Can Ethiopia’s Planned Economy Stand the Test of Time?

Ibrahim Babatunde Anoba
Can Ethiopia’s Planned Economy Stand the Test of Time?

By Ibrahim B. Anoba

Earlier this week, the World Bank reported that Ethiopia would be the most expansive economy in Africa for the year 2017. This forecast is because of its steady economic growth average of 10.8 percent since 2005, which peaked to 6.5 percent in 2016 – one of the highest in the world. But despite its commendable progress, a high tax rate and continued state monopoly in key sectors might compromise its ability to sustain the economic momentum.

Among emerging African economies, Ethiopia is prominent for its state dominated system. A 2016 Heritage Foundation report ranks it among the mostly unfree economies on the continent (142nd in the world), only surpassing the likes of Chad, Eritrea and Sierra Leone. This is relatively due to the numerous legislations that restrict foreign investments in major parts of the economy. Consequently, only a privileged few – usually politicians- have access to prolific industries like telecommunication and finance. One can attribute this to Ethiopia’s relatively stagnant per capita income of $590, which is substantially lower than the regional average. Coupled with its economic stiffness, Ethiopia has a burdening tax system.

Tax rate in the country is among the highest in Africa. It currently charge 15 percent in sales tax based on the purchase price of commodities; levy a 35 percent personal income tax and hold a 30 percent corporate tax rate. These heavy figures have reduced the consumer purchasing ability as most businesses hike prices on commodities to recoup loss to the state purse, thus inflicting blows on individual income. It has also affected the informal sector that fortifies the economy.

Besides the negatives of high tax, the Ethiopian of Government’s (GOE) monopoly in key sectors like telecom, finance and logistics undermines its economic prosperity.

In the logistics industry, GOE owns 60% of imports freights and cargos while 40 percent belongs to private firms. It is however unsurprising the industry has yet to contribute more than its present 10 percent quota to the GDP or create more jobs. And this is despite its enormous potentials if completely privatized.

Likewise, the state telecom agency, Ethio Telecom controls all services including fixed, mobile, internet and data communications. And to Ethiopia’s loss, the strong monopoly deprives the sector necessary competition that could birth profitable innovations. Moreso, the quality of telecom services in Ethiopia is on a level majority of Africa were over a decade ago. But while the rest of the continent is reaping the benefits of an increasing competitive telecom sector, Ethiopia remains stagnant.
However, a liberalized telecom industry promises more service quality at cheap prices, which many businesses crave in Ethiopia. If this happens, development in the industry might eventually influence other sectors, and of course, greatly help the 20 million unemployed Ethiopians. Similar positives can ensue in its enclosed banking sector is it extends the liberalization intent.

Although the GOE allowed the establishment of private banks and insurance companies in 1994, it still prohibits foreign ownership. Interestingly, Ethiopia’s banking system comprises of a central bank (NBE), two government-owned banks and eighteen private banks. This obviously appears sufficient for an emerging economy but, a US based financial monitor, the International Trade Administration (ITA) gave a clear picture of the banking sector when it noted:

“…. In September 2011, NBE issued a regulation that increased the minimum paid up capital required to establish a new bank from 75 million birr ($3.4 million) to 500 million birr ($22.6 million). As a result of this regulation, all banks under formation that didn’t meet all the necessary application requirements were either dissolved or diverted to other investments. The NBE …further increased the minimum paid up capital for banks to 2 Billion Birr ($90.4 million) and advised all the 18 currently operating private banks to increase their paid up capital to that amount by 2020.”

Expectedly, the policy hampered the operation of private banks and underscores GOE’s resolve to preserve its monopoly. Yet, foreign financial giants including Standard Bank Group, Kenya’s KCB Group, Citigroup, Commerzbank and Ecobank Transnational continues to show interest in the sector, substantiating its promising potentials.

Frankly, Ethiopia is doing well on the back of its anti-market policies, but it should not be lost in the euphoria while it can improve through free market measures. Many African economies including Nigeria (1970s), Tanzania (1960s) and Zimbabwe (1990s) experimented with similar anti-market policies but despite initial economic improvements –as it is in contemporary Ethiopia-, the absence of strong private sectors to absorb the shocks in dwindling revenue eventually busted their bubbles. If Ethiopia does not take advantage of its present gains to expand it economy, it might remain stagnant as the 12th poorest country in the world.

Published in AfricanLiberty.org on JUNE 12, 2017