THE PERFORMANCE OF PRIVATE INDUSTRY AND THE ROLE OF THE STATE

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Abstract

The neo-classical school argues that private entrepreneurs guarantee full employment through their independent actions in a freely competitive environment. On the contrary, according to structuralists, information asymmetry, externalities, failures to exploit economies of scale, the need for technological innovation and transfer and dynamic transformation of the structure of an economy require a well-thought action of the state. In light of these perspectives, the objective of the paper was to examine the performance of the private industrial sector after a package of liberalisation policy measures were undertaken in the country. Within the last couple of years, the number of private manufacturing establishments, their capital and output has increased as compared to their low basis. On the other side, factor productivity, capacity utilisation and other similar measures indicated that efficiency of private firms has still been very low and even deteriorated. The structure of sector and distribution of industries has still been lopsided. Under developed market structure and other infrastructure, swift liberalisation without developing local capabilities, low level of involvement and support from the side of the government in strategic industries and capability building ventures were some of the constraints. As structuralists contended, taking into account the nature of constraints, the state should play a supportive role to facilitate and improve private sector efficiency and its sustainable growth.

1. INTRODUCTION

Development stories of successful West and Far East Asians as well as the destitute life of Sub-Saharan Africa and the rest of the world reveal that a structural shift away from agriculture is a feasible policy instrument for sustainable economic development. Development manifests itself through dynamic transformation of the structure of the economy in terms of changes in the composition and the level of demand, input requirements, production and trade towards secondary and tertiary sectors (Chenery, Sherman and Syrquin 1986). In this endeavour, manufacturing industry plays a pivotal role.

The economic structure, the degree of political stability, the presence of resources, markets and strong capitalist class, the organisation of industries, and the conscientious and well-thought acts of governments are the primary determinants of industrial development. Volumes of literature are documented on the controversies of the role of market and the state.

Pro-market economists argue that enterprises allocate resources in accordance with consumers' demand by the '*invisible hand*' and free competition tends to ensure Pareto-optimality. Prices ensure that the structure of production in a country will be consistent with the resources available to it. In their motives of maximising profits, private entrepreneurs in a free market setting will guarantee full employment and maximise social welfare through their independent individual actions (Thrilwall 1994).

On the other hand, due to lack of adequate information and skills, governments are inflexible and unable to change course when mistakes become apparent. They even tend to represent sectional rather than national interests and they might even be venal or corruptible (Lall 1996). Governments usually tend to impede development as they interfere in well-functioning markets. Thus, they need to do away with such interventions as protection, subsidies, licensing, state-led researches and the provision of other similar facilities. Instead, governments should focus on liberalising markets, privatise public enterprises and allow individuals to accomplish their activities the way they like.

Other economists (Thrilwall 1994; Stiglitz 1996 and 1997; and Lall 1996) argue that markets are either non-existent or under developed particularly in third world countries. In such a situation, governments should intervene to guide and supplement markets for efficient allocation of resources and for a rapid pace of development.

Given the natural preference of people for present rather than future satisfaction, free markets will tend to allocate resources for the production of consumption goods than otherwise. This would definitely affect the welfare of the future generations. Indeed, individual firms may not be capable or are less willing to involve in huge investment ventures whose benefits might accrue in the long-run.

Co-existence of shortage of capital and foreign exchange, on the one hand, and surplus labour, on the other, at the existing market prices is an evidence for structural disequilibria. Indeed, individual investors tend to ignore external economies in their cost-benefit analysis due to lack of special incentives. Consequently, sub-optimal decisions of individuals on such areas as technical and managerial training may harm the development of the industrial sector.

According to the infant industry argument, industries require a certain period of protection. Leaving matters to the mercy of the market, where severe import competition exists, may hold back entry into activities involving risks and demanding huge investment on technology in developing countries. Furthermore, industrial success depends essentially on how much individual firms manage the process of technological and managerial development. Developing new skills requires a considerable investment and co-ordination among other firms and institutions (Lall 1996). The initiatives on this risky and unpredictable venture should come from the side of the state.

The existing structures of markets and the demerits associated with public actions could not allow for a choice between the two different actors. The issue rather revolves around the extent to which government should intervene into the actions of private firms such that the economy will grow.

As development literature indicates, behind the incredible economic successes of Japan, Hong Kong, Singapore and others, there have been thoughtful actions of governments to augment and regulate markets. Governments have influenced the allocation of capital (through banks) towards growth-oriented activities and availing better access to credits even at subsidised rates. There was a considerable investment on growth-oriented education by the state on such areas as engineering and science for smooth transfer and innovation of technologies (Stiglitz 1997).

China has been the world's fastest-growing economy since it was able to combine plans with markets in 1978. Significant restrictions remain especially on trade and entry (World Bank 1996).

In Africa, Botswana reported a remarkable rate of growth in manufacturing value-added. Government intervened through the provision of incentives for private entrepreneurs in the form of short-run subsidies for protected industries, financial assistance based on long-run merits and provision of infrastructure services priced at opportunity cost (Clough and Manor 1995). On the other side, the Ghanaian Government severely liberalised markets but with no avail to the economy. Employment in manufacturing drastically fell. Neither foreign investment responded to the adjustment, nor did activities of domestic private investors pick up (Lall 1996).

Based on the above discussions, one could tend to conclude that liberalisation by itself cannot lead firms to efficiency and make them successful in the face of international competitions. At any rate, governments should create an enabling environment and a level ground for domestic private entrepreneurs to strongly compete with imports.

When situations in Ethiopia are examined in this perspective, the manufacturing sector has gone ups and downs for about a century through seemingly polar cases of government intervention. Ten years earlier, directive system of management was governing the economy in which the private sector was highly marginalised. The contribution of manufacturing industry to GDP, employment and export earnings of the country have been very limited. Recently, market-driven economic policies have been introduced. These recent changes in the policy environment have led to the revival and expansion of private industries in some respects. Yet, markets are not only imperfect but also underdeveloped in many respects. The country has not built up a strong capitalist class. In terms of almost all indicators, the economy is extremely backward. Democratisation and institutional building is in its rudimentary stage. Other things being constant, the very socio-economic basis of the prevailing policies greatly affects the performance of the sector.

Thus, the objectives of this paper are to assess the performance of the Ethiopian private industrial sector during the reform period,[1] to identify the major constraints in the context of the existing market structure and in view of this to examine the room for government intervention.

The analysis of the paper largely depends on descriptive statistics and the sources of information are mainly Central Statistical Authority, Ethiopian Investment Authority, and the Ethiopian Privatisation Agency. Lack of cross-section data on the performance of private industries and the short period to evaluate impacts of the reform measures through time series analysis could not allow employing econometric models.

The rest of the paper is organised as follows. The second section briefly assesses the policy environment. Section three examines the performance and major constraints. Finally, the paper concludes its discussions in section four by identifying possible areas of government intervention to facilitate the activities of the private sector.

2. THE POLICY ENVIRONMENT

In line with a free market operation, selective intervention on private sector activities created a favourable condition for a progressive industrial sector during the Imperial regime. On the other hand, strengthening the role of the state in the economy as against the market was a driving motive of the system during the military government.

Both foreign and domestic enterprises were nationalised which broke the steady flow of foreign direct investment and the process of industrialisation thereof. Capital ceilings, tedious bureaucratic procedures, and restrictions on the supply of foreign exchange, skilled manpower and credit were imposed on private ventures. As a result, the shares of the private sector in output and employment in medium- and large-scale industrial establishments were only 4.0% and 8.1%, respectively in 1988/89 (CSA 1990). On the other hand, inefficiency and capacity underutilisation were found rampant among public industries (Worku 2000).

In contrast to the command policy of the Derg, the Transitional Government of Ethiopia introduced the New Economic Policy with the intent of granting a leading role to privates in development. In light of free market principles, the Public Enterprise

Reform (PER) was undertaken to ensure that forms of ownership would no more be barriers to competition. To further strengthen the share of the private sector, privatisation has also been undergone.

The investment proclamations and codes provided different incentives including tax holiday for a certain period and tariff exemption on machinery and equipment with their accessories. In order to promote exports, the Birr was devalued. Subsequently, an auction market for foreign exchange was introduced with an ultimate objective of setting a floating exchange rate regime. The provision of a duty drawback scheme, and the elimination of taxes and duties on exports except on coffee were some of the measures taken to encourage exports.

A downward revision of tariffs was introduced in step, the maximum tariff rate on imports being reduced from 230 per cent to 40 per cent. Profit taxes were also reduced from 89 per cent to 35 per cent and all forms of subsidies were removed. While these and other similar measures are targeted to liberalise the market, the government has also implemented the Agricultural Development Led Industrialisation Strategy (ADLI). The issue here is to what extent the existing policy environment, the nature of markets and other pre-requisites are conducive for the participation and performance of the private sector in general, and the growth of the manufacturing industry in particular.

3. PERFORMANCE OF PRIVATE INDUSTRIES AFTER THE REFORM

3.1. Operational Performance

In 1991/92, there were 131 private medium and large-scale industries, which engaged on the average 32 persons per establishment. Encouraged by the investment incentives provided, entrepreneurs have progressively established new manufacturing units and expanded small-scale enterprises. As a result, the number of operational private medium and large-scale industries grew to 607 in 1997/98 (CSA 1999).

Table 1: Performance in Terms of the Volume of Activities

Indicators	1991/2	1992/3	1993/4	1995/6	1996/7	1997/8	1998/9	Av. Growth Rate
Establishments	131	137	330	327	473	580	607	36.1
Persons Engaged	4172	4183	8518	9398	13239	21509	26028	45.2
Fixed Capital ('000 Birr)	24582	26476	127775	173235	369221	814539	1252792	118.9
Gross Value of Production (GVP) ('000 Birr)	133140	160575	430647	781014	790911	1243180	1813575	62.4
Value Added at Factor Cost (VAaFC)('000 Birr)	28849	27276	92604	120792	193254	321115	355806	66.9

Source: CSA (Central Statistical Authority) (1992-1999). Production values are adjusted in the 1996/97 prices.

Table 1 shows the performance of the private sector with regard to medium and large-scale industries during 1991/92-1997/98. In terms of all selective indicators, the private sector has registered a notable record.[2] Both gross value of production and value added at factor cost figures were growing at an average annual rate of 62 per cent and 67 per cent, respectively. This could be attributed to the revival of capacity utilisation due to the prevalence of peace and stability, the abolition of a seemingly monopolistic control of input and output markets by public firms and other discriminatory practices as well as the expansion of private investments in response to policy measures.

Labour force and net fixed capital were growing at a rate of 45 per cent and 118 per cent per annum between 1991/92-1997/98 owing to new investment activities and privatisation of public industries. The disproportionate growth of job opportunities and capital is mainly the result of the rising prices of machinery and equipment and the non-incompatibility of imported technologies to the country's resource endowment.

Even though the private firms have been reviving and expanding in terms of volume of activities, sub-optimal use of resources becomes apparently the main feature of the sector.

Table 2. Performance in Terms of Some Efficiency Indicators

Indicators	1991/2	1992/3	1993/4	1994/5	1995/6	1996/7	1997/8
Private Sub-sector							
VAaFC/GVP (%)	21.7	17.0	21.5	15.5	24.4	25.8	19.6
VAaFC/Persons (in 000 Birr)	6.9	6.5	10.9	12.9	14.6	14.9	13.7
VAaFC/Fixed Capital	1.2	1.03	0.72	0.70	0.52	0.39	0.28
Capital-Labour Ratio (in 000 Birr)	5.9	6.3	15.0	18.4	27.9	37.9	48.1
Total Factor Productivity	1.3	1.15	0.93	0.92	0.70	0.52	0.39
Capacity Utilisation in %	-	-	-	-	32.5	45.5	47.4
Medium & Large-scale: Total							
VAaFC/GVP (%)	19.1	6.7	29.6	27.3	27.4	28.0	24.0
VAaFC/Persons (in 000 Birr)	5.5	8.25	15.2	17	17.5	17.9	17.9
VAaFC/Fixed Capital	0.46	0.51	0.75	0.87	0.71	0.61	0.54
Capital-Labour Ratio (in 000 Birr)	12.0	16.1	20.3	19.5	24.7	29.3	33.2
Total Factor Productivity	0.45	0.73	0.90	1.03	0.98	0.94	0.94
Capacity Utilisation in %	-	-	-	-	53.8	48.6	58.2

Source: Own Calculations Based on CSA (1992-1999).

In 1991/92, one person in a private medium and large-scale industry contributed on average 6,900 Birr worth of value added. This amount has shown an increasing trend except the 1997/98 marginal decline. The growth of labour productivity is attributed to improvements in the availability of raw materials due mainly to the Economic Rehabilitation and Reconstruction Program and the continuous adjustments in the composition of capital and labour towards the former. No consistent tendency has been observed in the share of value added at factor cost to gross value of production. It oscillated with minimum and maximum records being 15.5 per cent and 25.8 per cent in 1994/95 and 1996/97, respectively. Both capital and total factor productivity[3] of private firms consistently declined throughout the years.

The performance of private firms was on the average better than their public counterparts in many respects sometimes back within the reform period but not recently. This may be partly due to the fact that a considerable number of private firms commenced production in recent times, which should have been allowed a learning period (through adequate protection) to operate at their optimum level of production. Indeed, even at a very low level of managerial capabilities of local entrepreneurs and insufficient experience in open market operation, recent liberalisation measures have created a fierce competition with imports.

3.2. Investment and Privatisation

The different investment proclamations and other related policy measures have created a favourable environment for both indigenous and foreign investments. During 1991/92-1998/99, 2003 new and 256 expansion industrial projects obtained permanent license. Among the 2259 projects, 532 (25 per cent) were under construction and 720 others (32 per cent) have already commenced operation. With a total investment cost of Birr 7,381.8 million, when all completed, these projects would create 40,821 permanent and 21,044 temporary jobs.

Table 3. Approved Investment Projects (1991/92-1998/99)

Project Status	Number	Capital in Million Birr	Job Opportunities			Share of Capital	
			Permanent	Temporary	Total	Local	Foreign
1 Permanent License Given	2259	15971.3	90174	23388	113562	96.2	3.8
1 New	2003	14547.5	82335	22991	105356	96.1	3.9
1.2 Expansion	256	1423.8	7839	397	8236	96.9	3.1
2. Under Construction	532	4864	23175	4977	28152	95	5
2.1. New	482	4415	21162	4977	26139	94.5	5.5
2.2. Expansion	50	449	2013	-	2013	98	2
3. Commenced Operation	720	2517.8	19659	16067	35726	97	3
3.1. New	628	2133.7	16599	15789	32388	97	3
3.2. Expansion	92	384.1	3060	278	3388	96.7	3.3

Source: Investment Office of Ethiopia (1999).

Noting the limited domestic investment potential and the depressing effects of the then command economic policies on local entrepreneurs, there was a great hope for foreign direct investment to play an active role in the country's industrial development. To this effect, the government put in place different incentive mechanisms to attract foreign investors including granting the right to extract profits and dividends accruing from investment. However, the measures could not bring about tangible results in this area. Foreign investors usually mention problems associated with the acquisition and conditions governing the availability of land and loan as well as poor infrastructure as their serious constraints.

With the aim of altering the role of the state in the economy in favour of the private sector, the Ethiopian Privatisation Agency put 56 public industrial enterprises for sale until June 1999. Out of these, 30 establishments were privatised with a total proceeds of Birr 1.06 billion (Ethiopian Privatisation Agency 1999). The slow process of privatisation is attributed to lack of resources and interest by local investors, limited participation of foreigners and obsolescence of the enterprises.

As it is indicated in Table 4 below, the share of the private sector from the total volumes of industrial activities has been increasing owing to investments in new and expansion projects as well as the privatisation measures.

Table 4. The Percentage Share of the Private Sector from the Total Activities of Medium and Large Scale Industries

Indicators	1991/92	1997/98
Gross Value of Production	5.6%	25.8%
Fixed Assets	2.5%	40.1%
Employment	5%	25.7%

Source: Own Calculations.

3.3. A Tendency for Structural Change

Structural change towards the production of capital and intermediate goods, and investment in the chemical, metallic and non-metallic industries play a pivotal role in determining the pace and sustainability of industrial development (Mahalanobis 1963). Experience of East Asian countries also revealed that emphasis towards the afore-mentioned sectors promotes technological innovation and strengthens both backward and forward linkages to the rest of the economy. Recent investment proclamations and codes have provided investors with various forms of incentives towards these areas.

The composition of private investment reveals that, coffee-hulling[4] enterprises alone accounted for around 50 per cent of the job created and 20 per cent of the total capital invested. The food industry also held 15 per cent of the labour force and 11.5 per cent of the total capital. On the other hand, metallic and chemical industries accounted for only around 20.6 per cent and 15.5 per cent of the total capital respectively, and their contribution in creating jobs was also very limited. Projects under construction are as well concentrated in the food sub-sector in terms of both investment and the creation of job opportunities.

Table 5. Distribution of Investment Across Sectors

Sub-sector	Commenced Operation		Under Construction	
	Capital % Share	Job Opportunities % Share	Capital % Share	Job Opportunities % Share
Food	11.5	15.0	22.2	23.6
Beverage	11.6	2.4	3.4	3.3
Coffee-Hulling	19.7	49.8	5.9	23.1
Textile	3.1	6.0	14.9	9.0
Leather	10.3	6.2	7.0	5.3
Wood	2.4	2.0	0.8	1.7
Paper & Printing	2.6	1.9	13.2	5.8
Chemicals	15.5	7.7	13.0	10.5
Non-Metallic	2.8	2.4	4	4.8
Metallic	20.6	6.8	15.4	12.9
Total	100	100	100	100

Source: Investment Office of Ethiopia (1999).

Table 6. Structural Change in Terms of Percentage Share of Sub-Sectors

Sector	1991/92				1997/98			
	Persons	VAaFC	Export	Import Intensity	Persons	VAaFC	Export	Import Intensity
Food	17.8	20.8	23.5	14	18.9	22.9	7.0	13
Beverage	9.3	13.1	0.3	27	8.7	11.3	26.4	33
Tobacco	1.1	11.7	-	41	1.0	6.4	-	72
Textile	41.1	17.0	7.3	24	31.2	8.5	2.8	36
Leather	7.6	6.1	68.9	23	8.2	7.1	63.6	20
Wood	5.6	4.1	0.1	29	6.0	4.0	-	37
Paper & Printing	5.3	10.6	-	59	5.9	7.1	-	69
Chemicals	4.3	8.8	-	86	7.7	15.1	-	82
Non-metal	3.9	5.0	-	57	7.8	12.2	0.1	36
Metal	4.0	2.8	-	86	4.6	5.3	-	96
Total	100	100	100	33	100	100	100	43

Source: Own Calculations from CSA (1992-1999).

Both public and private medium and large-scale industries concentrated on the production of consumer goods. The food, beverages, tobacco, textile and leather industries together accounted for 68 per cent, 56.2 per cent and 99.8 per cent, respectively of total employment, the gross value of production and exports in 1997/98. On the other hand, the share of capital and intermediate goods industries has slightly improved over the last seven years. This was at the expense of the noticeable decline in the textile sector due to lack of market.

Even the existing private factories and projects on chemical, metallic and non-metallic sub-sectors are and would be small in size and largely involved in the production of non-durable goods, which might not bring a multiplier effect on the economy.

According to the New Economic Policy, the government has expressed its intention to participate in strategic sectors as chemical, metallic and non-metallic industries. However, it has not sufficiently adhered to its promise. The experience gained from the last few years tended to suggest that without a firm commitment by the state, private investors alone could not bring about an observable structural change. Table 5 depicts changes in the relative shares of the sub-sectors. Sustaining high level of dependency for imported inputs in line with embryonic metallic and chemical industries is an indication of a gloomy picture with weak backward and forward linkages within and outside the sector.

3.4. Regional Distribution of Industries

An equitable distribution of industries amongst regions is justified on both social and economic grounds. The distribution of investment across regions depends on the degree of access to electricity, water, road, telecommunications and other facilities, input and output markets, population size and other factors. Addis Ababa accounts for a considerable proportion of the total industrial investment followed by Oromia, Tigray, Southern Nations and Nationalities and Amhara. Benishangul-Gumuz, Somalia, Afar and Gambella regions account for a marginal share of the total investment. Since investment is a flow, its direction changes the stock of industries amongst regions.

Table 7. Regional Distribution of Industries (Percentage Share)

Regions	% of Number of Establishments			Employment	
	1991/92	1994/95	1997/98	1994/95	1997/98
Addis Ababa	76	64.9	66.9	60.6	59.1
Oromiya	11.7	12.8	12.3	15.7	17.7
Southern Nations and Nationalities	2.1	7.0	7.2	4.6	5.1
Amhara	5.3	6.6	5.6	9.2	8.3
Tigray	0.7	3.2	3.7	0.3	2.9
Dire Dawa	2.5	3.8	2.8	7.7	5.6
Harare	1.4	1.2	0.9	1.4	1.1
Others	0.3	0.5	0.6	0.5	0.2
Total	**100**	**100**	**100**	**100**	**100**

Source: CSA (1992-1999).

There seems to be some improvements in the distribution of industrial establishments among regions. For instance, the relative shares of Oromia, Southern Nations and Nationalities and Tigray in terms of the number of establishments and employment have improved somewhat since 1991/92. However, Addis Ababa still remains the largest beneficiary while regions such as Benishangul-Gumuz, Afar, Gambella and Somalia continue to be the most disadvantaged. This disparity in the distribution of industries reflects economic imbalances, which might cause income and living standard inequalities among regions.

3.5. Constraints

The manufacturing sector in general and the private industries in particular are facing severe problems associated not only in terms of efficient use of resources and marketing, but also in their inherent structure and distribution. Among others, the following need mentioning.

a) Market Distortions and Swift Liberalisation Process

Markets in Ethiopia are highly imperfect and peculiarly underdeveloped. There is a dual economic structure with almost stagnating traditional agriculture and relatively modern industrial and service sectors. The vast majority of the population earn their living from subsistence farming in which the role of markets is marginal. The presence of non-monetised segment of the economy, risk-averting behaviour of farmers, and skill differentials between rural and urban areas are some of the rigidities behind the structure of the labour market. Only 6.5 % of the urban employed were wage earners, leave alone the 85 per cent of the population residing in rural areas. Of the remaining urban residents, 57.1 per cent were own account workers and the rest were unpaid family workers (Jemal 2000). Within this context, the role of markets in determining the level of employment and wages is insignificant.

Illiteracy has been a major bottleneck for development. According to MEDaC (1999), Ethiopia has one of the least enrolment rates (for instance 34.6 per cent in 1993/94 for grades 1 to 6 and 8.1 per cent in 1995/96 for grades 8 to 12). Communication services are by far inadequate. The prevailing road densities, domestic airline services and railway facilities of the country reflect that smooth flows of information are hardly possible. Due to these and other factors, distortions predominate in both factor and product markets.

In principle, land as a basic prerequisite for investment is recently left for the market in accordance with the lease policy. In practice, both local and foreign entrepreneurs complain about problems associated with the acquisition of land. While the supply is under the control of the state, the offer could reflect neither the opportunity cost nor it is set on the basis of demand and supply in the market.

The existence of well-functioning capital market plays a significant role to promote investment. In practice, the formation of a full-fledged stock exchange market is yet to be seen. The ethics of customers and their capacity to borrow on the basis of tangible economic rationale as well as the capacity of financial institutions to evaluate loan proposals has not developed leave alone expecting commercial banks to guide their customers.

On the basis of such types of markets and other supportive facilities, the government has been increasingly introducing liberalisation measures. However, operating under the command economic rules for years, the entrepreneurial and managerial capabilities of local firms are such that they could not withstand fierce competition from abroad. Their managerial weakness, among other things, is reflected in their failure to alleviate operational problems like shortages of raw materials and working capital, frequent breakdown of machinery and equipment and lack of spare parts. Of the 762 medium and large-scale industries, (607 are private enterprises), 360 industries (47.2 per cent) attribute market related problems for their malfunctioning (CSA 1999).

b) Inadequacy of Infrastructure Facilities and Policy Related Problems

Experiences of countries revealed that human resource development allows building entrepreneurial capabilities, facilitating the transfer, invention and innovation of technologies and improving productivity of workers. Skilled manpower shortage has been a great impediment to the country's industrial development. Even though, a number of training and education institutions have been established recently, they are not sufficiently guided to deal in accordance with the technical and managerial skill requirements of the sector. Strong co-ordination among training institutions, the Commission for Science and Technology, the Ministry of Trade and Industry, the Agency for Basic Metals and others has not been vividly observed. Neither adequate incentives nor efforts exist to develop technologies compatible to resource endowments of the country.

Lack of capacity to skilfully conduct feasibility studies, properly design and implement projects led industries, among others, to concentrate on the production of similar items and cost over-runs, which ultimately reduce the competitive advantages of local firms.

Generic policies, strategies and directives govern the industrial sector and industry sector-focused policy has yet to be pursued. The institutional capacity of tax and tariff authorities to properly assess incomes of customers and accordingly levy taxes as well as take proper inventory of the volume and type of goods in imposing tariffs is not sufficiently developed. Indeed, the government has not sufficiently committed itself to introduce discriminatory tax measures such that merchandise capital would be increasingly diverted to industrial investment. In a similar manner, financial institutions are not directed to extend their loans in favour of development projects.

Adequate provision of economic services like electricity, water and roads are prerequisites for equitable and sustainable industrial development. Acres (1992) indicated that the country was able to realise only 1 per cent of its hydroelectric potential. The consumption per capita of energy in 1995 was found to be only 22 kilowatt-hours, which put the country as the least user in the world (World Bank 1999). Frequent interruption of electric power also greatly affects the operation of industries. Similarly, the road network is also backward as compared to other Sub-Saharan African countries (World Bank 1994). Even though, efforts are made to mitigate these acute problems, they are still major impediments for investment and ultimately cause for the concentration of industries in very few urban centres.

c) Structural Problems

The concentration of industries is biased towards the production of consumer goods with very weak linkage to the rest of the economy. Capital and intermediate goods industries, which could have facilitated the transfer of technology and the development of heavy industries with multiplier effects, are at their infancy.

4. CONCLUSION AND POLICY ISSUES

The private sector in Ethiopia has gone through ups and downs. The command economic policy effectively stunted the role and share of private firms, which eventually dismounted the development of the industrial sector as a whole. On the contrary, the incumbent government introduced the New Economic Policy with various supportive measures with the view that active participation of the private sector in a free market setting will accelerate growth. In response to policy changes, the participation and share of the private sector has been expanding in terms of investment, employment and output.

However, the private sector found itself in a precarious situation in the case of efficiency and marketing. The industrial sector has also continued to face structural problems. Endless and excessive protection may perpetuate industries in acute inefficiency. On the same token, the cost of liberalisation without allowing local firms adequate periods for learning and building capabilities in the absence of well-developed product and factor markets and supportive institutional facilities might be unbearable.

Thus, taking into account the potential danger of its involvement beyond a limit, government should reconsider liberalisation measures and provide a reasonable support for the private sector in its endeavour to improve efficiency.

a) In order to improve their efficiency and develop their capacity to withstand the fierce competition in the domestic markets and to gain foothold in the export markets, local industries require support for a reasonable period. In this connection, policymakers should cautiously examine issues such as the adequacy of the existing support, the type of industries that require this privilege and other non-tariff.

b) Government needs to either extend its technical support to private institutions that may undertake project feasibility studies or strengthen its institutional capacity to directly conduct industrial projects and grant documents of viable projects for private investors with a subsidised price. Adequate support is also required for construction firms to develop their capacity. Mechanisms should be worked out for timely and effective enforcement of contracts.

c) Conditions should be created for industries to have easier access to both working and investment capital. Government may consider extending subsidised credit. It also needs to set a tax and tariff structure that tends to favour the manufacturing sector at the expense of other sectors such as the merchandise business.

d) Industries should be provided with technical assistance to alleviate shortages of skilled manpower and problems associated with entrepreneurial capability. Government should continue to establish technical training institutions, to provide incentives to private entrepreneurs involved in the area and to co-ordinate the efforts of all concerned public and private bodies.

e) The government should also adequately redress infrastructural problems such as communication, roads, water and power supply, in order to curb regional imbalances in the distribution of industries and allow the existing enterprises to constantly carry out their activities. The establishment of industrial estates should also be considered across regions as a special incentive to investors.

f) Due to the danger of excess capacity in the capital goods sector, private industrialists are reluctant to bear the risks of building far in advance of demand or of carrying large losses for long periods in a small country (Griffin 1989). Hence, government should certainly continue investing on industries with long gestation periods in line with its commitment to the New Economic Policy.

g) Finally, comprehensive industrial development policy that would guide and set the pace of industrialisation should be introduced as a matter of priority.

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[1] Due to data limitations to examine changes over time, the analysis focuses on large- and medium-scale industries.

[2] In this connection one could not deny the fact that the worse performance recorded during the last years of the Derg and initial years of the TGE (as a base) could partly attribute this remarkable achievement.

[3] Total factor productivity is measured through VAaFC/aW+bC. VAaFC, W and C stand for value added at factor cost, wages and fixed capital while a and b stand for factor shares of labour and capital, respectively.

[4] There might be a debate whether these enterprises should be considered as industries or not. However, the Ethiopian Investment Authority, the source of the information, considers them as industries.

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