

# **The Idea of Industrialization in Ethiopia: Fundamental Issues for Debate**

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Currently Ethiopia finds itself in an epoch-making process which I called structural transformation. In my previous short essay I tried to arouse an interest on this theme among academics, policy makers and ordinary readers. Continuing with the same interest, I would like to raise debate over the most notable feature of the structural transformation, namely on modeling industrialization strategy in Ethiopia.

Industrialization is a process of building up a country's capacity to convert raw materials into new products. It is accompanied by an increase in output and involves increasing complexity of production and demands greater reliance on others for certain activities. In the case of Ethiopia, while the awareness about the need for industrialization is traced back to the early 1960s, the design of comprehensive strategy with structural transformation in mind has come very late, with the 2004 declaration of the Ethiopian Industrial Development Strategy Document. “Though a favorable policy package to introduce and develop a modern economy was in place (during the imperial regime), there was not any deliberately drawn and explicitly specified industrial policy to accelerate industrialization in the country” (quoted in Admit, 2008). The 2004 document put in place an articulated industrial development strategy for the first time.

## **Debate (one) over Creation of Enabling Environment for Industrialization**

The document, among others, extensively discusses the basic enabling environments to speed up industrialization in Ethiopia: ensure macroeconomic stability, create a modern and development friendly financial sector, providing reliable infrastructure services (road,

railway, air transport, telecommunication, electric power and water supply services), carry out an effective manpower training, building efficient, transparent and accountable system of governance, and establishment of an efficient judiciary system. It is believed that without ensuring these enabling environments, the private sector cannot be the main driver of industrialization in Ethiopia. Both in the scientific literature and in the electronic media we see a number of debate and discussion regarding the enabling factors. Among the vast literature on the subject, I would like to mention the first and the second World Bank “Investment Climate Assessment” reports on Ethiopia (World Bank 2004; Ohashi, 2009). Both reports identified a set of issues that should be addressed jointly by the government and the private sector.

The discussion on the enabling factors is one of the conceptual areas advanced to explain the accumulation of capital and skill during the change in the productive structure. There are also other groups of concepts used to explain the model of industrialization (for detailed explanation of the hypothesis see Chenery, et al., 1986). What I find missing in the Ethiopian context are fundamental issues related to inward/outward orientation of the industrialization policy and the appropriateness of the organizational structure of industrialization. Policy orientation and organization forms affect the modeling and performance of industrialization in Ethiopia. The inward or outward orientation of the policy affects resource allocation in the manufacturing sector (for instance, is priority given to establishment of consumer goods industries or development of capital goods). Organizational structure affects the division of tasks and responsibilities between the federal government and regional states in undertaking industrialization in the country. For instance, the federal government can take the responsibility of establishing heavy industry (chemicals and metallurgy) while regional governments are assigned the task of establishing light industries (food processing and consumer goods).

## **Debate (two) over Industrial Policy Orientation**

What is the relevant industrialization policy orientation during the initial phase when there is a resource transform from agriculture to mix of industry-service sectors? Should the Ethiopian government follow an inward oriented industrialization policy like Latin America countries or outward oriented policy like East Asian countries? These two types of strategies are known by the name Import Substitution Industrialization and Export-oriented Industrialization respectively. The underlying goal of import substitution industrialization is to reduce a country's dependence on manufactured imports. This is achieved through complex of policy measures: giving protection of domestic industries, imposition of high import tariffs, restriction of import licensing, subsidizing import substituting industries and providing them cheap raw material and energy, providing them various tax benefits, overvaluing exchange rates, etc.

Export-oriented Industrialization policy uses measures that are opposite to Import Substitution Industrialization. It encourages exporting of goods which the country has a comparative advantages. For instance, the 2004 Industrialization Strategy stresses the meat, textile and leather processing sub-sectors which the government considers to have a comparative advantage and penetration of the international markets. Export-oriented Industrialization opens domestic market to foreign competition, reduces tariff barriers and devaluates national currency to encourage export.

Between 1958 and 1992, the governments of Ethiopia followed Import Substitution Industrialization policy. The three successive five year development plans (1958-1962, 1963-67 and 1969-74) of the imperial government emphasized private-led import substitution policy, while the Ten Year Perspective plan of the Derg Military Government adopted state-led import substitution industrialization. It seems to me that the case is different during the

period of EPRDF. From my readings of some documents I came to the conclusion that the EPRDF government seems to follow a neutral policy at first and since the early 2000s began to practice an Export-oriented Industrialization policy. This situation might have changed in the Growth and Transformation Plan (GTP) in which the public sector is given a leading role. I hope people from policy making institutions may enlighten us on the nature and negative/positive effects of this policy orientation in the allocation of investment in Ethiopia.

To raise a debate, I argue that Export-oriented Industrialization policy, if followed by EPRDF, is not relevant for current stage of industrial development in Ethiopia. I base my argument on Kaldor (1966) logic of cumulative causation during industrial evolution and my own study on effects of population pressure in Ethiopia. Kaldor (1966) laid out a four-stage model of industrial development. “The first stage is characterized by the emergence of a local consumer goods industry, which reduces dependence on imported consumer goods. The machinery and equipment needed to produce items of consumption are either produced in-house or imported. In the second stage domestic production of consumer goods provides the basis for net exports of these goods. The third stage (which may proceed simultaneously with the second) involves substitution of imported capital goods with locally made machinery and equipment. The fourth stage occurs when a country becomes a growing exporter of capital goods (heavy industries)”.

My observation is that Ethiopia is found currently at the first stage of the industrial evolution. In rural Ethiopia population growth has increased the number of subsistence households and their consumption and input requirements. It has also increased the volume and growth rate of labour force actively participating in rural labour market. Population pressure has created consumption and employment demand pressures in rural areas (see Tsegaye and Bo 2010). To create employment for the surplus rural labour and to supply the consumption requirements of the rural households it is necessary to establish consumer goods

industry. This means the country should replace manufactured products imported from other countries by products manufactured at home for reasons of balance of payment and sustained growth. There is a need for substantial protection of domestic manufacturing industries. In other words, at this stage the country should adopt Import Substitution Industrialization policy similar to Latin American countries.

### **Debate (three) on Appropriateness of Organizational Structure of Industrialization**

An appropriate organizational structure is a prerequisite of good management of industrialization. Enabling environmental factors (debate one) focus more on procedural reforms; they do not touch very much organizational structure, which is also a relevant element in the success of industrialization. An organizational structure refers to a pattern according to which industrialization tasks and responsibilities are formally allocated among the federal and regional governments. There are two approaches in the design of organizational structure: centralization or decentralization. Which is the appropriate structure in the current situation in Ethiopia?

Currently industrialization is administered centrally. Presumably, this type of administration is needed for the provision of uniform policy, to compensate lack of skill capability at lower levels, and to minimize corruption problems. In my previous postings I discussed the reasons for my preference for decentralized administration of industrialization (see references). I based my argument on two points. My first point refers to the growth and surplus of the rural labor and problems of creating employment. Since manufacturing industries have the capacity to absorb the surplus labor and provide productive employment owing to their growth character, I suggested for policy of rural industrialization and this is best achieved through decentralized administration of industrialization. My second point of argument for industrial decentralization is based on my observation of an increase in the

number of small and medium towns, spatial distribution of the urban population of Ethiopia and character of uneven and unbalanced growth of towns (see references).

## **Concluding Remarks**

To conclude, I am in favor of Import Substitution Industrialization policy and Industrial decentralization. My view is that these fundamental issues, which I think represent historical turning points, have not yet received the attention they deserve. Population growth and pressure have made the problem of industrialization in Ethiopia even more urgent. In the electronic mass media the problems of Ethiopia have become less economic and more political in nature. The discussion on fundamental changes in strategy of economic development has come to relate to the theory of political power. As I tried to discuss in this paper and in my previous postings if we are aware of the need for a relevant and appropriate development strategy we might reduce fragmentation along political lines. If we can unite sound economic policies with political feasibility we can change the character of the problem and such is the purpose of the essays.

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