DISCUSSION ON THE DRAFT ECONOMIC POLICY OF THE TRANSITIONAL GOVERNMENT

Chairman: Mr. Taye Mengistae

Discussants: 1. Dr. Eshetu Chóle
2. Mr. Tsegaye Teklu
3. Mr. Makonnen Abraham

Rapporteur: Mr. Tekie Alemu

The discussion started with a presentation by the chairman, in which he summarized the major components of "Draft Economic Policy of the Transitional Government". This was followed by comments from the three discussants.

Presentation by Mr. Taye Mengistae

The topic of this session is The Draft Economic Policy of the Transitional Government. As we all know, we have no longer a draft but an actual policy that has been approved by the Council of Representatives; so we are going to discuss that policy. We have with us the discussants to pick up the discussion: Dr. Eshetu, Ato Tsegaye and Ato Makonnen.

Well, I shall begin by summarizing the document that has been approved by the Council of Representatives and then we will open the floor for discussion. I will speak mostly on the parts of the preamble of the policy that I believe are worthy of note.

One is that the policy is intended to be the basis for a programme for economic recovery through institutional reforms and structural adjustments in the broad sense of that term. And secondly, the policy is intended to be a minimum programme of all the parties involved in the Transitional Government and, at the same time, is intended to lay the foundation for the policy of the post-transitional government.

As a minimum programme of all those who are party to (or participating in) the transitional power structure, the general principles that are stated in the document to govern all aspects of the policy are:

1) Private domestic or foreign capital should play the maximum role in the economy without any legal barrier to entry to any industry or sector of the economy;
2) The intention is to design a development strategy in broad terms, and forming an incentive structure for the attainment of that strategy.

These principles are translated into policies with respect to agricultural development, industrial development, domestic and foreign trade, fiscal and monetary management, and with respect to development in transport, communication, mining, energy and housing and construction.

As far as the agricultural sector is concerned, the new policy is based on state ownership of all rural land, and as such retains all the essentials of the 1975 Land Reform, except that now private commercial farms are legalized as long as they do not threaten the tenurial security of tenant farmers. The policy rejects any scheme of compulsory grain delivery of farm produce, and leaves the role of the government in agricultural marketing to that of organizing purchasing schemes aimed at stabilizing farm prices in the context of a free market. It also calls for the closure or privatization of non-profitable state farms. And it promises the allocation of a greater share of public investment in agriculture to the development of modern farming.

With respect to industry, the new policy calls for the provision of incentives to private capital in all lines of activity, the privatization of non-profitable public enterprises and greater managerial autonomy to public enterprises that would not be privatized for one reason or another.

With respect to domestic trade, the new policy promises an explicit role for private enterprise in retail trade and a dominant role for the same, i.e. to private enterprise, in wholesale trade. But the policy also asserts the need for the regulatory role of the government with the aim of stabilizing prices, both at the retail and wholesale level. The policy also abolishes government monopoly in foreign trade and promises incentives to those who invest in export industries.

And finally, the policy renounces import quotas as a means of controlling/regulating imports and promises that, if any instrument is needed as a means of controlling/regulating imports, it will be only in the form of tariffs.

The new policy targets a balanced budget as an ideal goal and renounces the financing of any unavoidable deficit by bank- borrowing. It also commits a non-inflationary monetary policy, in the sense of limiting the growth of money supply to a maximum set by the growth rate of output. It strictly ties growth in money supply with the growth rate in real output.

And finally, the policy accepts that the Birr is overvalued and may have to be devalued sometime. But for the moment it rejects any measure concerning the currency. That is, for the moment, it excludes the possibility of any devaluation. But in that part of the document in which the possibility of immediate devaluation is rejected, there is the statement that it is not unlikely for devaluation to have any impact on the country's trade balance.

Well, that is the summary that I could come up with.

Discussion by Dr. Eshetu Chôle

I will not attempt to provide an overall statement of the New Economic Policy (NEP) -- I will continue to refer to it as the NEP.

In order to grasp this, we have to understand what kind of transition we are making. The basic statement here is that we are moving from a state-controlled economy to one that is more oriented towards the market. This is in general terms.

It has been conventional to refer to the Ethiopian economy as socialist. This strikes me as being really loose because it was not a socialist economy, and speakers this morning have alluded to this fact. When we have something like two-thirds of GNP originating in the non-state sector, which is essentially the situation that prevails now in Ethiopia now, I think it would be incorrect to refer to this economy as socialist. But it was a command economy nevertheless, in the sense that when we look at decision-making, as opposed to ownership patterns, state intervention in the area of marketing, pricing, resource allocation in terms of investment, foreign exchange, taxation and so on, the heavy hand of the state was there clearly. And the manner in which most of the basic economic decisions were made gave a lot of latitude for the state and, therefore, in that sense, we can talk about a command economy. And that is what we are trying to move away from.

There has been a discussion on the March 1990 reform, and we generally tend to say that there was no time to implement it and therefore it remained on paper. By and large, this is true but it is not entirely correct. Particularly with respect to marketing and pricing of agricultural products and co-operatives, certainly it was effective.

This being the kind of situation we are trying to move away from, where are we moving to? If we look at the general principle of NEP, the role of the state will be limited, private capital will be encouraged, and there will be greater scope for popular participation in the economy. These are the general principles. In terms of ownership, with reference to existing state enterprises, the general move is towards privatization, and with respect to new enterprises, it is argued that private enterprises will be given a much larger scope. In terms of decision-making, the policy says that state intervention in the economy will be minimized; there will be no privileges to be enjoyed by state enterprises, that is by those that will continue as state enterprises. They will have to compete with private enterprises and will enjoy a broad degree of autonomy, and will be guided by the criterion of profitability. In general, in decision-making there will be greater decentralization, and so on.

This is at the level of intent. Now, at the level of intent, does it represent much of a departure? Ato Makonnen [in the presentation on the Economic Reform Programme] has contended that it does not represent a radical break with the March 1990 reform, and I think to a large extent this is correct, although we

should avoid extremes in this case. This is because it will be incorrect to say that this is a radical break, since it is not really, as some of these principles have been anticipated in the March 1990 reform. So it is not as if we are being offered something totally new. At the same time, I also think that we should be careful not to say that there are no differences between the March 1990 reform and what is stated in the NEP. In the areas of trade, for instance, there are definite departures; so I think we should maintain this perspective.

This is at the level of intent. At the level of intent, therefore, the attempt is to move from a command economy to one in which the private sector will be given a greater role. If we confine ourselves to the level of intent, I think we will be misreading the entire situation because I think an important determinant here is the prospects for implementation of what is stated in the NEP.

This document is referred to as an economic policy for the transition period only. Now, strictly speaking it is not really an economic policy for the transition period only; and this is so for a number of reasons.

Firstly, the document itself says that this policy is intended to apply for the post-transition period as well in only slightly modified form. In fact, there is a contradiction there. In places we get the impression that this is a policy that will remain in effect until an elected government comes to power which will then implement whatever its economic programme is. On the other hand, we are also told that even if it is a policy for the transition period, the expectation is that it will apply in only slightly modified form; so there is this ambiguity.

Secondly, even if the policy is supposed to apply for the transition period alone, remember that the transition period is not supposed to exceed two and a half years, out of which we have already consumed four months. The implications of the policy are going to be far-reaching. For example, suppose the transitional government sells urban houses and compensates owners out of this income. A new government would come in two years later but there would be very little to undo. It would not be able to return the houses to former owners, for instance. The implications of some of the policies, and we can go on a sector-by-sector basis, are far-reaching. This means that the impact of these policies transcends the transitional period.

Not only this, but perhaps even more important is that the implementation of the NEP, in my opinion, is unlikely to begin in the transition period. First of all, the major tasks of the transition period, given the state of the economy, are unlikely to be development tasks. I think most of the country's efforts will be directed at rehabilitation and reconstruction of the economy. And if we do that in two years, I think we will have done very well. So I do not think we will have even the time to develop the long-term vision that is required to think of development. Secondly, many of the proposed measures require a number of institutional changes. For example, there is a great deal of change in legislation that is required, and I do not think that the homework for this has been done. This means that it is only now that we begin in terms of amending existing laws, repealing them, putting new legislation in place and so on. Thirdly, in the policy,

we read phrases such as "after study", "after careful study", and that kind of thing in many places. We simply have our hands full with all these careful studies that we have to make before the policy is going to be implemented. So I think we have to recognize that the policy is really not a policy for the transition period.

In terms of ownership pattern, my judgement is that we really cannot expect radical departures during the transition period from what we have now. Now, what are we going to do with the existing state enterprises? The principle of privatization is there but I think to implement this in the next two years would be extremely difficult. Some of the preconditions for privatization are really stringent. Even on housing, for example, what the policy says is that houses that have been nationalized will be sold; priority in purchasing them will be given to those residing in them; and compensation will be paid to those who deserve it. Even to determine that is going to take a long period of time. As regards the state enterprises, what is going to happen is that the state may remain saddled with them for some time to come. This is partly because of the lack of capital in the private sector even if the government wants to sell or because the state in which many of these enterprises are found now is not likely to be considered lucrative by private investors. So, in terms of ownership patterns, I suspect the picture two years from now is not going to be radically different from what it looks now. Thus, the idea of moving from a command economy to a market-oriented one has to be tempered by this reality.

In terms of decision-making, there is a scope. This is easier to contemplate. In other words, if the government is committed to do so, there is greater room for having less state intervention. So, in that sense, we may have a less interventionist state by the end of the two-year period than what we have now. But in terms of ownership and so on, I suspect we will continue with business as usual.

Apart from the issues that I raised now, implementation of a policy requires political commitment. I really do not want to speculate on whether or not this commitment is on the ground today. But my feeling is that there are perhaps political tasks that are considered more overriding or of more immediate nature, and I suspect that the government probably will concentrate on these political tasks, and, I think, the economy is likely to get secondary attention. If that is the case, it is unfortunate and the reform programme might remain on paper. And ultimately, whether the reform programme is carried but or not will be determined by the political realities of the country.

So, basically, what I would really conclude is that it will not be very realistic to expect significant departures in the direction of a market-oriented economy. Therefore, some of the problems of the command economy that have been plaguing us for the past so many years will not be very easy to get rid of, and we may have to live with them for some time to come. This is not a very bright prospect to contemplate, but I think it is a realistic one. So, the basic direction where the policy tries to take us, the reorientation away from a command economy, is I think correct. Whether or not in fact it will be moving

in any significant manner in that direction, at least in the transition period, I prefer to remain skeptical.

The related issue I would like to identify for discussion is the whole future of state enterprises. Privatization is easier said than done for the reasons I mentioned earlier. And for those that remain under state ownership there are three issues that we should raise here.

The first is that these enterprises will be guided by the criterion of profitability. Now, supposing that an enterprise does not show profit and there is no private investor willing to buy it, what happens? This is a practical problem that we have to contemplate. And my feeling is that the state might simply go on carrying it.

Second, autonomy is easier to declare than to implement. What it should mean, of course, is that managers of these enterprises should have very broad autonomy in financial matters, in management matters, in deciding their output mix and where to sell it, etc.

However, there are practical problems here. I just do not see the state simply saying to these enterprises: Allright you are on your own now. And even if it says "You are on your own", it will have to work out specific guidelines as to how far the autonomy extends--in areas of finance, management, employing and firing workers, and so on. Effective guidelines have to be worked out, and to work out these guidelines requires time. Of course, there has been change in faces at the top, but we have been used to a tradition where the state always had the privileged position to say do this and do that. To come out of that tradition and make this sudden change in attitude is going to be extremely difficult, and this will be even more true particularly for people who are actually engaged in the bureaucracy.

Third is the whole question of workers' participation in management. This is going to be a very controversial question because, on the one hand, autonomy is being granted to management, on the other hand, the manager is being told that there will be a management board on which a third of the representation will be that of the workers.

This is a debatable issue. The rationale given is that this will give a chance to the workers to act as a kind of watch-dogs against nepotism and corruption. But it is very difficult to visualise how the workers can ensure this. The workers' representatives will come with a trade union kind of mentality, because they will consider themselves as representing the interests of the workers and not take a global picture of the problems of that particular enterprise. And, I am sure, what they are going to do is press for higher wages, press for better conditions, etc., so that what you will create is a situation where management will be at odds with workers' representatives, simply because they are thinking in terms of different perspectives. Thus the whole question of the future of state enterprises remains one problem area.

The other controversial issue is the question of land. There are clearly two views on this. There are people who argue that land should be like any other commodity, and it should be subject to the rules of the market, whereas we are told that land will continue under public ownership. I think this is an area of debate that we simply identify without going into the pros and cons.

Another point of controversy is the exchange rate. We began a discussion earlier and I think we should come back to it. The donors are going to be insistent on an immediate adjustment in the exchange rate. There are many, including myself, who are skeptical on what an immediate exchange rate adjustment can do. I think this is another area for debate.

Then there are the social welfare consequences of these reforms which are going to be far-reaching in the absence of any safety net. The latter is particularly related to the prospects of getting generous foreign assistance. Implementing these reform policies, with or without devaluation, will be accompanied with some hardships. This country, on the basis of its own resources, cannot really take care of those hardships. So what are the prospects that external assistance will be coming in magnitudes significant enough to help us tide over these very difficult times?

I believe these are some of the issues that need to be raised.

Discussion by Mr. Tsegaye Teklu

In the first place I would like to mention an example. When I was a student I had a Cuban professor, and on one occasion my fellow students were provocative. And he responded by saying that, deep at heart, all Cubans are capitalists. And like Dr. Eshetu said just now, and like Makonnen said this morning, we said "We are socialists", while in reality the structure of ownership definitely was private in the majority of cases.

Secondly, we said that the March 1990 economic reform programme was a move towards a mixed economy, and the New Economic Policy is similar. There are people who say we do not have a mixed economy; either you have a market economy, or you do not have it. A mixed economy is a mixed mind--you do not decide on either one. The main problem is that an economic policy can only be general, it cannot go into the details; and it should show the directions, and the direction is from a centralized economy -- a centralized planning, socialist-oriented economy -- into a market economy.

During the past few years, the government took over the leadership in economic activities and economic development. Now, the private sector is supposed to take over the leading role in economic development. The New Economic Policy has been endorsed recently, but has not been issued to the public yet. I do not even have a copy and my office is supposed to be an implementing agency.

I should mention that inspite of the fact that we do not have any constitution for the transition period, and inspite of the fact that our office [Office of Investments and Joint Ventures] did not have the advantage of being the drafters or financiers of the economic policy, we took it upon ourselves from past experiences to prepare the investment legislation that will be used during this transition period and beyond. Dr Eshetu said that we still have to prepare the investment legislation that should follow the economic policy. We have already prepared the draft. Now that the economic policy is issued, we will have to review it in light of the policy.

Another point that has been raised is the case of state enterprises that are supposed to be profitable and those with which the government is going to be saddled for some time to come. Even though the latter case may be true for many enterprises, rationalizing the whole set of public enterprises is necessary. In the first place, the government is going to be saddled with those state enterprises engaged in directly productive activities. As far as I am concerned, those state enterprises that are engaged in trade activities, i.e., retail and whole sale and import and export trade will have to be abolished immediately-- there is no question about that.

I had an opportunity of participating in a discussion on the Draft Economic Policy. There are some issues with respect to land holding in Ethiopia. As pointed out earlier by Dr. Eshetu, private investment should be undertaken immediately. And for this to happen investors have to feel confident, that is, the government should have to gain credibility. Now, as I said earlier, you cannot invest in any type of directly productive economic activity without solving the question of land. This is a very important question. People cannot invest without the right of owning land. According to NEP, land is going to remain in the hands of the state, and people are expected to invest. But, if the economic policy does not guarantee that whatever you invested now would be yours beyond the transition period, nobody is going to venture into any investment activity-- even to the extent of planting trees, for that matter, because the commercial use of trees is not possible before five or seven years. And even the peasant is not going to see to the conservation of water and soil--he is not going to invest; he is not going to take care of the environment, at least try to ameliorate the degradation of the environment. And individuals and associations are expected to play a major role in checking environmental degradation in the country.

Discussion by Mr. Makonnen Abraham

In the case of industry, as mentioned earlier by Dr. Eshetu, participation of labour in the decision-making process has been stipulated after the management structure of our existing industrial establishment has been streamlined. But, looking at the labour code of Ethiopia, one observes that it is highly prohibitive as far as investors are concerned. Investors simply get scared because of the freedom given to labour. On top of this, the participation of labour at the board level will definitely scare foreign investors--there is no doubt about that. Of course, this participation is considered to be only in the state-owned enterprises. But what is it going to offer to labour working in the private

sector? Although the economic policy may be adjusted and improved over time, and may be seen as a step forward in the economic development of the country, the participation of labour in decision-making is going to be the basic problem for investors, particularly for the foreign ones.

However, I am in favour of privatization in industry. But who are going to be the investors? Will it be the local or foreign investors who are going to participate? If we let it open for all, there is no problem. But if we reserve it for domestic investors only, then we would ask: are they really in a position to buy the industries? As is well-known, these enterprises are usually overstaffed and contain at least 25 to 30 per cent idle labour. Then what are the new owners going to do with the existing labour force?

As far as land is concerned, my concern has already been expressed by Ato Tsegaye. Because owning land is owning property, I consider it to be a component of the democratic rights. But if you do not provide the right to own and sell land whenever you want to do so, then how are you going to participate in any joint venture activities, especially with foreign investors? And the major factor that is going to be contributed by the Ethiopians are the resources that the country has, and land is one. And if land is not going to be sold, then what are we going to contribute in the joint ventures?

With regard to trade, both the Draft and Final Economic Policy stipulate that, at least, domestic trade will be open to private investors. In the case of foreign trade, the Draft Economic Policy has deliberately excluded items such as coffee, in the case of exports, and petroleum, in the case of imports, as specifically state sector activities. The policy of the past regime had also this kind of exclusions but at least as far as coffee is concerned, it was open to both private and public sectors. The Draft Economic Policy wanted to leave coffee trade as a state monopoly, but it has been dropped now in the final policy document. However, there are areas that are going to remain under state control after thorough investigation.

In the case of finance, banking -- both financial and insurance -- will remain under state monopoly. But unless we open our banking sector to foreign investors, I do not think that there is any possibility of attracting foreign capital. We may not have problems as far as domestic currency is concerned; however, when it comes to foreign exchange, there is no way out but to attract and invite foreign investors. In fact, foreign investment will be forthcoming provided there is a foreign banking institution in a country.

As far as currency adjustment is concerned, the Draft Economic Policy has clearly indicated its intention to devalue the highly overvalued Birr. I do not think there is any other alternative, and I do not understand why people are skeptical. Now if someone is really skeptical, then he has to come up with the alternative. The World Bank together with the EEC and other donors are already here to embark upon emergency, rehabilitation and reconstruction programmes on the assumption that Ethiopia will undertake SAP [structure adjustment programme] starting next June.

Anyhow, with or without SAP, the problems are here and are bound to get even worse. Therefore, I think some form of structural adjustment is going to be an inevitable issue. Therefore, as mentioned earlier by Dr. Eshetu, NEP is assumed to be a transitional programme but it is not going to be implemented during the transition period. Its implementation is a long-term one. In fact, SAP, if undertaken, will take more than two years. If that is the case, this NEP document is going to be revised again and again in order to really reflect the existing situation of the country.