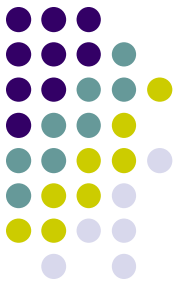


# Introducing Proactive FDI Policy in Ethiopia:

## Suggestions from an East Asian Perspective



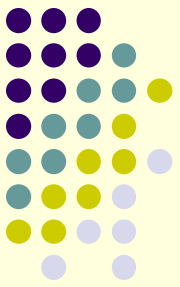
**Kenichi Ohno (GRIPS)**  
**Addis Ababa, January 16, 2013**



# Topics

1. Targeting light manufacturing FDI from Asia
2. Strategic FDI marketing
3. Improving investor support services
4. New Investment Law and EIA reform

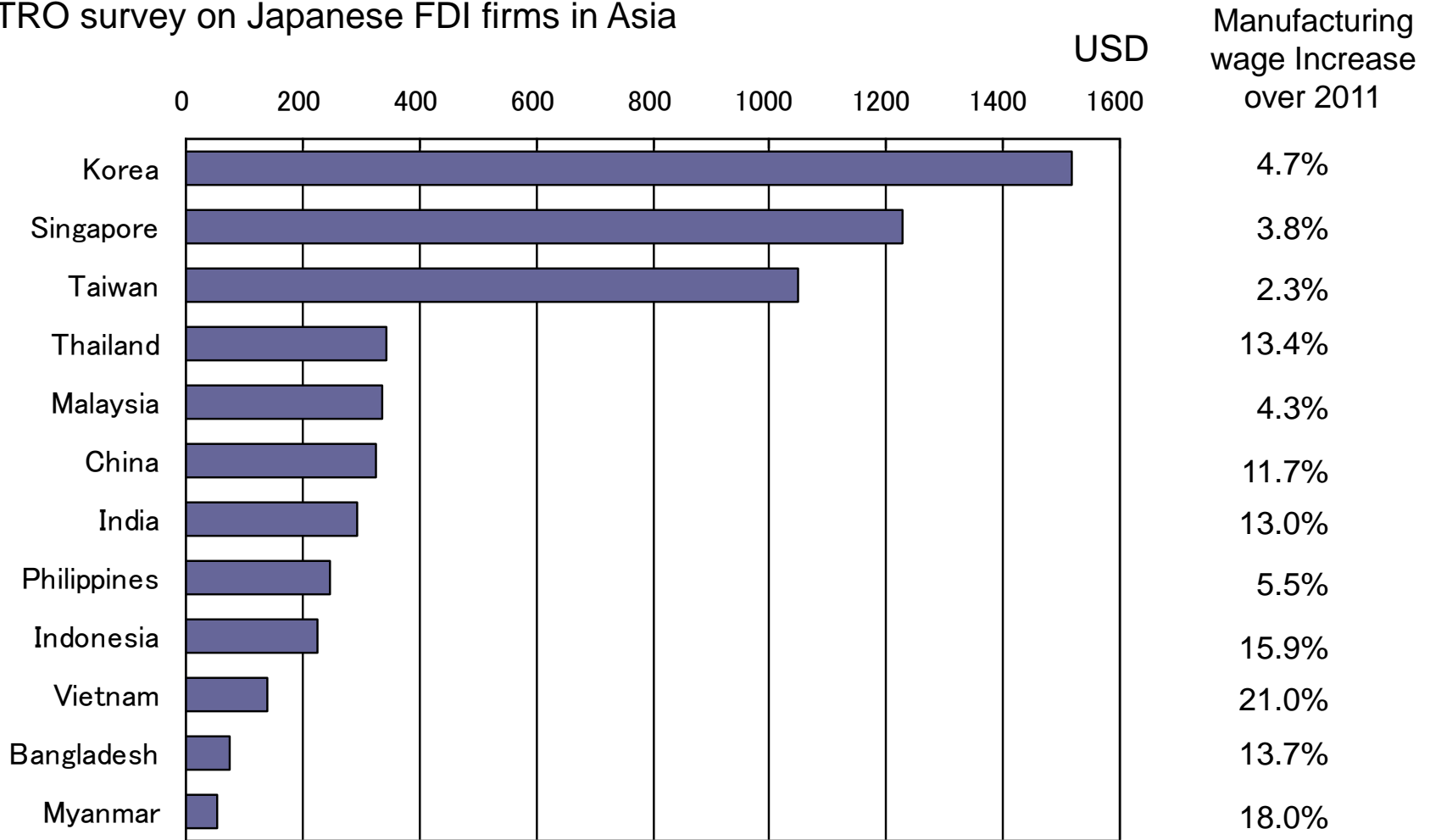
# 1. Targeting Light Manufacturing FDI from Asia (& Elsewhere)



- Many Asian countries face high or rising wages (Malaysia, Thailand, China, Vietnam...); they need to relocate labor-intensive production to other countries with lower cost.
  - Their main destinations are low-income Asia but Africa is also a potential destination.
  - Garment factories are moving to Bangladesh, Cambodia, Myanmar... Myanmar attracts attention as a new frontier.
  - Malaysia encourages outward FDI of labor-intensive manufacturing (“cross-border investment”).
  - Thailand wants to move out certain auto parts manufacturing.
- ➔ Receiving light manufacturing FDI from Asia can be one of the policy goals for Ethiopia. This will clearly define policy targets and necessary improvements and measures.

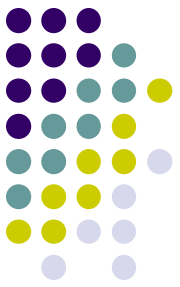
# Average Wages in Asian Countries, 2012

Monthly salary of full-time factory worker with three years of service  
JETRO survey on Japanese FDI firms in Asia



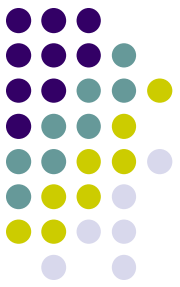
- Ten countries (not all shown) recorded wage increases of over 10% in 2012.
- 71% of firms responded that rising wages are a problem.
- Many countries adopt high wage policy to expand domestic demand.

# Ethiopia Receives Manufacturing FDI—But It Can Do More & Better



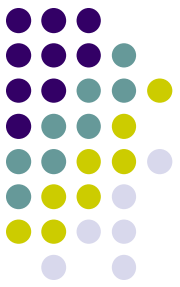
- Mozambique, Tanzania, Ghana, etc. with political stability, large ODA and coastal access receive little manufacturing FDI (unrelated to construction, energy, or extractive activities).
- Despite being poor and landlocked, Ethiopia attracts some garment & leather FDI from Turkey, China, India, etc.
  - Serious and active industrial policy (by African standard) since around 2002 with continuous learning and improvement
  - Aggressive approaches to individual FDI by Ethiopian government (PM, DPM, ministers, diplomatic missions)
  - Incentives, prioritized support, and high policy attention to target sectors and firms
- But this is not enough. Both investment climate and FDI strategy have much room for improvement. Ethiopia should build on past achievements to create a better FDI policy.

# Set Clear Goals and Concrete Action Plans



- Customs & trade regulations, tax rates & administration, and finance are major obstacles in Ethiopian business climate (WB survey on Chinese FDI, 2012).
- In addition to general improvement in business climate, FDI marketing should specify concrete target countries, sectors and even firms (this presupposes existence of an effective overall industrial strategy).
- Benchmark Asian countries which are sending out and/or receiving light manufacturing FDI, and identify necessary conditions & policy actions for absorbing it.
- Prepare concise but concrete action plans (cf. policy template used by the Vietnam-Japan industrialization initiative).
- Improve policy functions through international cooperation (cf. JICA assistance with the Zambia Development Agency).

# World Bank “Light Manufacturing in Africa” (2012)



- Produced by a team led by Hinh Dinh under the direction of former WB chief economist Justin Lin. Ethiopia is featured prominently, and Vietnam and China are compared.
- Ethiopia’s five manufacturing sectors—constraints are identified and recommendations are given (next slide).
- Labor productivity of Ethiopian garment is about the same as Vietnam and half of China. Ethiopia can expand light industry but only if it adopts good policies as in China or Vietnam [I feel Vietnam’s policy quality is grossly overestimated].
- General advice for Africa: (i) plug-and-play [investor-friendly] industrial parks; (ii) key input industries; (iii) trade logistics; (iv) assisting first movers; (v) entrepreneurial skills; (vi) vocational training; (vii) implementation issues.

# World Bank: Ethiopia's Light Manufacturing

**Table 1** Constraints in Ethiopia, by Importance, Size of Firm, and Sector

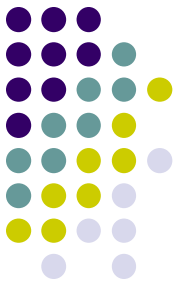
		Input industries	Land	Finance	Entrepreneurial skills	Worker skills	Trade logistics
Apparel	Smaller	Important	Critical	Critical	Important	Important	
	Large	Important			Important		Critical
Leather products	Smaller	Critical	Critical	Critical	Important		
	Large	Critical			Important		Important
Wood products	Smaller	Critical	Important	Important	Important	Important	
	Large	Critical	Important	Important	Important	Important	
Metal products	Smaller	Critical	Important	Important	Important	Important	
	Large	Critical	Important	Important	Important	Important	
Agribusiness	Smaller	Critical	Critical	Critical	Important		
	Large	Critical	Critical	Important			

Source: Authors.

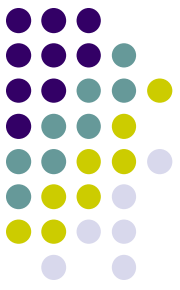
Note: Blank cells are not a priority.



# World Bank Survey: Chinese FDI in Ethiopia (Dec.2012)



- In Ethiopia, 372 Chinese investors are registered (May 2012); 86 in regular operation (Mar.2012); 69 responded to survey (45 manufacturing/13 construction/11 services).
- Manufacturing Chinese FDI covers food, garment, IT, machinery, non-metallic minerals, and “other” (largest).
- Total Chinese investment amounts to ETB7.5 (US\$450m); 15,910 full-time permanent jobs created; average monthly salary is ETB 1,445 (US\$85).
- Main FDI motives are informal Chinese network (friends), Ethiopian market attraction, low wage, incentives, and incentives from Chinese government.
- Major obstacles are customs clearance & trade procedure, currency convertibility & exchange rate, tax administration irregularities, finance, and lack of skilled workers.

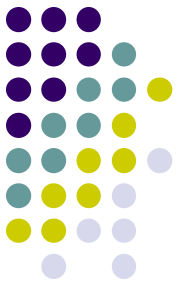


# Industrial Strategy Template

- **Situation analysis**—domestic, regional & Asian situation, etc.
- **Vision**—e.g. “Ethiopia is a preferred destination of labor-intensive manufacturing from Asia (and elsewhere)”
- **Targets**—quantitative & qualitative targets such as receiving garment & footwear from China, India, Turkey & Vietnam; even labor-intensive electronic assembly from Thailand & Malaysia, etc.
- **Policy issues**—e.g. (i) industrial parks; (ii) one-stop service; (iii) labor supply & quality; (iv) strategic FDI marketing, etc. (3 to 5 areas to be improved for achieving the above targets)
- **Action plan**—what, by whom, by when, performance criteria, monitoring mechanism

Note: The above format is being used in drafting action plans for the Vietnam-Japan Industrialization Strategy initiative.

# About FDI Source Countries



Each source country has different motives and characteristics.

FDI strategy must be customized to each target country (and even each sector):

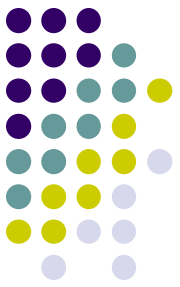
- Chinese—strong overseas network, commercial and short-term profit orientation, quick decision, very active in all sectors around the world, policy initiative & support for outward FDI.
- India—strength in some sectors (leather, garment, IT, auto parts...), active even in remote places, kaizen
- Korea—huge investment & risk-taking by chaebols (large business groups), official support & public promotion
- Japan—manufacturing oriented, slow decision but long-term commitment, assistance for local capacity building, observance of labor, social & environmental codes

# Characteristics of Japanese FDI

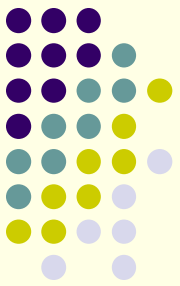


- Japan is never a first mover in new FDI frontier but comes in large number if the host country proves to be a good production base (Indonesia, Thailand, Malaysia, China, Vietnam, Cambodia, Myanmar...)
- Once agglomeration forms, late start is not really a big problem for Japanese FDI.
- Manufacturing oriented (incl. industrial services & logistics); not very active in trade, construction, real estate, banking, insurance, consultancy, etc. in comparison with China, Korea, Singapore, US, etc.
- Japanese firms often helps to improve local human & enterprise capabilities because strong “supporting industries” (upstream local production) enhance their competitiveness.
- Some countries appreciate long-term commitment and teaching of Japanese FDI (cf. Vietnam currently targets Japanese manufacturing SMEs instead of other nationalities).

# Characteristics of Japanese FDI (More)

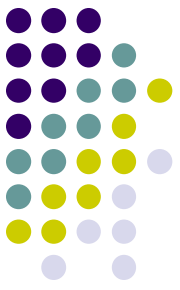


- China has attracted large amounts of Japanese manufacturing FDI but political risk and wage pressure are rising. Japanese firms want to diversify production locations (“China-plus-one”).
- Among Japanese manufacturing SMEs, most popular destinations are Thailand, Vietnam, and Indonesia. India and Myanmar also attract general attention but they are considered too difficult for SMEs to enter.
- At present, a large wave of Japanese manufacturing FDI is unlikely in Ethiopia (or Africa); but firms with specific objectives may be attracted.
  - Firms needing Ethiopia-specific inputs (high-quality leather & coffee, certain agro products, minerals and gems, etc.)
  - BOP businesses using Japanese technology
- Ethiopia can target Japanese FDI for quality, but it should also target other source countries for large volume.



## 2. Strategic FDI Marketing

- Improving general business climate is important, but it is only the first step toward effective FDI policy.
  - Publicizing priority sectors in the web may be useful, but that alone will not attract FDI in sufficient quality or quantity.
  - Additional effort should be made for more strategic marketing:
    - Identify target sectors and countries for FDI attraction
    - Identify even target companies
    - Approach target companies individually and negotiate special incentives if necessary; a large number of contacts and visits may be required to produce results
- (cf. Malaysia's Penang Island attracting semi-conductor giants; Mauritius attracting Hong Kong garment firms; Singapore attracting global aeronautic firms, etc.)



# Open vs. Targeted Approaches

- **Open approach**—offer good investment climate, set no priorities, and welcome all investors (except in sensitive areas such as defense) (Taiwan).
- **Targeted approach**—set concrete and narrow targets, then approach and negotiate FDI firms individually.
- **Two-track approach**—provide excellent investment climate for all but also adopt targeted marketing (Singapore).
- **Balanced learning**—improve investment climate generally, but also set priority areas and introduce measures to attract FDI in these areas (as part of policy learning); help of foreign experts may be needed to initiate targeted marketing.

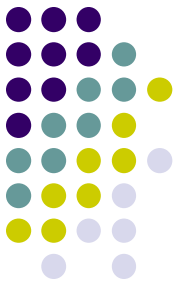
# Avoid General, Non-unique FDI Promotion



- Basic materials should be concise—investors are not very interested in general information.  
(eg. country profile; FDI data; list of industrial parks; incentives; priority sectors; general investment climate and policy measures...)
- Identify main concerns of targeted firms.  
(eg. parts-making Japanese SMEs need rental factories, one-stop service in Japanese language, assistance in finding new customers, recruitment of good engineer and professionals, good infrastructure services, etc.)
- Create and offer 3 or 4 compelling reasons to choose your location instead of rival countries/regions. These reasons must be unique and negotiable (respond to the requests of targeted firms).



# Vietnam: Ineffective Provincial FDI Competition



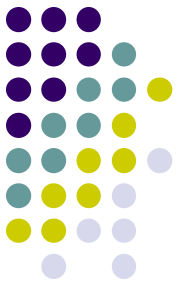
- Vietnam targets Japanese manufacturing SMEs. Many high-level missions are exchanged bilaterally at central and local levels.
- However, operational knowledge in FDI marketing and investor support is lacking. Vietnam cannot offer one-stop service without strong assistance from Japanese experts.
- Many provinces send investment missions to Japan but their presentations are too similar, too general and uninformative; each province must identify its own unique advantages and set specific target sectors & companies.
- GRIPS and Osaka/Kansai governments are jointly working to help break these operational barriers and link concerned officials and experts between Vietnam and Japan.

# The Case of Malaysia (MIDA)



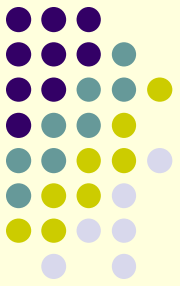
- Main investment incentives are *pioneer status* (corporate tax reduction) and *investment tax allowance*; import & sales tax exemption is also available for manufacturers; customized incentives are also possible.
- Licenses and incentives are centrally managed by MIDA with no distinction over nationalities. An effective one-stop service is offered. Greater incentives are given to remote regions.
- Provision of licenses & incentives are based on both published eligibility list and individual screening (no automatic approval). Applications are reviewed by MIDA's relevant divisions first, then sent to MIDA's weekly committee for final decision.
- Manufacturing (not disguised trading), value creation, technology and industrial linkage are key criteria for approval.

# Screening of FDI



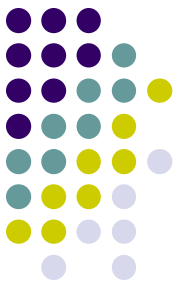
- Beware of investors with no industrial experience, disguised traders, and “license hunters” (obtaining license with no intention of investing).
- Some FDI firms violate labor, environmental or IPR laws.
- Proper screening of individual investors and project proposals should take at least one week per case.
- The case of Mozambique—all land is state-owned; land use rights can be rented out to investors at low cost according to official plan; however, if no investment is made as proposed within certain time limit the right will be revoked automatically with no compensation.

# 3. Improving Investor Support Services



- Many countries adopt “one-stop service” (“single-window”, “one-door”, etc.) but only in name. Ability to provide true one-stop service varies greatly across countries (Vietnam: “one door with many locks”).
- Ethiopia should learn to offer genuine “one-stop service.” Malaysia’s MIDA & Thai BOI are good models.
- Should industrial park developers be private or state-run? In many countries government sets policy and provides additional support but construction, marketing & park operation are mainly private responsibility.
- Every country is different. Work closely with the country people (eg. if you want to attract Japanese FDI, work with Japanese officials & hire Japanese experts; similarly for other countries).

# Taiwan's Export Processing Zones (EPZs): Key Success Factors



- A) **Right timing** (1960s: open & vibrant world economy)
- B) **Excellent location** (port, airport, freeway, metro)
- C) **Effective policy** (development strategy, land policy)
- D) **Perfect legal system** (clear and favorable law & policy)
- E) **Single contact window** (applications processed in 2 weeks)
- F) **Excellent investment environment** (infrastructure, tax breaks, power & water, life quality, service platform...)
- G) **Skilled workers**
- H) **Foreign technology transferred successfully**
- I) **Entry of high-quality tenant companies** with R&D capability, clean production, etc.

Source: EPZ Administration, Ministry of Economic Affairs, Taiwan.

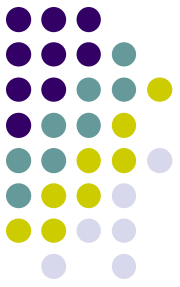
# Industrial Park Checklist (Vietnam)



- **Location**—port access, airport access, access to urban center, soil & topography
- **Hard infrastructure**—electricity, water, telecom, waste treatment, rental factories
- **Human resources**—workers, engineers, professionals
- **Soft infrastructure**—one-stop service, on-site customs clearance, on-site business services
- **Living conditions (for expats)**—housing, school for children, clinic & hospital, restaurants, recreation & sport, greenery
- **Incentives & costs**—incentives, land cost

Source: Vietnam Development Forum (March 2012).

# One-stop Service Requested by Osaka Manufacturing SMEs



## Pre-investment services

- Support for procedural documents (corporate registration, etc.)
- Introduction of factory builder and interior fitting companies
- Support for importing equipment & components

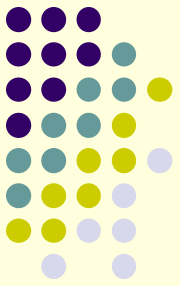
## Post-investment services

- Consultation for tax, accounting, labor matters
- Support for domestic procurement of parts & materials
- Support for marketing and finding new domestic customers
- Support for trade fair participation
- Support for recruiting local staff
- Information updates on legal and policy matters
- Support for exiting

**Japanese or Japanese-speaking staff with sufficient experience on duty, preferably 24 hrs/365 days**

Source: Questionnaire to industrial park operators in Vietnam prepared by GRIPS & Osaka Prefectural Government.

# 4. New Investment Law & Ethiopian Investment Agency Reform



- We are concerned about some features of policy change that seem to go against global competitive trends and offering welcoming attitude to investors:
  - Industrial zone developers shall be state-owned or JV between state & private firm.
  - Sectors permitted for FDI are now defined in a positive list instead of a negative list.
  - Minimum capital requirements are raised (eg. \$200,000 for 100% foreign owned FDI, which shuts out foreign SMEs)
- Creation of contact desks of relevant organizations within EIA is a good first physical step; however, establishment of true one-stop service will take much time and effort.
- Large-scale mining and agricultural FDI projects require more intensive preparation and examination than manufacturing or service FDI. One-stop service does not eliminate such needs.



# Remarks by HE Mr. Hailemariam

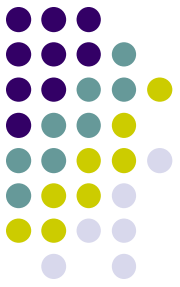
## (Jan.15, 2013)



- We are a beginner in the learning process; not sure if our FDI policy is on the right track. Free discussion and frank advice are welcome.
- Investment proclamation can be changed as needed. Any change will be for better for the majority of investors.
- Our priority is private IZ developers, but we have to adjust policy because we cannot wait forever: private (no result) → JV (unsuccessful) → state-owned IZ development
- Regarding minimum capital requirement, previously we wanted to reserve SME sector for local firms and invite only large FDI. But we now know that some foreign SMEs are creative. Foreign SMEs are welcome as long as they add value and transfer technology to Ethiopia.

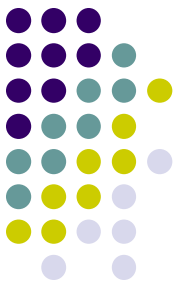
# Board of Investment, Thailand

(Thamrong Mahajchariyawong, Deputy Secretary General, March 2005)



- Our FDI policy is changing every five years (synchronized with five-year plans) but always for better. We have centralized general incentives and promotion. We do not have case-by-case treatment.
- Technical transfer measures are tricky because investors become angry if you regulate them too much. We implement only broad measures to encourage technical absorption. We just open up and let the market decide.
- The greatest attractiveness of Thailand is its welcoming attitude toward FDI. “Red carpet treatment” for investors should always be maintained in the future.

# References



- K. Ohno, *Learning to Industrialize: From Given Growth to Policy-aided Value Creation*, Routledge, 2012.
- Hinh T. Dinh, Vincent Palmade, Vandana Chandra, and Frances Cossar, *Light Manufacturing in Africa: Targeted Policies to Enhance Private Investment and Create Jobs*, World Bank Africa Development Forum, 2012.
- United Nations Conference on Trade and Development, *Creating Business Linkages: A Policy Perspective*, 2010.
- Small and Medium Enterprise Administration, *White Paper on Small and Medium Enterprises in Taiwan, 2010*.
- GRIPS and Osaka Prefectural Government, Questionnaire for Industrial Park Developers in Vietnam, 2012.
- Vietnam Development Forum, “Industrial Park Checklist,” compiled for policy discussion, 2012.
- Vietnam Industrialization Strategy Working Group, Industrial Action Plan Template (for the case of agricultural machinery), work in progress, 2012.