducing new taxes						MoFEC, ERCA		
1.1.3	Strengthen and expand saving instruments including contractual savings and services such as saving for housing, investment equipment scheme, social security, and health insurance						MoFEC, ERCA		
1.2	<b>Output 1.2:</b> Domestic revenue mobilization capacity (both from	Reduced tax compliance cost							

	tax and non-tax sources) enhanced and enabling environment for doing businesses improved	Number of businesses registered for taxes						
		Number of ERCA staff members with relevant skills and knowledge on domestic revenue mobilization						
		Number of new tax bases and taxes identified and introduced						
		Number of revenue offices with a comprehensive modern database system						
		Number of new industrial parks constructed and strengthened						
		Number of factories established in the industrial parks						
		License and customs procedures streamlined						
		Ease of Doing business rank improved						
		Availability of approved tax potential assessments and tax policies						
	<b>Key interventions:</b>							
1.2.1	Undertake assessment of tax potential and identify feasible tax bases for the country						MoFEC, ERCA	
1.2.2	Design a nationally appropriate resource mobilization strategy to guide strategic interventions						MoFEC, ERCA	
1.2.3	Improve human resource development and management of revenue offices by supporting establishment of tax and customs institute						MoFEC, ERCA, Development Partners (DPs)	
1.2.4	Strengthen and expand modern information system and improve data quality						ERCA, Development Partners (DPs)	
1.2.5	Improve customer relations, services and awareness creation among tax payers						ERCA, Development Partners (DPs)	
1.2.6	Strengthen and support the tax and customs policy and research directorates (e.g. MoFEC and ERCA)						MoFEC, ERCA, DPs	
1.2.7	Equip tax collection institutions with adequate enforcement power (with adequate information and strong tax-auditing systems) to detect trade misinvoicing						MoFEC, ERCA, DPs	

1.2.8	Develop comprehensive programmes to improve voluntary tax compliance through tax education, revisiting existing tax systems and administration, and promote use of electronic payment system						ERCA, DPs	
1.2.9	Strengthening and upgrading the Standard Integrated Government Tax Administration System (SIGTAS) for self-help services such as online registration, e-filing, e-payment and reports to considerably reduce the time costs and the overall tax compliance costs for businesses						ERCA, DPs	
1.2.10	Introduce a simplified presumptive tax for small, informal businesses, in part to drive activity into formal enterprises						MoFEC, ERCA, DPs	
1.2.11	Improve coordination through establishing a robust communication for better tax coverage through investment in networking/interfaces relevant institutions						ERCA, DPs	
1.2.12	Establish and support integrated industrial development parks						Industrial Development Corporation( IDC), DPs	
1.2.13	Assess the benefits and costs of preferential tax treatments including tax incentives						MoFEC, ERCA, EIC	
1.3	<b>Output 1.3: Capital markets introduced to leverage development finance needed to implement sustainable development interventions</b>	Policy and legal frameworks formulated & implemented for capital market development						
		Capital market established						
		Human capacities created & technological facilities put in place to run the capital market						
	<b>Key interventions</b>							
1.3.1	Formulate relevant policy and legal frameworks to establish and run capital markets in Ethiopia						NBE, MoFEC, DPs	
1.3.2	Establish a capital market to raise finance domestically						NBE, MoFEC, DPs	
1.3.3	Popularize the uses of capital market among the public, create the required capacities in terms of human and technological facilities to effectively run and sustain it						NBE, MoFEC	
1.4	<b>Output 1.4: Public-Private Partnership (PPP) policy and legal frameworks developed or finalized and established</b>	PPP Policy document and legal frameworks finalized and approved						
		Number of PPP units established at different levels (federal and regional)						

		Appropriate platforms created to build capacities & consensus between the public & private sector						
	<b>Key interventions</b>							
1.4.1	Finalize the ongoing PPP policy and develop appropriate legal frameworks for Ethiopia and popularize it at all levels						MoFEC, NBE, EIC and Chamber of Commerce and Sectoral Associations	
1.4.2	Establish dedicated unit to run PPP at national and regional levels						MoFEC, EIC, NBE, Chamber of Commerce, Sector ministries, DPs	
1.4.3	Build capacities of private sector and government sector offices on PPP with particular attention to the design, management, monitoring, evaluation and review of contractual agreements and other types of public-private modalities						MoFEC, EIC, NBE, Chamber of Commerce, Sector ministries, and DPs	
2	<b>Outcome 2: International private business and finance boosted</b>	FDIs increased both in terms of quantity, quality and diversification						
		Effective FDI and remittances policies and legal frameworks in place						
		Share of remittances in GDP						
		Share of FDI in GDP						
2.1	<b>Outputs 2.1: Remittances inflow enhanced to support development financing in Ethiopia</b>	Enabling policy & legal frameworks developed						
		Number of institutions licensed for money transfer						
		Number of money transfer agents that opened branches abroad						
		Number of banks that opened branches in selected countries with large concentration of diaspora						
	<b>Key interventions</b>							
2.1.1	Develop policies and legal frameworks to engage other institutions (post offices, cooperatives, microfinance institutions, or possibly telecom operators) and enhance competition						NBE, MoFEC, DPs	
2.1.2	Provide licenses for relevant institutions to engage in remittance transfer						NBE, MoT	

2.1.3	Facilitate money transfer agents or banks to open branches in countries with large diaspora concentration						Money Transfer agents/banks, NBE, Ministry of Foreign Affairs (MoFA)	
2.2	<b>Outputs 2.2: Quality and diversified FDIs attracted to support development financing in Ethiopia</b>	Number of foreign investors licensed						
		FDI as a percentage of total FDI						
		Number of FDI using industrial parks						
		Number of FDIs using incentive packages						
		Type of FDIs by origin						
2.2.1	Avail organized information to foreign investors regarding investment opportunities and incentives						EIC, ERCA, MoFA	
2.2.3	Popularize investment opportunities through international media, meetings and conferences						EIC, ERCA, MoFA	
2.2.4	Target quality and high impact FDIs from non-traditional FDI source countries						EIC, MoFA	
2.2.5	Provide and strengthen a one-window service for FDI through strengthening the Ethiopian Investment Commission						EIC, DPs	
3	<b>Outcome 3: Grants and loans maximized through enhanced cooperation</b>	Increased utilization and delivery of grants and loans						
		Grants and loans disbursed as a share of commitments						
3.1	<b>Output 3.1: Official development assistance (ODA) from traditional sources enhanced</b>	Amount of ODA generated from traditional sources through blended finance (in Million USD)						
		ODA per capita from traditional sources (In USD)						
		ODA from traditional sources as a share of GDP (Percent)						
		Grants as a share of total ODA						
		Loans as a share of total ODA						
		Improved implementation capacity of public and private sectors (including contractors)						
	<b>Key interventions:</b>							
3.1.1	Enhance ODA inflow through blended finance						MoFEC	
3.1.2	Diversify ODA through targeting non-traditional development partners						MoFEC	



	Strengthen the implementation capacity of government, especially ODA-financed projects through regular monitoring and evaluation						MoFEC, DPs	
3.1.3	Support and facilitate timely disbursement of ODA						MoFEC, DPs	
<b>3.2</b>	<b>Outputs 3.2: South-South and triangular cooperation enhanced to mobilize new and additional finance sources</b>	Amount of ODA generated from South-South cooperation (in Million USD)						
		Number of new financial sources identified through South-South cooperation						
		Number of South-South cooperation agreements signed						
		Number of bilateral trade agreements signed through South-South cooperation						
	<b>Key interventions</b>							
3.2.1	Develop appropriate resources mobilization strategy to tap into new finance sources through South-South cooperation						MoFEC, DPs	
3.2.2	Explore financial sources such as bonds, climate finances, etc. through SSC						MoFEC, MEFCC	
3.2.3	Explore and identify new finances instruments (e.g. blended finance) from SSC						MoFEC, MEFCC	
3.2.4	Strengthen South-South cooperation through bilateral, trilateral and interregional trade initiatives						MoFEC, MoT	
<b>4</b>	<b>Outcome 4: Healthy external debt sustained</b>	Present Value (PV) of debt to export, GDP and revenue ratios						
		Debt service as a percentage of exports of goods and services						
		Improved project implementation rate						
		Improved capacity to repay debt						
<b>4.1</b>	<b>Output 4.1: Government capacity improved in external resources utilizations, project planning, delivery and management</b>	Number of people trained in project management, planning and management						
		Effective M&E tools developed and implemented						
		Clear contract management tools and procedures in place						
	<b>Key Interventions:</b>							

4.1.1	Build domestic capacities across sectors in project planning, management, monitoring, and contract administration						NPC, MoFEC, DPs, Universities	
4.1.2	Design tailored-made training programmes in project design, planning, management, and implementation						NPC, MoFEC, Universities, DPs	
4.1.3	Linking key government institutions with universities for strengthening capacity building in project design, planning, and management							
5	<b>Outcome 5: Synergies and coordination enhanced, good governance surfaced, social protection and inclusiveness ensured, and capacity strengthened to effectively respond to climate change and disasters</b>	Number of institutions with improved efficiency in service delivery						
		Country's rank in corruption index improved						
		Extent to which M&E outputs are used for decision making						
		Share of population covered with social security						
		Functional networking platforms in place						
5.1	<b>Output 5.1: Enhanced capacity in M&amp;E system, networking, and comprehensive management information system</b>	National M&E policy developed and ratified						
		Number of government institutions having a functional M&E units						
		Management information system (MIS) for online data sharing and networking established						
	<b>Key interventions:</b>							
5.1.1	Develop and strengthen a robust monitoring and evaluation (M&E) system at all levels through establishing a functional M&E unit and developing monitoring and evaluation policy and guidelines						MoFEC, NPC, Sector ministries, DPs	
5.1.2	Boost enforcement capacity through appropriate infrastructure and enhance networking and coordination with relevant institutions, and develop a comprehensive management information system						NPC, PMO, sector ministries, DPs	
5.1.3	Strengthen institutional capacity to improve and enforce transparency and accountability at all levels						NPC, PMO, sector ministries & DPs	
5.2	<b>Output 5.2: Inter-sectoral and development partners coordination mechanisms enhanced</b>	Cross-sectoral coordination platform established						
		Joint planning, implementation and review enhanced						
		Cross-sectoral information sharing improved						

		Data quality and timeliness improved						
	<b>Key Interventions:</b>							
5.2.1	Strengthen sectoral working groups and establish inter-sector coordination platform to provide guidance on effective planning, implementation, monitoring, evaluation and reporting							MoFEC, DPs
5.2.2	Strengthen statistical capacity building and improve the quality and timeliness of statistical data							MoFEC, NPC, CSA, Sector ministries, DPs
5.2.3	Expand sectoral working groups to include other relevant stakeholders such as foundations and CSOs (representatives)							MoFEC, DPs, Sector ministries
5.3	<b>Output 5.3: National climate related finance information improved and capacity to access climate finance enhanced</b>	CRGE-related investment needs identified						
		Climate finance tracking tools developed						
		Number of climate-related projects approved for funding						
		Climate focused project preparation fund established						
		CRGE-related economy-wide baseline data established						
	<b>Key Interventions:</b>							
5.3.1	Enhance coordination and harmonization of climate-related programmes to maximize synergies							MoFEC, MEFCC
5.3.2	Undertake comprehensive assessment of CRGE investment needs							MoFEC, MEFCC, DPs
5.3.3	Establish economy-wide baseline climate change relevant finance							MoFEC, MEFCC, DPs
	Establish project preparation fund to strengthen government capacity to access climate related finance							MoFEC, MEFCC, DPs
5.4	<b>Output 5.4: Capacity to ensure social security, inclusiveness and social services enhanced</b>	Number of people covered with social security						
		Number of small and medium sized enterprises created						
		The share of micro and small scale industry in total GDP (Percent)	1.4					
		Amount of loan provided to SMEs through banks (In ETB)						

		Number of jobs created through SMEs						
	<b>Key interventions:</b>							
5.4.1	Encourage job creation through expansion of small and medium enterprises						MoLSA, FeSMEDA, MoI, DPs	
5.4.2	Establish a SMEs bank to ease their financial constraints						FeSMEDA, MoUDH, NBE, DPs	
5.4.3	Establish standardized one stop service centres for SMEs						FeSMEDA, MoI, MoUDH, DPs	
5.4.4	Provide continuous extension services, training on basic entrepreneurial skill and outlook and training of trainers on business development services						FeSMEDA, MoI, MoUDH, DPs	
5.4.5	Enhance social protection and security through expanding the coverage of social security						MoLSA, MoH, DPs	

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### Annex

#### List of institutions consulted

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