Acknowledgements

This report is the final deliverable of a capstone project undertaken at the Elliott School of International Affairs' International Development Studies (IDS) Program at the George Washington University. A capstone project constitutes the final project/practicum for graduate students in the program and requires students to undertake consulting work with organizations within their field of study.

The Capstone team would like to acknowledge the many individuals and organizations that made this study possible.

• Megha Mukim, the capstone adviser at the World Bank’s Urban Development Unit for making this study possible. Without her mentorship and guidance, this project would not have been possible.

• Professor Sean Roberts, the capstone advisor at the Elliott School of International Affairs, for his outstanding guidance throughout the capstone process.

• Somik V. Lall, Nancy Lozano Garcia and the entire team for input and assistance in making the capstone trip possible.

• The World Bank office in Addis Ababa, Ethiopia, led by Guang Z. Chen, for hosting the capstone team, sharing their insight, and assisting in arranging our in-country research.

• The Elliott School of International Affairs and the World Bank, for providing financial support for this project.

• The over 50 interviewees from government organizations, the Addis Ababa Chamber of Commerce and all the individuals who generously offered their time to meet with us and share their stories.
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### Abbreviations

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<tbody>
<tr>
<td>AABOFED</td>
<td>Addis Ababa City Government Finance and Economic Development Bureau</td>
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<td>AACC</td>
<td>Addis Ababa Chamber of Commerce</td>
</tr>
<tr>
<td>ADLI</td>
<td>Agriculture Development-Led Industrialization</td>
</tr>
<tr>
<td>EC</td>
<td>Ethiopian Calendar</td>
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<tr>
<td>GTP</td>
<td>Growth Transformation Plan</td>
</tr>
<tr>
<td>DCED</td>
<td>Donor Committee on Enterprise Development</td>
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<tr>
<td>DLM</td>
<td>District Level Decentralization Program</td>
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<tr>
<td>EBDSN</td>
<td>Ethiopian Business Development Services Network</td>
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<tr>
<td>ETB</td>
<td>Ethiopian Birr</td>
</tr>
<tr>
<td>GoE</td>
<td>Government of Ethiopia</td>
</tr>
<tr>
<td>GERD</td>
<td>Grand Ethiopian Renaissance Dam</td>
</tr>
<tr>
<td>HICE</td>
<td>Household Income, Consumption and Expenditure survey</td>
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<tr>
<td>ICSC</td>
<td>International Council of Shopping Centers</td>
</tr>
<tr>
<td>IDPP</td>
<td>Integrated Development Plan Program</td>
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<tr>
<td>IDS</td>
<td>Industrial Development Strategy</td>
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<tr>
<td>IHCP</td>
<td>Integrated Housing Development Program</td>
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<tr>
<td>LIDI</td>
<td>Ethiopia Leather Industry Development Institute</td>
</tr>
<tr>
<td>MFI</td>
<td>Microfinance institution</td>
</tr>
<tr>
<td>MOFED</td>
<td>Ministry of Finance and Economic Development</td>
</tr>
<tr>
<td>MOTI</td>
<td>Ministry of Trade and Industry</td>
</tr>
<tr>
<td>MSE</td>
<td>Micro and Small Enterprises</td>
</tr>
<tr>
<td>ORAAMP</td>
<td>Office for the Revision of the Addis Ababa Master Plan</td>
</tr>
<tr>
<td>PASDEP</td>
<td>Plan for Accelerated and Sustained Development to End Poverty</td>
</tr>
<tr>
<td>RSDP</td>
<td>Road Sector Development Program</td>
</tr>
<tr>
<td>SDPRP</td>
<td>Sustainable Development and Poverty Reduction Program</td>
</tr>
<tr>
<td>SME</td>
<td>Small and Medium Enterprise</td>
</tr>
<tr>
<td>SOE</td>
<td>State Owned Enterprise</td>
</tr>
<tr>
<td>TIDI</td>
<td>Ethiopian Textile Industry Development Institute</td>
</tr>
<tr>
<td>TVET</td>
<td>Vocational Education and Training Center Agency</td>
</tr>
<tr>
<td>UNU</td>
<td>United Nations University</td>
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<tr>
<td>WB</td>
<td>World Bank</td>
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This study on the spatial determinants of growth in Addis Ababa has sought to examine the impact of city level policies on creating an urban environment more conducive to attracting and sustaining growth. The study also investigates the economic geography of Addis Ababa’s industrial sector, focusing mainly on the differences between formal and informal entrepreneurial activity. The findings from this study will contribute to broader studies by World Bank’s Urban Development Unit, including the Ethiopia Urbanization Review and a regional study of spatial development in African cities.

Key Findings

I. Excessive market intervention

II. Market distortion from an uneven incentive structure

The GoE’s support and incentives for businesses are skewed in favor of MSEs and large exporting firms in priority sectors. However, the unintended effect from excess subsidies to these two categories of firms has led to a distortion in the market whereby there are very few medium size firms.

Focus on MSE

MSE development is at the heart of the country’s Urban Development Strategy for reducing unemployment and poverty. One way the GoE is supporting MSEs is through the Micro and Small Enterprise Development Agency (MSEDA). With a special focus on youth and women, the MSEDA provides a wide range of support including business development training, equipment, loans, and working premises for new businesses in clustered areas. All formal MSE representatives interviewed in this study reported to have received some sort of government support when starting their business.

The focus on MSE has had a visible impact. Unemployment rates have steadily declined over the last five years from 32% in 2007 to 23% in 2012. Furthermore, according to the Addis Ababa City Government, over 83,000 MSEs and 74,457 new job opportunities were created between 2004/5-2008/9 (AABOFED 2009). However, the government’s heavy hand in influencing market entry with the establishment of so many micro and small enterprises in the market has created an uneven economic landscape in Addis Ababa. Unfortunately many MSEs find it difficult to expand to medium size status without further support from the government and as many are necessity entrepreneurs engaged in business activities due to lack of alternate employment opportunities. MSE firm owners stated that they were offered less assistance for further expansion once they were established as small enterprises and listed the following constraints: i) lack of financing ii) access to land/business premises iii) burdensome tax iv) market saturation v) competition from the informal sector.

Large Firms
Similar to MSEs, large firms also reported to have received government support both during market entry and expansion. For example, large firms in the leather industry reported that they were able to utilize the services of the Leather Industry Development Institute (LIDI), which included both short-term (1-6 months) and long-term (MSc or PhD) training and access to fully equipped research labs. Representatives from large firms also revealed a number of other incentives such as income tax exemption during startup phase, which were up to five years for certain manufacturing sub sectors. The government also provides premium land with affordable lease rates that range from 60-99 years for large exporting firms. For MSEs, lease terms are much less favorable and have to be renewed on an annual basis. However, even large firms face significant challenges that raise their cost of business and hinder further expansion. These constraints include: i) weak credit markets ii) access to land iii) poor infrastructure and iv) lack of skilled labor.

Overall, the GoE has succeeded in implementing key provisions of the Urban Development Policy, which focused on MSE growth, and the Industrial Development Strategy, which focused on large exporting firms. However as observed in the qualitative study, many of the MSEs interviewed have remained small for 5-10 years and face significant challenges from growing to medium size. This reveals the challenges that entrepreneurs have to survive without government support, which is reflected in the small number of medium size firms that exist in the industries analyzed.

III. Several Good Policies Lost in Implementation.

The GoE’s ambitious and generally well conceived policies are in many cases faced with a myriad of hurdles during the implementation phase, which have resulted in the accentuation of challenges and constraints facing firms in Ethiopia.

In mid-2000s, Ethiopia underwent a second wave of decentralization. In 2012, the city of Addis Ababa implemented a new administrative structure that consolidated 190 Kebeles into 116 Woredas. This process was particularly important for the business-enabling environment. In order to facilitate the process for local businesses, the devolution granted more powers to municipal offices. Despite their stated goals, the devolution process has constraints in two main areas:

(i) **Accountability**: a degree of top-down partisan control by the dominant party, and
(ii) **Capacity**: low administrative capacity at municipal levels.

The tax system in Ethiopia reflects the shortcomings of decentralization. In the past two years, the city of Addis Ababa in coordination with the Woreda offices has started to vigorously implement the new commercial tax code. While the new tax code is a positive move in business regulation it has lagged in successful implementation thus far. Some of the findings by the capstone team include contradictory calculation systems for tax collection that differs from one Woreda to another and discrepancies in the implementation of the law.

Another area, where the law gives ample support but the government falls short in implementation relates to women. The GoE intends to ensure that special attention is given to enable women to participate and compete equally with men in the political, economic and social fields both within

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1 The first wave of decentralization occurred in 1970s, when the country established the ethnic federalism system.
public and private organizations. This is of particular interest given women’s indispensable role in the MSE sector in the Ethiopian economy. Data indicates that despite the considerable decline in the overall unemployment rate, female unemployment is twice the size of male unemployment. Some of the systemic challenges for women entrepreneurs include i) overregulation ii) access to finance and iii) lack of subsidized day-care.

IV. Urban Planning: A Driving Force Behind Spatial Distribution and Expansion of Firms

Policy and program initiatives such as industrial zoning, cluster development, regional integration, and urban renewal are facilitating the spatial distribution and market entry of firms. In addition, urban infrastructure upgrading has received increased attention in Addis Ababa within the past decade. This is particularly important, given the positive linkage between urban infrastructure and productivity of urban economies and macroeconomic development (Mathewos Consult. 2006). Nonetheless, the implementation of these initiatives has also been marked with associated challenges and implementation difficulties, which are impacting the expansion of firms.

*Cluster Development*

This study also found the existence two main forms of industry clusters in Addis Ababa: natural and government clusters. Natural clusters such as Merkato and Shiro Meda consist of firms at various levels of an industry’s value chain in industries such as textiles and leather. Government clusters have also been created to address the problem of the lack of business and operating premises for small firms. The government’s effort to create clusters has delivered benefits such as increasing the supply of affordable business premises, but has also occasioned disruptions in business networks and increases in transportation costs. Additionally, problems related to the supply of services such electricity persists within many cluster facilities persist.

V. Informality- A Policy Dilemma

*Linkages Between Formal and Informal Sectors*

The study has identified both positive and negative linkages between formal and informal sectors. One of the positive linkages identified was related to the low-price goods provided by informal material suppliers for formal manufacturers. Another positive linkage is the convenience of sourcing from informal input suppliers. For example, many formal leather firms can procure abundant accessories from informal traders operating in the Merkato market.

In contrast, a negative linkage was also observed between the formal and informal sectors. In the leather and textile sectors, many micro and small-scale formal manufacturers lost their market share due to price competition from informal producers. However, in the leather sector, large firms benefited from economies of scale allowing them to sell their goods at much cheaper prices and with higher quality than those produced in the informal sector.

*Challenges to Formalizing*

The informal sector in Addis Ababa is an important segment for economic activity and the government needs to encourage this vulnerable segment to formalize by addressing their biggest challenges without overregulation. Confiscation of merchandise by the police has forced many informal business actors to formalize, but more constraints including lack of affordable land to operate and lack of finance. On one hand, although the government does provide business support
by subsidizing rent for formal micro enterprises, the demand far outweighs the supply. On the other hand, registering for a license and renting business premises adds significant start-up costs, while paying for taxes increases the operational cost.

Government Policy on Informality

The government faces a dilemma with the informal sector. Even though the informal sector is hard to regulate and operates outside of the tax system, jobs created within the informal sector promote the economy and increase the income of families.

In order to address the problem of informality, the federal government passed the Commercial Registration and Business Licensing Proclamation in January 2011, laying out severe penalties for those engaging in unlawful (including informal) economic activities. Being caught comes with large fines, confiscation of goods and even prison sentences. The government in the past has also demolished many settlements where informal businesses were active.

However, there is huge potential for exploiting the manufacturing capacity of the informal sector and the government is taking steps to engage with this sector. For example, the city government has established policies and agencies to facilitate the transition of informal firms through skills training, provision of business premises, and the provision of loans. There are also areas in the city where informal street vendors were relocated in sheds and forced into savings groups to accumulate adequate capital to formally register their businesses.
**Key Definitions**

**Informal Entity:** Defined as person(s) or firms who engage in commercial activities without having a valid business license or paying taxes associated with their business activities as required by law in Ethiopia. Informal actors can be both manufacturers and service providers (Proclamation No. 686/2010).

**Micro and Small Enterprises:** Firm size is measured by using two characteristics - number of employees and amount of capital. However, firm size categorizations and definitions are not uniform across different sources. The diagram below illustrates how the Addis Ababa Micro and Small Enterprise Development Agency (MSEDA), defines micro and small firms in manufacturing and service industries.

<table>
<thead>
<tr>
<th>Enterprise Level</th>
<th>Sector</th>
<th>Hired Labor</th>
<th>Capital</th>
</tr>
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<tbody>
<tr>
<td>Micro</td>
<td>Manufacturing</td>
<td>≤5 Employees</td>
<td>≤ETB 100,000</td>
</tr>
<tr>
<td></td>
<td>Service</td>
<td>≤5 Employees</td>
<td>≤ETB 50,000</td>
</tr>
<tr>
<td>Small</td>
<td>Manufacturing</td>
<td>6-30 Employees</td>
<td>≤ETB 1,500,000</td>
</tr>
<tr>
<td></td>
<td>Service</td>
<td>6-30 Employees</td>
<td>≤ETB 500,000</td>
</tr>
</tbody>
</table>

**Medium/Large Enterprises:** According to the Ethiopian Central Statistics Agency (CSA), large firms are those with 50 or more employees. Thus, firms that have between 31 and 50 employees were categorized as medium enterprises for the purpose of this study.

**Entrepreneurship:** The definition of entrepreneurship lacks common language, and in most cases excludes the informal economy (World Bank 2007). For the purpose of the analysis in this report, entrepreneurship is defined as the activity of an individual or a group in pursuit of perceived business opportunities in both formal and informal economies.

**Ethiopian Calendar (EC):** The Ethiopian calendar is based on the ancient Coptic Calendar and is always seven years and eight months behind the Gregorian (Western) calendar during September and December and eight years and four months behind during January and August.

**Gregorian Calendar (GC):** The Gregorian calendar is the internationally accepted civil calendar also known as the “Western” or “Christian” Calendar.
This document presents the findings of a study on the spatial determinants of growth in Addis Ababa, Ethiopia’s capital. This study is part of a broader World Bank assessment of the spatial development of cities in Africa, including Addis Ababa. The analytical work of the World Bank’s assessment of the spatial development of African cities seeks to develop a clear strategy for urbanization to drive economic growth and reduce poverty. The study on the spatial determinants of growth contributes to this effort. This report outlines an overview of the study’s objectives, research questions, a literature review, and methodology. The report also highlights preliminary findings from the desk research and interviews with key stakeholders during the fieldwork phase of the study.
1. Background & Context

Ethiopia is one of the fastest growing economies in both Africa and the world. During the last decade, the country had average growth rates of over 10% (WB Ethiopia Economic Update 2013). The GoE’s 2010 Growth and Transformation Plan (GTP 2009/10-2014/15), outlines a structural transformation agenda, which emphasizes the development of the industrial sector, with a focus on urban areas. Beginning in the late 1990s, Ethiopia adopted an Agriculture Led Industrialization (ADLI) growth model in its quest to achieve broad based economic development. Ethiopia has one of the lowest rates of urbanization and agglomeration. By 2000, for example, agglomeration in Ethiopia was 11.9%, much lower than other East African countries, which had rates of between 25% and 32% (Dorosch and Schmidt 2010). At the same time, the country has seen significant urban growth over the past three decades as the number of cities with 50,000 people has grown. However, Ethiopia’s rapid urbanization and population have outpaced the country’s ability to create jobs. In the meantime, Ethiopia’s private sector, which is concentrated within and around Addis Ababa, is largely informal (African Development Bank 2011). The sector largely consists of low productivity small-scale enterprises spatially concentrated around Addis Ababa. Further, the private sector firms face constraints such as a complicated land tenure system, a burdensome tax system, and limited access to finance (African Development Bank 2011).

Addis Ababa is an emerging global city with untapped potential for the private sector. According to a recent Global Cities Index, Addis Ababa is one of the cities in sub-Saharan Africa that is likely to achieve a developed city status over the next 10 to 20 years (A.T. Kearney 2014). Addis Ababa is endowed with Ethiopia’s key infrastructure assets and is a major center for rural-urban migration. With the growth of the city’s population, there has been a spatial expansion of urban land driven by city development projects. Concurrently, the city faces critical development challenges, which include high unemployment, low income, and urban poverty. Furthermore, surrounding Addis Ababa’s urban core are the city’s slums, which represent a critical challenge where 50-80% of the city’s houses are informal, lack building permits, and are generally poor quality habitations (United Nations Habitat 2008). Still, the city is the midst of tremendous change arising from the various institutional and policy reforms which both the federal and city government are implementing.
2. Research Objectives & Questions

The purpose of this qualitative study is to analyze and describe the economic geography of Addis Ababa’s industrial sector, focusing on the differences between informal and formal entrepreneurial activities. The overarching research question is “How have city-level policies implemented in Addis Ababa created a conducive urban environment for entrepreneurship and economic growth?” To answer this question, two hypotheses were developed. The first hypothesis is that city-level policies in Ethiopia have played a positive role in influencing firm market entry. The second hypothesis is that city-level policies have also played a positive role in firms’ ability to expand their business activities in Addis Ababa.

The analytical and descriptive work in this study seeks to accomplish the following:

(a) Identify concrete city-level policies that have helped to produce an urban environment more conducive to attracting and sustaining growth.

(b) Understand urban constraints to firm growth and dynamism.
To address the foregoing research question, a multi-stage, iterative research project was designed. The research design focused on the following distinct analyses:

- Examination of the spatial development of Addis Ababa – analysis and description of the development of the spatial form of the city, especially as it relates to economic activity, over time.
- Institutional and policy framework analysis – identification of city level development policies and tracking how they have changed over time. The analysis also included an assessment of their impacts on the spatial and economic organization of Addis Ababa.
- Constraints Analysis – identification and analysis of Addis Ababa’s urban constraints on firm dynamism and job growth. An assessment of how they constrain firm creation, growth and development was also undertaken.
- Sector analysis – an industry based analysis of formal and informal entrepreneurial activity in order to understand the determinants of its performance. This analysis included an examination of the agglomeration patterns and locational characteristics of firms and industries.

The two main sectors chosen for this study were: (1) Leather and Leather goods and (2) Food Processing. Both have been identified as priority sectors for development in the GTP. Upon the commencement of fieldwork in Addis Ababa, the (3) Textile industry was added as an additional sector for consideration in the study given the high prevalence of observed textile firms in the city. In addition, the study also included the (4) Construction sector, specifically focused on the Cobblestone Project and its contribution to job creation and entrepreneurship in Addis Ababa.

All of the focus sectors share two similarities. Firstly, they make major contributions to Ethiopia’s GDP. Secondly, the industries are all labor intensive.

### 3.1 Data Collection

Data collection for the project utilized desk research and field based interviews. The project team conducted a comprehensive literature review and country context analysis to better understand the institutional context and how it affects economic activity in Addis Ababa. Data and studies from a range of secondary sources were reviewed and analyzed throughout the project along the core issues of the study. Concurrently, fieldwork was conducted by three consultants who travelled to Addis Ababa in March 2014 for a period of two weeks. The fieldwork involved interviews with informal and formal firms in all four focus sectors. In addition, focus groups and semi-structured interviews were administered with over 50 individual representatives from government and private sector stakeholders. Below is a profile of interviewees from the four focus sectors. (Figure 1) Please see Annex 1 for a complete list of interviewed firm representatives and sites visited.
Figure 1: Stakeholder Profile (Firm Representatives Only)
4. Literature Review

4.1. Addis Ababa city profile

Addis Ababa was established as the nation’s capital in 1886 by Emperor Menelik. The city grew spontaneously around major political, religious, and business centers until the first city master plan was issued by the Italians in 1936 during their occupation of Ethiopia (ORAAMP 2007). The city administration established the Master Plan Revision Office (ORAAMP) in 1991 to undertake the task of developing a comprehensive urban development plan. The Government of Ethiopia (GoE) has adopted nine city master plans thus far which have all suffered from ineffective implementation. In the meantime, urban sprawling has continued to occur haphazardly along major transportation corridors. (See Figure 2)

Figure 2: Growth Trends in Addis Ababa (1935-2013)
According to the City Administration, Addis Ababa has grown by more than 80% in the last two decades. The city is also the largest urban center in the country and is made up of 10 sub-cities. Each sub-city is divided into “Woredas”, which are the smallest administrative units of the city. Addis Ababa is also considered as a primate city as it is estimated to be fourteen times bigger than the country’s second largest city, Dire Dawa. In 2013, Addis Ababa had a population of over 3.1 million and was home to 30% of the country’s urban population (City Government of Addis Ababa, 2013). Furthermore, an estimated 48% of city residents were migrants (Population and Housing Census 2007). Given current growth rates and rural-urban migration, the city is expected to double its population in the next 20 years. However, the urbanization rate in Ethiopia, which was estimated at 16% in 2009, is still comparatively lower than the 30% average for Sub-Saharan Africa (Schmidt and Kedir 2010).

Historically, urban housing policies and programs have also played a significant role in why the city has grown at a relatively slow pace, particularly from 1975 to 1991. For example, in 1975 the socialist political regime issued Proclamation No. 47 which nationalized all urban land, limited the number of residential units that a household could own, and temporarily halted new housing developments in cities. This eventually led to housing shortages, along with deteriorating housing conditions owing to overcrowding, and the spread of slums and informal settlements (UN-HABITAT, 2006). Ethiopia’s widespread urban housing problem was further exacerbated even after the country’s return to a market economy in the early 1990s. Between 1994-2007, Addis Ababa did not experience a large increase in urbanization when compared to other decades. During this period, the devaluation of the ETB and rising mortgage interest rates exerted an additional strain on the country’s urban poor. The new government also decided to claim urban land as government property and tighten control on land use.

4.2. Policy, institutional and regulatory environment

4.2.1. Urban Policy in Ethiopia and Addis Ababa

Urban Policy in Ethiopia and Addis Ababa

The Urban Development Policy in Ethiopia and the Plan for Accelerated and Sustainable Development to End Poverty (PASDEP) outline the roles for cities in promoting national development (Asfaw et. al 2011). Ethiopia’s urban development strategy utilizes an integrated approach, which incorporates goals such as the promotion of property ownership, job creation, improvement of the urban environment, and infrastructure development (Asfaw et al. 2011). The program has been implemented nationwide with large infrastructural investments especially in Addis Ababa. Additionally, urban development has gotten increasing momentum with the launch of the GTP (2009/10-2014/15). After 1991, the GoE decentralized urban governance. A constitution was created establishing nine regional states and two charter cities - the federal capital of Addis Ababa, and the special administrative region of Dire Dawa (Ministry of Works and Urban Development 2007). Each regional government has its own constitution and city proclamations, which establish the legal, institutional and organizational framework (Ministry of Works and Urban Development 2007). Before this, urban governance was centralized with local governments functioning as an extension of the central government. The city of Addis Ababa was established by the Addis Ababa City of Government Revised Charter Proclamation 361/2003.
Addis Ababa has been implementing a multifaceted urban development strategy, which seeks to achieve diverse goals such as infrastructure development, job creation, housing development, and small enterprise development.

**Laws, Strategies and Programs**

In 2005, Ethiopia’s council of ministers approved the Urban Development Policy which informs the development of the urban development and good governance package. The urban policy has the following interventions areas which form the basis of the urban development package: 1) Expansion of micro and small enterprise; 2) Housing development; 3) Land infrastructure provision; 4) Social services; and 5) Urban planning and environments (Ministry of Works and Urban Development 2005). Summarized below is the framework of urban development strategies and programs in Ethiopia:

**Figure 2: Framework of Urban Development Strategies**

Urban development strategy in Ethiopia reflects the federal government’s approach of integrating the urban development and the urban good governance packages of the national urban development policy. According to the Ministry of Works and Urban Development (2005), the urban development package specifies ‘what’ the government intends to do in terms of tangible urban services delivery such as housing, jobs, schools, and water supply. The urban good governance package, on the other hand, specifies the ‘how’ aspect of service delivery by focusing on such issues as effectiveness, efficiency, accountability, rule of law, democracy, and participation.

**The Micro and Small Enterprise Development Program**

An important element of the Ethiopia’s urban development strategy is the Micro and Small Enterprise (MSEs) Development Program. A notable feature of Ethiopia’s approach towards the development of MSEs is the integration of the program with investments in low cost housing through the Integrated Housing Development Program (Ministry of Works and Urban Development 2005).
Addis Ababa Spatial Determinants of Growth

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Development 2005). Other important elements of the program involve efforts by the government to provide serviced land for formal and informal businesses (Ministry of Works of and Urban Development 2005). The program was created with the goal of creating 1.5 million jobs (Ministry of Works and Urban Development 2005) with the following supporting targets:

Table 1: Micro and Small Enterprise Development Program Targets

| 1. Training of 2,500 MSE extension workers to staff the one-stop service centers |
| 2. Providing business development support training 360,000 MSE entrepreneurs |
| 3. Establishing One-Stop Service Center for micro and small entrepreneurs in 825 cities with the specific purpose of improving the regulatory environment |
| 4. Providing working premises for 820,000 MSE entrepreneurs mainly clustered in production premises |
| 5. Providing EB 5.2 billion (USD 576 million) in MSE loans for 1.2 million MSEs through microfinance institutions |
| 6. Promoting market opportunities and identify market linkages for 710,000 MSE entrepreneurs and |
| 7. Equipping 341,000 MSE entrepreneurs with modern and improved equipment and machinery |

Source: Ministry of Works and Urban Development. For specific project financing estimates refer to Annex 2.

In 2006/2007, Addis Ababa was targeted for participation in the first phase of the program. According to the Ministry of Works and Urban Development (2005), the program had the following financing objectives and goals:

- USD 576 million for start-up funding in support of micro finance institutions to provide credit for MSEs
- USD 13.3 billion for training MSE extension agents
- USD 102.9 million for the establishment of MSE production clusters (MSE incubators).

4.3. Entrepreneurship in Ethiopia

4.3.1. Firms in Ethiopia

Ethiopia’s MSE sector is characterized by a range of economic activities that generate job opportunities for a substantial segment of the population. The government is using the sector to curb unemployment and facilitate a suitable environment for new job seekers and for self-employment (EBSDN). The implementation of the MSE development strategy has been led by the Federal Micro & Small Enterprise Development Agency (FMSEDA), which until recently only operated at the national level. In 2004/2005, the GoE decentralized this process by establishing individual regional MSE coordinating bodies at city and sub-city levels.

A recent study by the World Bank reveals several trends related to firm dynamism in Ethiopia. While the entry size of firms in Addis Ababa has increased over the last decade, the ability of these firms to absorb shock is limited. For example, the exit rate for firms established in early 2000s is higher than that of firms established in 1990s. Furthermore the new generation of firms is primarily concentrated in risk-averse industries where competition is not a major challenge and marginal
profits to investment ratios are high. This is particularly evident in the cement industry, given the recent economic boom in the country. Startups in the cement industry have more than tripled (8% in 2000 to 30% in 2011) in the last decade, while investment in start-ups in traditional industries - food and beverages - has decreased by almost eight points (World Bank, 2012) (See Annex 3).

There is great variation in productivity among Ethiopian manufacturing firms, which is coupled with high firm turnover. For instance 60% of firms exit within the first three years of entry (Gebreyesus 2006). According to Tilman Altenbur (2010), this reflects two phenomena. First, there is a large group of “necessity entrepreneurs” who start own-account activities for lack of employment alternatives and without any clear business idea. It is among these necessity entrepreneurs, that productivity tends to fall far below the level of well-established medium-sized firms. Furthermore, failure rates are high, and it is not uncommon for owners to shift to other activities. Second, some firms are particularly more constrained in their access to credit, land, and product markets than others.

4.3.2. Informality
The literature on informal sectors finds evidence of roughly four primary degrees of enterprise informality (For a full typology of the degree of enterprise of informality refer to Annex 4). At one end of the spectrum are informal traders involved in subsistence activities. On the other end are large, well-established firms that are, to some extent, involved in the informal economy. Between these two are the so-called “unofficial enterprises” (DCED 2009). Djankov (2002) argues that the lack of skills and education among the members of the subsistence economy hinders their ability to “graduate” into more productive enterprises (Djankov, et al., 2002). The focus of this study was on subsistence and “unofficial enterprises.”

A 2002 study by the Association of Ethiopian Microfinance Institutions estimated the informal sector in Addis Ababa to be 51 percent of the productive economy (UN-Habitat 2006). While the informal economy in Ethiopia is considerably large - for every ten registered firms there are almost four non-registered firms (Enterprise Survey, 2014) – this number is significantly lower compared to Ethiopia’s regional counterparts. For instance, the average for Sub-Saharan Africa is 7.5). Ethiopian entrepreneurs also indicated one of the lowest rates of firms identifying competitors in the informal sector as a major constraint (only 11%). This number is over three times higher in Sub-Saharan Africa (37%).

A survey conducted by the Central Statistical Authority (CSA), in 1997, showed that there were 584,913 informal sector activity operators and 2,731 small-scale manufacturing industries, employing a total of 739,898 people. (EBDSN, 2014) The survey indicated that activity is concentrated in the manufacturing (47%) and trade and services (42%) sectors. According to the 1997 data by the CSA, the size of labor force engaged in informal sector activities and small-scale manufacturing industries was eight times larger than that of the medium- and large-scale manufacturing industries (EBDSN). Recent estimates of the informal sector in Ethiopia place the sector at 69% in Addis Ababa, compared to the national average, which lies below 15% (Fransen, Jan & Van Dijk, M. Pieter).

4.3.3. Demographics of the Ethiopian Entrepreneur
The Global Entrepreneurship Monitor classifies entrepreneurs into two categories: opportunity entrepreneurs and necessity entrepreneurs (Sriram and Mersha 2010). In contrast to their necessity
According to a recent study by the World Bank, there is an increase in the number of opportunity entrepreneurs. This can be explained by two factors: growing number of new graduates and increased number of female entrepreneurs entering the workforce. According to Enterprise Survey (2011), Ethiopia has one of the highest rates of skilled workers in Sub-Saharan Africa. Data from the Urban Bi-Annual Employment and Unemployment Surveys indicate that between 2003 and 2012, the percentage of persons with higher degrees choosing to become entrepreneurs has more than doubled - this number has increased from 7% to 17%. According to recent data there is increasing number of women joining the labor market as entrepreneurs; this number has doubled between 2003 and 2012 from 6% to 12% (World Bank 2012).

Despite these positive indicators, various challenges still exist in the Ethiopian labor market. Ethiopia has the highest number of temporary and unskilled workers in the world. As such, the informal sector assumes the role of absorbing this excess supply of labor.

4.3.4. Role of Gender

The SME sector in Ethiopia provides livelihoods for 49 percent of employed women (Abegaz, 2004). Women entrepreneurs in Ethiopia initiate businesses at a faster rate than men. Between 1991 and 2003, 50 percent of all new jobs were created by small businesses and 49% of those businesses were owned by women (Bekele & Jacobs 2008). Despite their key role played in entrepreneurship, women are not provided with adequate policy assistance (Welfare Monitoring Unit).

Even though the constitution calls for affirmative action to allow women to participate equally with men in political, economic, and social fields (Ethiopian Constitution, Chapter 3), in the past four decades, the government has failed to adequately address the plight of women entrepreneurs (Bekele & Jacobs 2008). Literature indicates that this problem stands in the overregulation of the SME sector by the Ethiopian authorities (Bekele and Jacobs (2008) provide a longitudinal analysis of entrepreneurs in Ethiopia between 1996-2001. According to the study, 78% of all failed businesses (that were included in the study) were owned or operated by women - this number is indicative of the level of support, or the absence thereof, to female entrepreneurs. The main concern expressed by women entrepreneurs in the study was lack of adequate financing (69%). Furthermore, female entrepreneurs displayed higher levels of poor managerial skills (72%), shortage of technical skills (74%) and lower levels of education (55%) when compared to their male counterparts.

4.4. Industry Analysis

This study analyzed entrepreneurship in the following sectors: (1) leather and leather products industry, (2) food processing industry, and the (3) textile industry, and (4) construction.

4.4.1. Leather and Leather Product Industry

Ethiopia’s GTP (2009/10-2014/15) has earmarked the leather industry as a priority sector. The sector was also recognized as an essential element in the Agricultural Growth Program.

Export data from 2011 reveals that the Ethiopian leather sector ranks 4th in Africa. Ethiopia’s leather sector is relatively competitive by the virtue of its abundant livestock. The country has the tenth largest livestock inventory in the world with 52 million cattle, including 10.5 million dairy cattle, and 47 million goats (USAID 2013).
In 2013, the sector created 10,000 formal sector jobs. There are 25 commercial tanneries, 17 footwear factories, 8 leather goods factories and around 100 small and medium scale enterprises within the sector (USAID 2013). A large number of MSEs, which are mainly informal footwear and leather goods manufacturers, tend to cluster in the Merkato area in Addis Ababa. These firms have an overall estimated manufacturing capacity that equals that of the formal sector (UNIDO 2012).

The leather value chain activities include animal husbandry, livestock trading, slaughtering, and hides and skin trading. Production activities include tanning, leather processing, shoe production and garment manufacturing. National retailers can sell finished and semi-finished leather goods in local markets, while exporters are limited to finished products. The GoE’s Proclamation No. 567/2008 imposes a 150% tax on semi-finished leather product exports, in order to promote local value-addition and capacity improvement. Additional government measures include the establishment of the Ethiopian Leather Industry Development Institute (LIDI) and the development of industrial zones. For instance, the Modjo industrial zone brings together tanneries and manufacturers of leather products to improve the efficiency of the value chain by decreasing associated transaction costs.

4.4.2. Food Processing Industry

Ethiopia’s food-processing industry is the country’s largest manufacturing subsector. The gross production value of industry’s large food-processing factories is about 15,792 million ETB ($790 million), while small-scale food manufacturers contribute approximately 308 million ETB ($16 million), excluding grain milling (CSA Ethiopia 2012)( Soethoudt et al. 2013).

The food-processing sector includes subsectors such as cereals, oilseeds and pulses, fruits, vegetable and potatoes, dairy products, livestock and meat. Coffee, vegetables and oilseeds are Ethiopia’s main processed food exports, accounting for 83% of the country’s processed food export value. Other products, in particular cereal, bread, and injera are mostly consumed domestically (Soethoudt et al. 2013).

There are about 560 large and medium size food-processing manufacturers in Ethiopia, providing over 60,000 jobs. These jobs account for 45% of all the jobs in the food-processing sector. Small-scale food processing, excluding grain millers, has 1,541 food processors, which employs about 4,748 people (Soethoudt et al 2013).

4.4.3. Textile Industry

The Ethiopian textile industry is one of the country’s oldest industries with a history of 70 years and a key part of the nation’s industrial strategy. Ethiopia boasts a long tradition of cultivating cotton, mainly through rain fed agricultural methods in the country’s lowlands, although, recently the country has begun to deploy modern and integrated irrigation techniques (Embassy of Ethiopia UK 2010).

Owing to both its linkages with other sectors of the and its potential to employ large numbers of people, the textile sector has strategic importance to Ethiopia. During the socialist era, Ethiopia had committed large areas of land to the sector and nationalized private sector firms leading to a growth in the sector. However, the sector began to decline in the face of policy neglect but has
begun to see an upswing in recent decades as government has once again begun to prioritize the sector. The sector employs about 9,746 employees (World Bank 2011). Small scale enterprises are important players in the sector employing about 91% of the labor force (World Bank 2011).

Key actors in the value chain include small farmers, garment manufacturers, ginneries, collectors, state farms, and private commercial farms. Enterprises in Ethiopia are classified as small, large, and medium based on a variety of variables such as turnover, production capacity or number of employees (World Bank 2011).

### 4.4.4 Construction

Construction, as an essential part of infrastructure, contributes to 6% of GDP in Ethiopia for 2006/07 (Central Statistical Authority 2008). Infrastructure has been under great growth following the GTP. The current GTP aimed to increase the roads network should from 49,000 km to 64,500 km by 2015 and construct 2,395 km of railway line (GTP 2010/11-2014/15).

Within the construction industry, the cobblestone construction sector in Ethiopia has been used as an approach to create additional employment opportunities and provide road lower cost construction material. The project has sought to strengthen the private sector, promote employment creation and skills development, as well as the promotion of local economies through the provision of construction contracts to MSEs. The project was originally run as a pilot in 2005 by the Mayor of Dire Dawa, Ethiopia’s second largest city, and was later adopted by Mayors across several Ethiopian cities. The project was launched in Addis Ababa, Ethiopia’s Capital, in 2007. By 2008, 150 pavers and 1150 stone producers (chiselers) had been trained. By 2009, 350 km² of roads and pedestrian walkways in 140 cities had been created at an estimated investment of 1.3 billion ETB. (GIZ, 2012) Currently, 2,000 people have graduated from the project, including 1,300 who have started their own businesses in brick making. Another 8,000 people are expected to graduate in 2014. The
5. Key Fieldwork Findings

5.1. Excessive market intervention

5.2. Market Distortion from an Uneven Incentive Structure
The study revealed that although the GoE gives substantial support and incentives to businesses, those are generally skewed to favor MSEs and large exporting firms in priority sectors. The priority industries, as stated in the country’s Industrial Development Strategy (IDS), include textile and garments, meat and leather products, agro-processing, and the construction industry. However, the unintended effect from excess subsidies to these two categories of firms has led to a distortion in the market whereby there are very few medium size firms.

5.2.1. Focus on MSEs
In 2005, the GoE released the first Urban Development Policy package that consisted of five intervention areas. The first of these was the Micro/Small-Enterprise Development as a driver for reducing unemployment and poverty. One way the GoE is supporting MSEs is through the Micro and Small Enterprise Development Agency (MSEDA). With a special focus on youth and women, the MSEDA provides a wide range of support including business development training, equipment, loans and working premises for new businesses in clustered areas. Their activities are coordinated by 116 one-stop shops (one for each Woreda) in Addis distributed in 10 sub cities (5-6 in each).

Addis Ababa has experienced a steady decline in unemployment rates in the last five years, much of which can be attributed to the focus on entrepreneurship as an instrument for job creation in urban areas. In 2007, Addis Ababa had the highest urban unemployment rate in Ethiopia at 31%. However, unemployment rates have been steadily declining and were reported to be at 23% in 2012. According to the Addis Ababa City Government, over 83,000 MSEs and 74,457 new job opportunities were created between 2004/5- 2008/9. The majority of these jobs have been in the construction sector that accounted for 30% of new jobs during that time period. (AABOFED 2009).
However, the government’s heavy hand in influencing market entry with the establishment of so many micro and small enterprises in the market has created an uneven economic landscape in Addis Ababa. Many MSEs find it difficult to expand to medium size status without further support from the government as they mainly consist of necessity entrepreneurs engaged in business activities due to lack of alternate employment opportunities. Interviews with MSE firm owners revealed that these small firms are offered less assistance for further expansion once they are established stating the following constraints:

i) **Lack of financing** - private financial institutions and banks in Ethiopia generally require 30% collateral in fixed assets. Many business owners cannot meet the high collateral needs of banks which cannot include land (as all land is government owned).

ii) **Land** - Although the government does provide MSEs with shops or land for manufacturing purposes along with subsidized rent, many interviewees stated that they found it hard to get additional land from the government for expansion purposes. Focus groups with micro firms in the leather industry also revealed that two of the firm owners in manufacturing, were not able to get additional space for retail due to the short supply of land/government subsidized space as priority was given to first time entrepreneurs and the unemployed. Firms reported that without subsidized rent, they were unable to expand due to inflated rent prices from private landlords that are double or triple the price without the government subsidy.

iii) **Tax** - Small firms in category B are still experiencing the negative effects of a new tax system that requires a 15% VAT on all items sold. Many firms stated that they were unable to compete with smaller firms that were only required to pay a 2% TOT tax due to their firm size. For a full list of tax categorization see Annex 3.
iv) **Market saturation** - Increased competition as the market becomes saturated with similar firms is also driving down prices. One small textile retailer in Shero Meda (a natural cluster of traditional textile manufacturers and retailers) stated that 20 years ago, there were only 108 shops in the area and now there is an estimated 500 shops that directly compete with her business.

v) **Competition from informal sector** - A number of MSEs reported that their biggest competitors were those in the informal sector that do not pay taxes (VAT or TOT) and can therefore sell similar goods at lower prices.

### 5.2.2. Large Firms

Similar to MSEs that reported to have received training through the MSEDA, large firms in the leather industry reported that they were able to utilize the services of LIDI. The Institute was created to build local capacity in the country’s key industries (leather and textile) to improve the quality of products that would be main drivers for the country’s exports. Services include both short-term (1-6 months) and long-term (MSc or PhD) trainings and fully equipped research labs for public use.

Representatives from larger firms also revealed a number of other incentives such as income tax exemption during startup phase, which were up to five years for certain manufacturing sub sectors. Furthermore, any investor who exports or supplies to an exporter as production or service input, at least 60% of his products or services, is entitled to income tax exemption for two years (Regulation No. 270/2012). Additionally, the GoE allows for import of duty-free capital goods and construction materials necessary for the establishment of a new enterprise or expansion or upgrading of an existing enterprise. The government also provides premium land with affordable lease rates that range from 60-99 years for large exporting firms. For MSE’s, lease terms are much less favorable and have to be renewed on an annual basis.

However, even large firms face significant challenges that raise their cost of business and hinder further expansion. Below are some constraints highlighted by large firm owners during fieldwork interviews:

i) **Weak credit market** - large firms stated their difficulty in acquiring loans from private banks citing the high retention rates and the strict requirement of banks accepting only fixed assets. One owner of a large food processing firm, stated that his business has not been able to expand as private banks were not willing give out loans without high collateral exclusively in fixed assets.

ii) **Land** - large firms in the leather industry reported no difficulty when requesting land for expansion while large firms in the food processing sector experienced constraints. One owner of a large food processing company stated that he had been waiting for 10 years to be assigned land in neighboring region Oromia to expand.

iii) **Infrastructure** - All firms identified limited infrastructure (e.g. electricity and water) as a primary constraint for business growth. This was also true for firms located in industrial zones.

iv) **Lack of skilled labor** - Lack of skilled labor was another reason for slow growth for large firms. One, owner of a large leather factory, Dire Industries PLC, cited lack of skilled labor and high labor turnover as one his firms challenges. According to him, his company spends significant amount of money to train employees by sending them to training programs at LIDI, however, many leave to start their own businesses.
Overall, the GoE has succeeded in implementing key provisions of the Urban Development Policy, which focused on MSE growth, and the Industrial Development Strategy, which focused on large exporting firms. However, although government support has had a substantial impact on market entry and the sustainability of large exporting firms, it has also created a distortion in the market. Many entrepreneurs establish MSEs out of necessity to take advantage of the government support but are unable to expand without continued assistance. For example, the majority of MSEs interviewed have remained small for 5-10 years and face significant challenges from growing to medium size.

5.3. Several Good Policies Lost in Implementation

Great strides were made two years ago in facilitating service delivery for businesses in Addis Ababa when the city government underwent a major decentralization process. Although the GoE has developed ambitious and generally well-conceived policy programs, the implementation of these policies has been problematic. This has in many cases resulted in the accentuation of the challenges and constraints facing firms in Ethiopia.

5.3.1. Decentralization

Addis Ababa’s decentralization process is an example of a good policy lost in implementation. The city of Addis Ababa implemented a new administrative structure in 2012, consolidating 190 Kebeles into 116 Woredas (See Table 2). The devolution granted more powers to officers at the sub-city and Woreda levels to perform such functions as renewing licenses and collecting taxes.

This process was not unique to Addis Ababa - the federal government underwent a District Level Decentralization Program (DLM) that resulted in further devolution of authority, substantial fiscal transfers, and a furthering of electoral accountability to local populations. Despite these achievements, there are some notable constraints, especially in three areas (USAID, 2010):

(i) Authority: Authority is well established de jure for local governments, but is insufficient to ensure successful decentralization, as it can be undermined de facto through the party system.

(ii) Accountability: a degree of top-down partisan control by the dominant party.

(iii) Capacity: low capacity at sub-national levels for management, planning, administration, and service delivery are constrained by low levels of preparedness among many staff and officials.

Below is a list of constitutional powers of Woredas Councils in the Amhara region (USAID 2010):

- Approval of woreda’s social service, economic development and administrative plans and programs;
- Levying and collecting land use taxes, agricultural income revenues and other local taxes
- Utilizing the woreda source of revenues, excluding such other revenue allocated and administered by regions;
- Preparation and approval of the woreda budget;
- Construction and maintenance of lower grade rural roads;
• Directing basic agricultural development activities, administering and protecting the natural resources of the woreda

Table 8: Decentralization from Kebele to Woreda

<table>
<thead>
<tr>
<th>Sub-City</th>
<th>No. of Kebeles</th>
<th>No. of Woredas</th>
</tr>
</thead>
<tbody>
<tr>
<td>Addis Ketema</td>
<td>21</td>
<td>10</td>
</tr>
<tr>
<td>Akaki-Kaliti</td>
<td>19</td>
<td>11</td>
</tr>
<tr>
<td>Arada</td>
<td>16</td>
<td>10</td>
</tr>
<tr>
<td>Bole</td>
<td>22</td>
<td>14</td>
</tr>
<tr>
<td>Gulele</td>
<td>21</td>
<td>10</td>
</tr>
<tr>
<td>Kirkos</td>
<td>19</td>
<td>11</td>
</tr>
<tr>
<td>Kolfe</td>
<td>16</td>
<td>15</td>
</tr>
<tr>
<td>Lideta</td>
<td>17</td>
<td>10</td>
</tr>
<tr>
<td>Nifas Silk Lafto</td>
<td>18</td>
<td>12</td>
</tr>
<tr>
<td>Yeka</td>
<td>21</td>
<td>13</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>190</strong></td>
<td><strong>116</strong></td>
</tr>
</tbody>
</table>

Source: Current Administrative map for Addis Ababa (For more detailed information, please see Annex 7 & 8)

By delegating power to the Woreda level, the city administration aimed to facilitate the private sector and curb the burdensome bureaucratic process. The interviews and focus groups with over fifty businessmen, however, revealed low capacity in these local municipal offices. What is lacking, from the design of such a progressive policy is due attention given to the capacity at the lower levels of administration.

Given the high government employee turnover rates, many employees working at local offices, are not familiar with the local regulations. Furthermore, in some cases laws are implemented retroactively. Such hurdles do not only incur additional costs, account for loss of time and decrease in productivity, but are discouraging for entrepreneurship, in general. “Sometimes we have to ourselves explain the Woreda officials differences between specific laws,” said one of the interviewees.

5.3.2. Tax code

In the past two years, the city of Addis Ababa has started to vigorously implement the new commercial tax code. What was intended to be a positive move in business regulation (the new tax law was to simplify some of the hurdles that came with tax enforcement- i.e. firms in Category C did not have to save records), has in some cases negatively impacted the progress of struggling entrepreneurs. (For more information on tax code, see Annex 5).

During the fieldwork, the team visited a number of clusters within Addis Ababa. Some of the findings revealed not only contradictory calculation systems for tax collection from one Woreda to another, but also discrepancies in the implementation of the law. While the new tax law is a valuable tool for government revenue generation, it is not taking into account the unique characteristics of each firm. Furthermore, the standardized tax law does not take into account seasonal revenue fluctuations of the firms.
A small shop owner in Shero Meda is an owner of a micro retail shop in a natural textile cluster in Shiro Meda. Although she has been operating in the same location for five years, the authorities started implementing the TOT system only two years ago. Two years ago, she had to pay an arbitrary amount based upon estimated annual sales by Woreda administration (note that the change from Kebele to Woreda administrative system was only implemented two years ago). The same retailer said that she was very pleased with the TOT system - it is less burdensome, especially during the slow season.

Another salesman in the Shiro Meda cluster had a different story to share. According to the team’s interview with him, tax implementation differs in each Woreda. He stated that since he was registered as a store with 500,000 ETB annual sales, he had to pay 15% VAT, while his neighbor in Woreda Two in the same sub-city (Gulele) pays TOT. In the past six months, however, his store has had only 19,000 ETB in sales. Unfortunately he is unable to move to Woreda Two since there is no available space. And his story was not unique; there were other salesmen from the Merkato cluster that faced similar challenges.

5.3.3. Women and the Law

With respect to women, the legal framework provides ample sources for equal opportunity, but lacks in successful implementation. The GoE intends to ensure that special attention is given to enable women to participate and compete equally with men in the political, economic and social fields both within public and private organizations. Despite these bold statements by the government, women are not given due attention, when it comes to implementation of the same laws.

As already mentioned in Section 4 MSEs account for the majority of jobs created in Ethiopia and women play an indispensable role in this segment of the economy. Furthermore, as Table 9 indicates, unemployment rates are unevenly distributed between men and women. Despite the considerable decline in the overall unemployment rate, female unemployment is twice the size of male unemployment (See Table 9).

During the fieldwork, the research team had the opportunity to meet with representatives from the Addis Ababa Women Entrepreneurs’ Association. The association currently has members from formal and informal segments of the economy. Some of the services provided by the association include skills training, networking, and counseling. Achamyelesh Ashenafi who is the president of the Association, highlighted a number of systemic challenges that particularly impact women entrepreneurs in Ethiopia.

1) Overregulation of informal sector remains a critical challenge. Given the high rates of unemployment among women, women make up a considerable portion of the informal economy. The majority of the interviewed women were engaged in informal subsistence activities.
2) Far more debilitating is poor access to finance. While access to finance is a broader challenge that affects the entire spectrum of firms (large, medium and small), lack of financial capital is a greater challenge for women. Microfinance institutions (MFIs) have very strict conditions that small entrepreneurs are unable to satisfy. Most MFIs require 30% collateral and repayment in as little as three years - conditions that most subsistence entrepreneurs are unable to meet.
iii) **Gender specific challenges include child day-care and family responsibilities.**

According to Ms. Ashenafi, “women entrepreneurs are not allowed to fail—once they fail, it is harder to stand back on their feet.” Some of the legal challenges highlighted by World Bank’s Women Business and the Law, are lack of deductible payments for childcare, absence of mandated free and compulsory primary education.

<table>
<thead>
<tr>
<th>Year</th>
<th>Male (%)</th>
<th>Female (%)</th>
<th>Total (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998</td>
<td>21.2</td>
<td>43.7</td>
<td>32</td>
</tr>
<tr>
<td>1999</td>
<td>22.3</td>
<td>36.8</td>
<td>29.1</td>
</tr>
<tr>
<td>2000</td>
<td>22.8</td>
<td>40</td>
<td>31.4</td>
</tr>
<tr>
<td>2001</td>
<td>21.4</td>
<td>36.1</td>
<td>28.6</td>
</tr>
<tr>
<td>2002</td>
<td>18.4</td>
<td>38.3</td>
<td>27.9</td>
</tr>
<tr>
<td>2003</td>
<td>17.9</td>
<td>36.1</td>
<td>26.6</td>
</tr>
<tr>
<td>2004</td>
<td>17.3</td>
<td>33.7</td>
<td>25.1</td>
</tr>
<tr>
<td>2005</td>
<td>15.6</td>
<td>31.1</td>
<td>23</td>
</tr>
</tbody>
</table>

Source: Population, Gender and Development in Addis Ababa (2005 EC)

### 5.4 Cluster Development Efforts: Mixed Results

**Natural and Government Clusters**

This study found the existence two main forms of industry clusters in Addis Ababa: natural and government clusters. Natural clusters have emerged organically in particular locations within Addis Ababa in response to the availability of raw materials and input suppliers, markets for products, and the availability of abundant pools of labor. These clusters have developed around industries such as textiles, leather, handlooms, and metals in markets such as Merkato and Shiro Meda. The natural clusters typically consist of firms at the various levels of an industry’s value chain. Thus, the leather cluster in Merkato, for example, has firms producing leather products and accessories as well as engaging in the marketing and distribution of such products.

In addition to natural clusters, the study found the existence of government clusters created to support MSE development and promote priority industries. The government clusters have also been created to address the problem of the lack of business and operating premises for small firms in Addis Ababa. Furthermore, in an effort to facilitate linkages between, MSEs and medium and large enterprises, some government clusters were located within the proximity of industrial zones which host medium and large scale firms. In many cases, the government has created such clusters close to natural clusters in a bid to alleviate the shortage of expansion space within the natural clusters such as Merkato. In other cases, however, the government has established clusters with the explicit purpose of promoting particular industries such as textiles & leather. In these cases, firms have had to relocate to such clusters from different parts of the city.
Achievements and Ongoing Challenges

While the government’s attempt to create clusters has addressed some key challenges faced by businesses, it has also resulted in additional challenges. For instance, the government has been able to address the problem of providing business premises, which many small business owners cited as a major business constraint. Furthermore, the government clusters provided small businesses with premises at highly subsidized and affordable rents in some cases as low as 300 ETB per month. In other instances, the premises were provided for free, leading to individuals acquiring the premises and renting the space out to other businesses. New problems have emerged with the implementation of the government’s cluster development efforts. These include the increases in transportation costs, as firms have had to seek skilled workers outside the government clusters and transport them to these new locations. This study found some of the following key achievements and challenges associated with the government’s cluster program:

Achievements

Supply of Premises

Through the creation of the cluster development program, the government has begun to address the problem of the shortage of space for business operations. With the launch of the program, businesses have had the opportunity to acquire spacious premises at affordable rents. The premises have typically been used for production and operations activities. The table below shows the number of working premises constructed and transferred from 2004 to 2011 in Addis Ababa:

<table>
<thead>
<tr>
<th>Working Premise</th>
<th>Constructed</th>
<th>Transferred</th>
<th>Male</th>
<th>Female</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Textile and Garment</td>
<td>47</td>
<td>39</td>
<td>4208</td>
<td>2042</td>
<td>6250</td>
</tr>
<tr>
<td>Construction</td>
<td>566</td>
<td>517</td>
<td>4283</td>
<td>1344</td>
<td>5627</td>
</tr>
<tr>
<td>Wood and Metal Work</td>
<td>966</td>
<td>938</td>
<td>3307</td>
<td>824</td>
<td>4131</td>
</tr>
<tr>
<td>Urban Agriculture</td>
<td>127</td>
<td>127</td>
<td>1201</td>
<td>553</td>
<td>1754</td>
</tr>
<tr>
<td>Food Processing</td>
<td>508</td>
<td>454</td>
<td>734</td>
<td>5291</td>
<td>6025</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>2214</strong></td>
<td><strong>2075</strong></td>
<td><strong>13733</strong></td>
<td>10054</td>
<td><strong>23783</strong></td>
</tr>
</tbody>
</table>

Source: Addis Ababa Micro and Small Scale Enterprise Development Agency

Benefits of Collocation

As stated earlier, the government has established some clusters in the vicinity of natural clusters. This has created the benefit of placing businesses close to suppliers of raw materials and inputs.
Locating government clusters in the proximity of natural clusters has also provided firms with access to markets for their output.

Challenges

Infrastructure Quality

Although the government has made the effort to increase the stock of premises for small firms, several challenges still remain. A key challenge is the overall quality of the infrastructure and service provision. Although many of the cluster buildings were G+4 buildings, several of these facilities were created with basic building materials, with the facilities suffering from the lack of a consistent supply of electricity and water.

Similar to industrial zones, reliable electricity supply is a major challenge for small businesses as well. As already mentioned, in the previous section, the new tax code requires most businesses to calculate taxes through the VAT system. The VAT sales recording machine requires electricity to operate, but there are frequent electricity shortages within these clusters. One of the small salesmen interviewed at the Shiro Meda cluster described how lack of reliable electricity affects his business. Since he is required by law to record every single sale, it is illegal to sell an item if it is not recorded in the VAT. He may face felony charges if he does not comply with the regulation.

Impacts on Business Networks and Disruptions

Relocating firms also reported disruptions to their business operations and networks. Since firms had to relocate to new premises they reported losing key business and supply networks. Relatedly, some relocated cluster firms reported difficulties in selling their products to buyers in the large markets such as Merkato. This was because buyers in those clusters had established business relationships and networks with suppliers within the cluster. Infrastructure upgrading efforts have also added yet another dimension to this problem with the government’s plans to major roads through clusters such as Shiro Meda. These planned infrastructure development projects will likely create short term business disruptions for firms in these locations. However, in the long-term, it is likely that business activities will increase after the completion of such infrastructure projects as market access improves for the firms.

Low occupancy rates
In several cases, the study found that cluster facilities were not being utilized to the fullest. Many cluster facilities were vacant (namely facilities in Kaliti) with only a small number of businesses operating in them. Several reasons were cited for the low occupancy rates including lack of awareness of the existence of the clusters and the lack of selling premises, which made it difficult for firms to sell their products.

5.5. Informality - A Policy Dilemma

5.5.1 Linkages between formal and informal

The interviews with various government offices and the focus groups with large formal firms and small informal business owners revealed positive and negative linkages between the formal and informal sectors.

Focus group discussions revealed a positive linkage between formal manufacturers and informal material suppliers. Compared to other input suppliers, informal firms sell their products at lower prices since they do not pay taxes. Therefore, formal firms can decrease their production costs by acquiring raw material from the informal sector. However, since manufacturers can import raw materials duty-free, this is not a big driver for maintaining the linkage with local informal input suppliers.

In addition to the price advantage, convenience is another factor that builds positive linkage. During one focus group, a formal leather producer noted that he found it convenient to acquire input materials in the informal market within and around the Merkato area. In the interview with micro enterprises in Shiro Meda, some retailers also stated that they preferred to purchase goods from informal producers that tend to travel door to door selling their products. For micro firms, many also cited that their informal suppliers also gave them goods on credit once they had established trust.

In contrast, a negative linkage was also observed between the formal and informal sectors. In the leather and textile sectors, many micro and small-scale formal manufacturers lost their market share due to the price competition from informal producers. However, in the leather sector, large firms benefited from economies of scale allowing them to sell their goods at much cheaper prices and higher quality than those produced in the informal sector.

5.5.2. Challenges to Formalizing

The informal sector in Addis Ababa is an important segment for economic activity and the government needs to encourage this vulnerable segment to formalize by addressing their biggest challenges without over regulation. Many live in the fear as a result of recent policy that authorizes police to detain and confiscate merchandise from informal traders. Although tighter regulation may force a few informal businesses to join the formal sector, the majority may not comply simply due
to lack of resources. Many informal actors cited the lack of an affordable place to operate their businesses as a main reason for remaining in the shadow economy. Although the government does provide business support by subsidizing rent for formal micro enterprises, the demand far outweighs the supply. Many of interviewees in the informal sector claimed that they had been on the waiting list for several years.

From different interviews with informal business owners in several markets in Addis Ababa, it became clear that another key constraint facing informal business owners was lack of finance. Registering for a license and rent add significant costs to starting a business while paying for taxes also increases the operational cost. A lady who produces bread at home told researchers that she spends a sizeable part of her income on transportation and is barely able to cover basic costs of living.

5.5.3. Government Policy on Informality

The government faces a dilemma with the informal sector. Even though the informal sector is hard to regulate and operates outside of the tax system, jobs created within the informal sector actually promote the economy and increase the income of families. There is huge potential in manufacturing capacity of the informal sector, and the government seeks to utilize the manufacturing capacity of the informal firms through skills training, provision of business premises, and the provision of loans.

In order to address the problem of informality, the federal government passed the Commercial Registration and Business Licensing Proclamation in January 2011, laying out severe penalties for those engaging in unlawful (including informal) economic activities. Being caught comes with large fines, confiscation of goods and even prison sentences. The government in the past has also demolished many settlements where informal businesses were active.

The city government has also established policies and agencies to facilitate the informal sector become formally registered micro or small business. Coordinating with the Federal Micro and Small Enterprise Development Agency, the Micro and Small Business Development Bureau in Addis Ababa has helped unemployed and informal business people engage in government led cobblestone project as a means to accessing finance. There are also areas in the city where informal street vendors were relocated in sheds and guided to save enough capital before officially registered.
As Ethiopia undertakes its growth trajectory to become a middle income country, national and city level policies will need to address key challenges that still confront the private sector. In Addis Ababa the city government is taking notable strides towards creating a conducive urban environment for sustainable economic growth. This is particularly important given the city’s position as an emerging global city with a plethora of untapped private sector.

Improvements include addressing its infrastructure deficit by investing heavily in increasing electricity capacity and road construction and alleviating high urban unemployment by creating avenues for job creation and incentives for entrepreneurship. The government has given particular attention to the development of the MSE sector by establishing the Federal Micro and Small Enterprise Development Agency and its regional and city counterparts across the country.

Additionally, the government was also able to address administrative constraints facing private firms through its decentralization efforts. However, implementing the decentralization strategy has been a challenge. Institutional capacity is still lagging at the lower levels of government structure and undermining the efficiency gains from decentralization. Institutional strength is pivotal for the development of the country and the GoE needs to place special focus on capacity building. As highlighted in the analysis, the lack of human capital in government institutions is a critical challenge for entrepreneurs.

Overall, despite the notable gains however, many structural challenges remain. Key areas for policy reform include addressing land tenure rights, galvanizing private bank lending, and ensuring the business enabling environment not only supports market entry but also firm expansion.
8. Recommendations

Short Term (0-1 year)

Task: Build government capacity at lower levels of City Administration
Priority: High
Feasibility: Yes
Implementer: Government

Decentralization has been one of the key achievements of the Addis Ababa City Administration. Despite significant *de jure* achievements: the eventual devolution of authority, substantial fiscal transfers, and a furthering of electoral accountability to local populations, there is considerable gap in *de facto* powers of these offices. In particular, the lowest administrative levels of government, the Woredas, lack in the technical capacity and adequate skills to successfully implement the laws and regulations pertaining to local businesses.

The city administration of Addis Ababa should deliver mandatory skills training as well as ensure knowledge of laws and regulations by Woreda staff on a regular basis. This should particularly target underperforming Woredas to address the plague of lack of capacity in these Woredas. Furthermore, there needs to be performance improvements systems in place to increase similar capacity among all Woredas. To address the challenges for market entry for small firms, the government needs to improve efficiency of distribution and delivery of business premises.

Short Term (0-1 year)

Task: Establish a task force between education institutions and business reps to ensure training is meeting market needs
Priority: High
Feasibility: Yes
Implementer:

Medium Term (2-3 years)

Task: Improve performance of financial sector to expand the flow of credit to firms
Priority: High
Feasibility: Yes
Implementer: Micro- & small firms and missing middle

GoE has taken great strides in helping subsistence entrepreneurs with market entry. Through various programs spearheaded by the Federal Micro and Small Enterprise Agency and other agencies the GoE helps struggling entrepreneurs acquire much needed seed capital for their individual ventures (i.e. Cobblestone project provides with 80% of seed capital needed).
However, there are important institutional gaps in the overall financial sector. While there are 10 working commercial banks, three of them are state-owned, and the remaining 7 are under strict supervision of the National Bank of Ethiopia. The GoE should revise its financial sector laws, in particular those pertaining to retention rates and types of collateral. Furthermore, GoE should consider opening up the banking sector to greater competition, including foreign investment. Additional recommendations include strengthening credit information bureaus, and creation of collateral registries. Such systemic changes will eventually contribute to a more balanced business development strategy.

**Long Term (4-5 years)**

**Task:** Strengthen private sector institutions and their ability to influence policy  
**Priority:** high  
**Feasibility:** Yes  
**Implementer:** Private sector actors, donors

If Ethiopia wishes to achieve its goal of reaching middle-income country status by 2025 it is imperative that private sector development be a priority. Private sector institutions and sector associations need to be at the forefront of policy formulation to ensure that their voices are heard. Until now the GoE has had a significant role in influencing the market such as directing capital to priority sectors. However, private sector institutions need to be consulted to identify and lift existing constraints and ensure that investment is directed to the most productive industries without political interference.
7. References


Federal Democratic Republic of Ethiopia. Proclamation No. 455/1997 E.C

Federal Democratic Republic of Ethiopia. Regulation No. 135/1999 E.C.


Annex 1: Interviewee Profile by Sector

<table>
<thead>
<tr>
<th>Industry</th>
<th>Sub-Sector</th>
<th>Firm Size/Category</th>
<th>Firm Name</th>
<th>Years of Operation</th>
<th>Gender</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing &amp; Retail</td>
<td>Large (250 Employees)</td>
<td>Modem Zege</td>
<td>24</td>
<td>M</td>
<td></td>
</tr>
<tr>
<td>Manufacturing &amp; Retail</td>
<td>Large (430 Employees in tannery, 300 in Shoe Manufacturing)</td>
<td>Dire Industries PLC</td>
<td>42</td>
<td>M</td>
<td></td>
</tr>
<tr>
<td>Manufacturing</td>
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<td>-</td>
<td>55</td>
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<tr>
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<td>Medium</td>
<td>K &amp; T Trading PLC</td>
<td>30</td>
<td>M</td>
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<tr>
<td>Manufacturing</td>
<td>Small/Medium 5-20 (seasonal employees)</td>
<td>-</td>
<td>7</td>
<td>M</td>
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<tr>
<td>Leather</td>
<td>Retail</td>
<td>Micro</td>
<td>9</td>
<td>F</td>
<td></td>
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<tr>
<td>Manufacturing</td>
<td>Micro</td>
<td>-</td>
<td>10-Sep</td>
<td>F</td>
<td></td>
</tr>
<tr>
<td>Category</td>
<td>Type</td>
<td>Duration</td>
<td>Status</td>
<td>Details</td>
<td></td>
</tr>
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<td>------------------------</td>
<td>-----------------</td>
<td>----------</td>
<td>--------</td>
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<td></td>
</tr>
<tr>
<td>Manufacturing</td>
<td>Micro</td>
<td>-</td>
<td>6</td>
<td>Female</td>
<td></td>
</tr>
<tr>
<td>Retail</td>
<td>Micro</td>
<td>-</td>
<td>1 month</td>
<td>Female</td>
<td></td>
</tr>
<tr>
<td>Retail</td>
<td>Small</td>
<td>-</td>
<td>7</td>
<td>Female</td>
<td></td>
</tr>
<tr>
<td>Retail</td>
<td>Micro</td>
<td>-</td>
<td>6</td>
<td>Male</td>
<td></td>
</tr>
<tr>
<td>Retail</td>
<td>Micro</td>
<td>-</td>
<td>3</td>
<td>Male</td>
<td></td>
</tr>
<tr>
<td>Baker</td>
<td>Informal</td>
<td>-</td>
<td>4</td>
<td>Female</td>
<td></td>
</tr>
<tr>
<td>Food Caterer</td>
<td>Micro</td>
<td>-</td>
<td>3</td>
<td>Female</td>
<td></td>
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<tr>
<td><strong>Food Processing</strong></td>
<td>Baker</td>
<td>Informal</td>
<td>8</td>
<td>Female</td>
<td></td>
</tr>
<tr>
<td>Meat processing</td>
<td>Large</td>
<td>Organic Export Abattoirs</td>
<td>7</td>
<td>(2) Male</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Baby Food and Organic Foods</td>
<td>Large (150 employees in healthcare foods, 278 in Helina foods)</td>
<td>Hilina Enriched Foods</td>
<td>25</td>
<td>Male</td>
<td></td>
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<tr>
<td>Cereal Processing</td>
<td>Large</td>
<td>Eatteff Flour Factory and Injera Bakery</td>
<td>9</td>
<td>Male</td>
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<tr>
<td>Cereal Trader</td>
<td>Medium??</td>
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<td>10</td>
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<tr>
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<td>Informal</td>
<td>-</td>
<td>1</td>
<td>Male</td>
<td></td>
</tr>
<tr>
<td>Retail</td>
<td>Micro</td>
<td>-</td>
<td>6 months</td>
<td>Female</td>
<td></td>
</tr>
<tr>
<td>Manufacturing</td>
<td>Micro</td>
<td>-</td>
<td>11</td>
<td>Male</td>
<td></td>
</tr>
<tr>
<td>Manufacturing</td>
<td>Informal</td>
<td>-</td>
<td>2</td>
<td>Male</td>
<td></td>
</tr>
<tr>
<td>Textile</td>
<td>Manufacturing</td>
<td>Informal</td>
<td>9 months</td>
<td>Male</td>
<td></td>
</tr>
<tr>
<td>Retail</td>
<td>Micro</td>
<td>-</td>
<td>5</td>
<td>Female</td>
<td></td>
</tr>
<tr>
<td>Retail</td>
<td>Micro (2 Employees)</td>
<td>-</td>
<td>20</td>
<td>Female</td>
<td></td>
</tr>
<tr>
<td>Industry</td>
<td>Subindustry</td>
<td>Size (members)</td>
<td>Type</td>
<td>Gender</td>
<td></td>
</tr>
<tr>
<td>----------</td>
<td>-------------</td>
<td>--------------</td>
<td>------</td>
<td>--------</td>
<td></td>
</tr>
<tr>
<td>Retail</td>
<td>Micro (3-5 Employees)</td>
<td>-</td>
<td>3</td>
<td>F</td>
<td></td>
</tr>
<tr>
<td>Retail</td>
<td>Medium</td>
<td>-</td>
<td>22</td>
<td>M</td>
<td></td>
</tr>
<tr>
<td>Retail</td>
<td>Micro (2 Employees)</td>
<td>-</td>
<td>20</td>
<td>M</td>
<td></td>
</tr>
<tr>
<td>Stone-cutting</td>
<td>Small (18 members)</td>
<td>Group of stonecutters</td>
<td>2</td>
<td>M</td>
<td></td>
</tr>
<tr>
<td>Stone-cutting</td>
<td>Small (15 members)</td>
<td>Group of stonecutters</td>
<td>3</td>
<td>M</td>
<td></td>
</tr>
<tr>
<td>Stone-cutting</td>
<td>Small (18-20 members)</td>
<td>Group of chiselers</td>
<td>4</td>
<td>M</td>
<td></td>
</tr>
<tr>
<td>Stone-chiseling</td>
<td>Small (8 members)</td>
<td>Group of chiselers</td>
<td>3</td>
<td>F</td>
<td></td>
</tr>
<tr>
<td>Stone-chiseling</td>
<td>Small (10 members)</td>
<td>Group of chiselers</td>
<td>3</td>
<td>F</td>
<td></td>
</tr>
<tr>
<td>Stone-chiseling</td>
<td>Small (12 members)</td>
<td>Group of stone chiselers</td>
<td>1 year 4 months</td>
<td>M</td>
<td></td>
</tr>
<tr>
<td>Paving</td>
<td>Small (17 members)</td>
<td>Group of pavers</td>
<td>2</td>
<td>M</td>
<td></td>
</tr>
<tr>
<td>Paving</td>
<td>Small (18 members)</td>
<td>Group of pavers</td>
<td>3</td>
<td>F</td>
<td></td>
</tr>
</tbody>
</table>

**Site Visits**

- Interviews from Government stakeholders included representatives from the following offices:
  - Federal Micro and Small Enterprise Development Agency
  - Addis Ababa City Administration Micro and Small Enterprise Development Agency
  - Master Plan Project Office
  - Addis Ababa City Administration – Office of the Mayor and Cabinet Affairs
  - Integrated Land Information Center
  - Ethiopia Leather Industry Development Institute (LIDI)
  - Ethiopian Textile Industry Development Institute (TIDI)
• Addis Ababa Cobble Stone Project Coordination Office

• Private Sector Representatives/Institutions
  o Addis Ababa Chamber of Commerce
  o Addis Ababa Women’s Entrepreneur’s Association
    o Focus Groups with individuals in working in the leather and food processing industries
    o Interviews with individuals in all four focus industries
  o Ethiopian Commodity Exchange

• The team also visited six primary, secondary and tertiary markets within Addis Ababa in order to achieve a broad geographical representation of interviewees. Below is a list of markets and construction sites visited:
  o Shiro Meda
  o Shola
  o Ehil Berenda
  o Merkato
  o Zenebe Werq
  o Kaliti
  o Nifas-Silk
  o Bole
Annex 2: Market Distribution and Hierarchy

Source: City Development Plan 2001-2010, ORAAMP

Annex 3: Percent of newly created firms entering in the listed sectors

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2007</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>% of</td>
<td>% of</td>
<td>% of</td>
</tr>
<tr>
<td></td>
<td>start-</td>
<td>other</td>
<td>start-</td>
</tr>
<tr>
<td>beverages</td>
<td>ups</td>
<td>firms</td>
<td>ups</td>
</tr>
<tr>
<td>Food</td>
<td>35%</td>
<td>29%</td>
<td>22%</td>
</tr>
<tr>
<td>Textile</td>
<td>2%</td>
<td>6%</td>
<td>1%</td>
</tr>
<tr>
<td>Leather</td>
<td>5%</td>
<td>8%</td>
<td>5%</td>
</tr>
<tr>
<td>Cement</td>
<td>8%</td>
<td>11%</td>
<td>34%</td>
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Source: World Bank 2012
Annex 4: Typology of the Degree of Enterprise Informality

<table>
<thead>
<tr>
<th>Characteristic</th>
<th>Informal Economy</th>
<th>Formal Economy</th>
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<tbody>
<tr>
<td></td>
<td>Unofficial</td>
<td>Official</td>
</tr>
<tr>
<td>Degree of Informality</td>
<td>100 percent</td>
<td>High proportion of sales undeclared and workers not registered</td>
</tr>
<tr>
<td>Type of activity</td>
<td>Single street trades, cottage/micro enterprises, subsistence farmers</td>
<td>Small manufacturers, service providers, distributors, contractors</td>
</tr>
<tr>
<td>Technology</td>
<td>Labor intensive</td>
<td>Mostly labor intensive</td>
</tr>
<tr>
<td>Owner profile</td>
<td>Poor, low education, low levels of skills</td>
<td>Poor and non-poor, well educated, high level of skills</td>
</tr>
<tr>
<td>Markets</td>
<td>Low barrier to entry, highly competitive, high product homogeneity</td>
<td>Low barriers to entry, highly competitive, some product differentiation</td>
</tr>
<tr>
<td>Finance needs</td>
<td>Working Capital</td>
<td>Working capital, some investment capital, supplier credit</td>
</tr>
<tr>
<td>Other needs</td>
<td>Personal insurance, social protection</td>
<td>Personal and perhaps business insurance</td>
</tr>
</tbody>
</table>

Source: DCED 2009

Annex 5: Categorization of Taxpayers

<table>
<thead>
<tr>
<th>Category “A”</th>
<th>(a) Any incorporated company (b) Any business that has an annual turnover of ETB 500,000 or more</th>
<th>Pay a Value Added Tax (VAT) system</th>
</tr>
</thead>
<tbody>
<tr>
<td>Category “B”</td>
<td>Any business having an annual turnover of between 100 ETB and 500,000 ETB</td>
<td>Pay a Value Added Tax (VAT) system</td>
</tr>
<tr>
<td>Category “C”</td>
<td>Firms that have an estimated annual turnover of 100 ETB.</td>
<td>Pay an annual estimated tax – Turnover tax (TOT)</td>
</tr>
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</table>

Source: 2Merkato.com
## Annex 6: Income Tax

<table>
<thead>
<tr>
<th>Employment Income</th>
<th>Income Tax Payable</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 - 150</td>
<td>Tax Exempt</td>
</tr>
<tr>
<td>151 - 650</td>
<td>10%</td>
</tr>
<tr>
<td>651 - 1400</td>
<td>15%</td>
</tr>
<tr>
<td>1401 - 2350</td>
<td>20%</td>
</tr>
<tr>
<td>2351 - 3550</td>
<td>25%</td>
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<tr>
<td>3551 - 5000</td>
<td>30%</td>
</tr>
<tr>
<td>Over 5000</td>
<td>35%</td>
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</tbody>
</table>

Source: Proclamation No.286/2002
Annex 7: Map of Addis with Kebele as Administrative Unit
Annex 8: Map of Addis with Woredas as Administrative Unit