

## Ethiopia-Japan Industrial Policy Dialogue: Learning Eastern Methods through Intensive Discussion and Concrete Cooperation

Kenichi Ohno and Izumi Ohno

### 1. Introduction

With a per capita income of 856 US dollars as of 2019,<sup>1</sup> Ethiopia remains a low-income country with a weak private sector, imperfect policy, and poor business conditions. Nevertheless, it embraces high aspirations for national development, and has in the last two decades pursued a development strategy quite unique in Africa. Prime Minister Meles Zenawi (in power 1991-2012) in his later years and Prime Minister Hailemariam Desalegn (in power 2012-18) adopted a developmental state model that actively guided and selectively promoted private industrial activities. For this purpose, the Ethiopian government eagerly sought policy experiences and lessons from East Asia, while rejecting the neoliberal doctrine of the World Bank and the International Monetary Fund (IMF). Korea first and Japan later were consulted in formulating industrial strategies and concrete policy actions including *Kaizen* and export promotion. Meanwhile, rapid construction of power and transport infrastructure progressed, often with Chinese assistance as well as economic cooperation of other bilateral and multilateral partners. From around 2008, foreign investments in light manufacturing began to pour into Ethiopia, to which the government responded by building a large number of state-owned industrial parks as their receivers. As a result, Ethiopia has emerged as a dynamic latecomer economy featuring a development philosophy, policy effort, and growth performance which resemble those of East Asia's past and present latecomers rather than its African peers.

Despite these achievements, Ethiopia's economic transformation has been slow. Targeted and subsidized manufacturing subsectors such as

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<sup>1</sup> Gross national income (GNI) per capita, measured by the World Bank Atlas method (World Development Indicators database).

garment, leather, and food processing remain small and stagnant. The manufacturing sector remains small and its share of GDP fluctuates at 4-6 per cent. Active promotion of these key subsectors did not produce a visible increase in manufactured exports. Exports continue to be dominated by primary commodities such as coffee, sesame, oil seeds, chat, and gold. The overall export trend is flat, and the balance of payments is perpetually in huge deficit. These disappointing results are contrary to the experiences of high-performing economies in East Asia, where rapid rises in manufacturing output and export were attained. This lack of industrial performance constitutes a serious challenge for Ethiopia as it aims to reach lower middle income by 2025.

This chapter assesses the evolution of Ethiopia's policy learning from the East, considering both its positive and negative aspects, from the perspective of one of its policy dialogue partners, the National Graduate Institute for Policy Studies (GRIPS) Development Forum. The GRIPS Development Forum is a Tokyo-based research unit which has conducted Ethiopia-Japan industrial policy dialogue continuously and intensively since 2008 in close cooperation with the Japan International Cooperation Agency (JICA). Special attention is given to the seriousness of national leaders to learn from Japan and East Asia, and the approach taken by the Japanese side which was interactive, hands-on, and pragmatic.

The remainder of this chapter is organized as follows. Section 2 reviews the history of Ethiopia's industrial policy. Section 3 explains the features of Japan's policy dialogue with developing nations and the particular modality adopted in the Ethiopian case. Section 4 discusses how the policy agenda evolved from the first phase to the third phase of bilateral policy dialogue under the governments of Prime Minister Meles and Prime Minister Hailemariam. Section 5 considers the industrial cooperation of development partners in Ethiopia other than Japan. Section 6 deliberates on the policy style and economic prioritization of the current government of Abiy Ahmed. Section 7 describes the historical flying geese pattern of development in East Asia and implications for Ethiopia in the absence of such a regional network in Africa. Finally, in Section 8, remaining challenges to Ethiopia's industrialization are enumerated from the East Asian perspective.

## 2. History of Ethiopian Industrial Policy

Ethiopia's industrial policy has evolved dynamically in the last three decades as policy goals and economic landscape continually changed. Under the government of the Ethiopian People's Revolutionary Democratic Front (EPRDF) which came to power in 1991, the weight of policy attention shifted gradually from building a new nation to promoting economic development and transformation.

In 1991, when the oppressive Mengistu government was toppled by military force, the first task of the interim government was building a new nation amidst the social and economic damage caused by the previous regime. This included restoring peace and stability, creating a federal state, drafting a new constitution, resuscitating the suppressed private sector, and re-connecting with the outside world for aid and support. The Ethiopian-Eritrean War (1998-2000) and continuous food shortage also nagged Ethiopian leaders. But even in this early period, the government drafted in 1994 a document entitled 'An Economic Development Strategy for Ethiopia,' which proposed Agricultural Development Led Industrialization (ADLI) (FDRE 1994). This was a strategy to create active interaction between agriculture and industry, with the weight of the latter increasing over time. However, in reality, ADLI was not adopted as a key policy strategy in the first decade of the new government. Politics, war, hunger, and other urgent priorities superseded.

According to Prime Minister Meles, it was around 2002-03 that the Ethiopian government judged that the issues related to national survival were largely under control, and time had come to turn seriously to economic development. A series of strategic documents were drafted including the Ethiopian Industrial Development Strategy, the Urban Development Strategy, and the Rural Development Policies, Strategies and Instruments. Among these, the Ethiopian Industrial Development Strategy emphasized (i) the leading role of the private sector; (ii) ADLI, (iii) export orientation; (iv) prioritization of labor-intensive sectors; (v) balance between local and foreign direct investment (FDI) firms; (vi) strong state guidance; and (vii) all-nation mobilization (FDRE 2002).<sup>2</sup>

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<sup>2</sup> These were the seven policy pillars in the Ethiopian Industrial Development Strategy. In our bilateral policy dialogue, Prime Minister Meles confided that he personally 'had a hand' in drafting this and other documents.

Prime Minister Meles proved to be an avid learner and practitioner of industrial policy. From around 2003, Ethiopia began to learn about East Asia's developmental experiences. Learning was done through books and articles as well as by sending young officials to the Korea Development Institute (KDI) School in Seoul.<sup>3</sup> Taiwan was another model for Ethiopia but direct access was difficult. Prime Minister Meles himself often made speeches on development models, and participated in international conferences and research projects on industrial policy including the Democratic Developmental State in Africa project hosted by the Center for Policy Studies in Johannesburg, and the African Task Force of the Initiative for Policy Dialogue organized by Professor Joseph Stiglitz of Columbia University and supported by JICA. Prime Minister Meles generously spent his time with foreign researchers who helped to deepen his industrial knowledge. He read their books and papers, and exchanged letters and emails with them. Besides Joseph Stiglitz, his list of foreign advisors included Mushtaq Khan (University of London), Dani Rodrik (Harvard University), and the present authors of GRIPS, among others.

As a result of initial learning, the monthly National Export Steering Committee was established in 2003 and began to be used actively to monitor progress in export promotion (Oqubay 2015). This was a mechanism copied (in a modified form) from Korea in the late 1960s to the 1970s under President Park Chung-hee. Separately, support functions for specific sectors such as textile, leather, metals, and horticulture were established as directorates of the Ministry of Trade and Industry and other ministries, which were later upgraded to Institutes. These key sectors received considerable policy attention, budget allocation, and donor support.<sup>4</sup> Productivity tools that were not exclusively East Asian such as balanced score cards, business process re-engineering, benchmarking, and institutional twinning were also introduced, often with donor support.

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<sup>3</sup> Prime Minister Meles instructed officials dispatched to the KDI School to copy all materials provided and send to the Office of the Prime Minister for his perusal. However, Prime Minister Meles later acknowledged that Korea after the 1997-98 financial crisis no longer embraced the developmental state model which he wanted to study, and instead turned to neoclassical policy formulation (policy dialogue, October 14, 2008).

<sup>4</sup> Even before industrial policy dialogue with Japan began in 2008, the Netherlands was helping Ethiopia to foster floriculture, which grew to be a successful export industry (Oqubay 2015). The UNIDO and Italy assisted the drafting of *A Strategic Action Plan for the Development of the Ethiopian Leather and Leather Products Industry* in two volumes in 2005, which to Japanese experts was too detailed and plan-oriented. China supported the drafting of a master plan for the textile and garment sector. Neither of these documents was actually put into practice.

None of these, however, had a lasting impact on growth performance or industrial transformation.

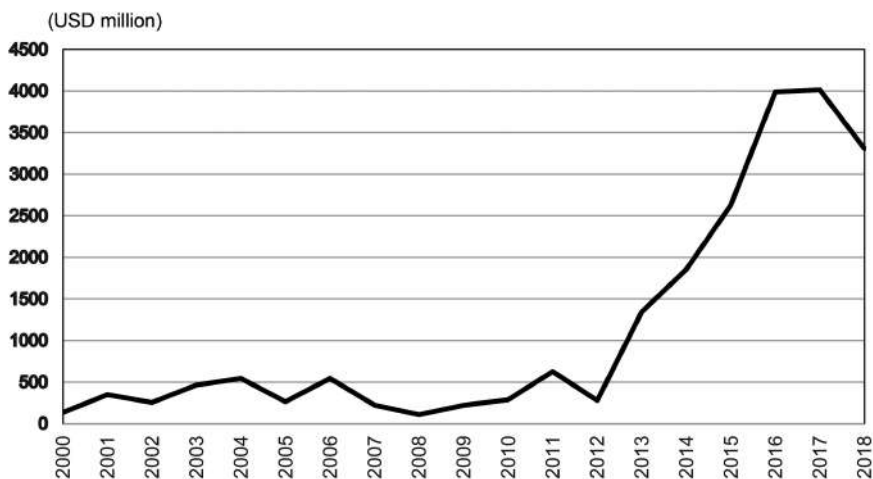
Although the idea of ADLI was mentioned in the first and second national development plans of the 1990s, it was the Sustainable Development and Poverty Reduction Program (SDPRP) 2002/03-2004/05 that tried to concretize the ADLI strategy by introducing agricultural extension services and staff training, farmer training, water harvesting and irrigation, marketing, peasant cooperatives, and micro finance. However, farm productivity failed to improve and output was heavily dependent on the amount of rainfall. Policy makers realized that targeting only smallholder farmers in rural areas was insufficient. In the subsequent Plan for Accelerated and Sustained Development to End Poverty (PASDEP) 2005/06-2009/10, the policy scope was considerably enlarged to cover industry, the urban sector, private sector development, and commercialization of large farms. Encouraging results were obtained in the first few years, but growth slowed down subsequently while inflation and foreign currency shortage worsened in the latter years of the PASDEP period. Even though overall growth remained relatively high, industrial and agricultural transformation did not happen.

In 2008, industrial policy dialogue with Japan was started and, in 2009, JICA began to cooperate in *Kaizen*, a Japanese method to improve workplace efficiency. At the same time, through Ethiopia's energetic top sales effort and investment promotion, labor-intensive manufacturing FDI began to arrive in Ethiopia from emerging economies. This investment wave was spearheaded by Turkey, India, and China, followed by investors from the United States (US), the European Union (EU), Taiwan, Korea, Indonesia, Sri Lanka, and Bangladesh. The arrival of Ayka, a large-scale integrated knitted apparel manufacturer from Turkey, in 2009 was the game-changer, prompting many other Turkish apparel firms to invest in Ethiopia.<sup>5</sup> Foreign manufacturers were attracted mainly by Ethiopia's low-cost labor, privileged access to EU and US markets, and the government's

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<sup>5</sup> It should be added that many of these Turkish apparel projects were bankrupted within a decade and are currently in the custody of the Development Bank of Ethiopia, their main lender. For Turkey, which faced rising wages at home, Ethiopia was the first major destination for external investment. The Ethiopian government offered generous policy loans to Turkish firms, the amounts of which were excessive relative to their business prospects. This led to over-investment and eventual loan default. Turkey was thus unable to become a 'flying goose' in Africa. Such collective failure did not occur in the case of Indian or Chinese investors.

industrial support and commitment even though the general investment climate remained far from satisfactory. Ethiopia thus emerged as one of the favored destinations for light manufacturing. FDI inflows to Ethiopia increased sharply during 2009-17 from 109 million US dollars to 4,017 million US dollars (Figure 8.1). But the volume of FDI inflows is still small compared with the massive and continued FDI inflow into East Asian economies.<sup>6</sup>



Source: Authors' compilation using the UNCTAD statistics. The Japanese policy dialogue team has been unable to construct a consistent FDI time-series from the national data even after many inquiries and interviews.

**Figure 8.1. FDI Inflows to Ethiopia**

To seize this historical opportunity, the government introduced a number of new policy initiatives. The country's investment proclamation and regulation were revised. FDI administration was centralized and strengthened at the Ethiopian Investment Commission (EIC), which was placed directly under the Prime Minister. Many government-owned industrial parks and their managing authority—the Industrial Park Development Corporation (IPDC)—were created, and zero liquid discharge technology and one-stop services for investors were adopted at these industrial parks. The state-run Hawassa Industrial Park has

<sup>6</sup> Ethiopia's FDI inflow is on the order of a few billion dollars per year (implementation basis) while FDI inflows into Southeast Asian nations such as Thailand, Indonesia, and Vietnam are on the order of tens of billions of dollars on approval basis, of which roughly half materializes in actual implementation.

become Ethiopia's flagship industrial estate whose successes and lessons are to be replicated in a dozen-or-so proposed state-run industrial parks (Oqubay 2015). Other parks for agro-processing and for small and medium enterprises (SMEs) are also under construction, and large national projects of an integrated steel mill and petrochemical complex are being contemplated. The quality and productivity of industrial workers have become critical issues. Meanwhile, the private construction boom continues and aggressive public investment programs have built hydraulic power plants, express ways, railroads, highways, and so forth, often with support of China and other donors.

Backed by these achievements, by around 2010 the main thrust of development planning shifted from poverty reduction to industrial catchup and transformation. The five-year plan document was renamed the Growth and Transformation Plan (GTP) 2010/11-2014/15 (FDRE 2010). In the following GTP II 2015/16-2019/20, a vision for 'becoming a leading nation in light manufacturing in Africa in particular and in manufacturing in general' was inserted (FDRE 2016). At the same time, heavy industries and import substitution sectors with large expected domestic demand would also be promoted. By now, Ethiopia's industrial policy issues have come to closely resemble those of FDI-led industrializing economies in Southeast Asia.

### **3. Systematic Learning from Japan and East Asia**

As explained in Chapter 1, since the 1980s Japan has been providing development policy support to a dozen partner countries. The objective and nature of development policy support range from policy advice on medium- and long-term development strategies to action-oriented emergency advice in response to economic crises, differing according to the prevailing situations within partner countries. Despite differences, this support often includes a component of policy dialogue with national leaders and key policymakers. Ethiopia-Japan industrial policy dialogue is a typical example where intensive bilateral dialogue has been conducted for more than ten years.

Here, we define policy dialogue as custom-made intellectual cooperation between a developing country and an advanced country, held regularly over a few to several years with an open, evolving, and action-oriented agenda for promoting the economic development of the former. It is a



flexible consultative mechanism Japan often employs in East Asia and elsewhere,<sup>7</sup> but Ethiopia is the first country in Africa where Japan has applied such a mechanism (Ohno and Ohno 2019). The coverage of policy support varies depending on the needs and requests from partner countries. While Ethiopia-Japan policy dialogue focuses on industrial development, the Okita Report in Argentina (Chapter 6) and the Ishikawa Project in Vietnam (Chapter 7) dealt with broader topics in economic development including the macroeconomy and agriculture.<sup>8</sup>

The Japanese development policy support in general and its policy dialogue in particular are deeply rooted in Japan's past experience as a latecomer nation as well as the history of its development cooperation (Ohno and Ohno 1998; Ohno 2013). Japan's policy dialogue is unique in several aspects. First, it aims to strengthen the state's role and policy capacity in industrialization rather than reduce the scope of government intervention. Second, there is no predetermined format or agenda. Policy consultation and knowledge sharing are tailor-made to each country through a highly interactive process. Policy dialogue usually starts with a national leader of a developing country requesting that Japan discuss developmental strategies generally or share and transfer particular experiences of East Asian development. This differs from standard technical assistance projects with narrowly and meticulously prescribed terms of reference. It is also unlike many seminars and study visits sponsored by advanced countries to show off their achievements as models. Third, Japan is willing to explain the experience of any country in the world, not just Japan's own experience, that fits the reality of the learning country, and even organizes visits to these countries. Japanese policies and institutions are often highly complex or too advanced to digest for beginner countries.

The term policy dialogue is not new in the international aid community, and many donors and international organizations claim to have been engaged in policy dialogues with developing countries. But 'traditional'

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<sup>7</sup> Japanese development policy support started with Argentina in 1985, using various modalities regarding theme, scale, participants, duration, and frequency (see Chapter 1: Overview). In countries such as Vietnam, Indonesia, Laos, and Myanmar, the Japanese government mobilized a large number of academics, businesses, and aid consultants to identify and analyze key issues and offer policy advice.

<sup>8</sup> The formal titles of the Okita Report and the Ishikawa Project are, respectively, *The Study on Economic Development of Argentine Republic (JICA 1987)* and *The Study on Economic Development Policy in the Transition toward a Market-Oriented Economy in Viet Nam (JICA 1996, 1998, 2001)*.



policy dialogues tend to cover topics that are less industrial and more focused on macroeconomic, legal, social, or governance issues. When industrial issues are taken up, they are usually cross-sectoral problems such as Information and Communication Technology (ICT), globalization, green growth, and enterprise reform rather than sector-specific targeting and promotion.<sup>9</sup> Korea, with its Knowledge Sharing Program (KSP), also offers large-scale policy cooperation to developing countries, but its topic coverage is broader and its approach is more schematized and standardized than Japan's (Ohno 2016).

As noted above, Ethiopia began to learn seriously from the East, especially Korea, around 2003. Subsequently, two events in 2008 caught the attention of Prime Minister Meles, who then decided to begin Ethiopia's learning from Japan.

In May 2008, Japan hosted the Fourth Tokyo International Conference on African Development (TICAD IV) in Yokohama, which forty African heads of state, including Prime Minister Meles, attended. This conference expanded the scope of Japanese cooperation in Africa from official support to private business partnership. Separately, on July 10-11, 2008, Professor Joseph Stiglitz of Columbia University organized the third Africa Task Force meeting of the Initiative for Policy Dialogue, which was financially supported by JICA, in Addis Ababa. Prime Minister Meles attended most sessions. The present authors explained the concept of Dynamic Capacity Development and the typical East Asian way of learning-by-doing (Ohno and Ohno 2012). The GRIPS team also offered to the prime minister an edited book on East Asian lessons for African growth.<sup>10</sup> In the following week, Prime Minister Meles officially requested to the Japanese government two-part bilateral industrial cooperation consisting of a quality and productivity (*Kaizen*) project, just as JICA provided in Tunisia, and regular policy discussion with GRIPS. Prime Minister Meles

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<sup>9</sup> One exception is Germany. Like the Japanese, Germans are interested in industrial cooperation although focal issues are not the same between the two. German cooperation usually highlights industrial TVET, engineering education, activation of business associations, and so on.

<sup>10</sup> The offered book was a collection of ten papers by economists and officials in Japan, the United Kingdom, Malaysia, and Uganda (GRIPS Development Forum 2008). Chapter 7 of this book compared how Japan and the EU approached the problem of quality and productivity in Tunisia, and explained how JICA implemented *Kaizen* in that country (Kikuchi 2008). This book was later re-issued commercially as Ohno and Ohno (2013) with additions and updates.

explained that TICAD IV and discussion with GRIPS researchers had convinced him that the time was ripe for direct intellectual exchange with Japan, the country that led the East Asian miracle (policy dialogue, October 14, 2008). In 2009, Japanese industrial cooperation with the two requested components was officially launched.

JICA's *Kaizen* cooperation in Ethiopia followed standard procedure and method offered to any other country (GRIPS Development Forum 2009; JICA and GRIPS Development Forum 2011a). *Kaizen* is a Japanese word for improvement, which means continuous improvement in quality and productivity with the participation of an entire company to establish a spontaneous and permanent process of eliminating *muda* (any thing or action that adds no value, often translated as waste). As of early 2021, both *Kaizen* and the industrial policy dialogue are in the third phase.

Regarding industrial policy dialogue, Ethiopian participants were many and multi-layered, including top leaders. On the Japanese side, GRIPS led the bilateral dialogue that was joined by Japanese ministries and agencies including the Ministry of Foreign Affairs, the Ministry of Economy, Trade and Industry (METI), the Japan External Trade Organization (JETRO), and JICA. Intensive policy dialogue at the high level was held four times a year, supplemented by a large number of research projects, additional mutual visits, exchange of policy letters, and research missions to third countries in Asia and Africa (GRIPS Development Forum 2016ab). Prime Minister Meles (from 2008 to 2012) and Prime Minister Hailemariam (from 2012 to 2017) participated in high-level discussions with zest and seriousness. Eighteen such sessions lasting one to two hours were arranged with them.<sup>11</sup> Separately, 19th High Level Forums with ministers, state ministers, officials, and experts were held regularly in Addis Ababa. Besides this, there were numerous visits to offices, factories, and project sites; discussions with international organizations and other bilateral donors; regional trips inside Ethiopia and Japan; and invited lectures at ministries and universities. Additionally, 19 policy research visits to third countries in Asia and Africa were organized (not counting mutual visits between Ethiopia and Japan).

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<sup>11</sup> There were eight face-to-face meetings with Prime Minister Meles Zenawi, and twelve such sessions with Prime Minister Hailemariam Desalegn, two of which were held when he was Deputy Prime Minister.

Table 8.1 illustrates the topics deliberated at High Level Forums from 2009 to 2017. These Forums were used not only to convey requested knowledge to Ethiopian policymakers but also to test and propose new policy areas that were missing but considered necessary in the context of Ethiopian policy evolution. Some topics were directly suggested by top leaders and senior policymakers such as Prime Ministers, Chief Economic Advisors to the Prime Minister, Ministers and/or State Ministers of Industry, while others emerged at the operational-level discussions. After each policy dialogue mission, both Japanese and Ethiopian sides exchanged views on topics for subsequent policy dialogues, particularly with Neway Gebreab who served as Chief Economic Advisor to the Prime Minister at the Prime Minister's Office and Minister and State Ministers of Industry. Especially, Neway chaired the High Level Forums during phases 1 and 2 and was deeply involved in agenda setting.<sup>12</sup> The JICA Ethiopia Office, in consultation with the Japanese Embassy in Ethiopia, has assumed a coordinating role in this process. Overall, this bilateral policy dialogue provided intellectual inputs to the formulation and implementation of the government's five-year development strategies such as PASDEP, GTP, and GTP II in the areas related to industrial development. Within a broad framework, flexibility was exercised to respond to evolving policy priorities of the Ethiopian government.

As is clear from this table, sharing of policy knowledge was mutual rather than unilateral from Japan to Ethiopia. Moreover, discussions were not confined to the experiences of Japan or countries that Japan assisted to develop. A large number of concrete cases were drawn from Asia and Africa, and industrial officials and experts from Malaysia, Thailand, and Vietnam were invited to present their practices and research.

Dialogue modality changed in 2018 with the inauguration of Prime Minister Abiy who had a different working style from the previous two prime ministers (Section 6). Small-group discussions have frequently been held with the members of the Macroeconomic Team that supported Prime Minister Abiy, and many policy workshops and meetings were organized on concrete issues such as productivity and the automotive and apparel

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<sup>12</sup> Neway Gebreab was Chief Economic advisor to Prime Ministers Meles and Hailemariam, and also served as Executive Director of the Ethiopia Development Research Institute (EDRI), which is now merged with another institute to become the Policy Studies Institute (PSI). He regularly chaired High Level Forums and was the main counterpart of the Ethiopia-Japan industrial policy dialogue.

sectors, instead of direct talks with the prime minister as in the previous years.

**Table 8.1. Topics Discussed at High Level Forums (Ministerial Level)**

	<b>Presentations by Japan or Third Country</b>	<b>Presentations by Ethiopian Government</b>
<b>&lt;PHASE 1&gt;</b> Session 1 June 2009	(1) JICA's plan for policy dialogue (2) ADLI and future directions for industrial development	(1) Evaluation of current PASDEP focusing on industrial development and related sectors
Session 2 Sep. 2009	(1) Cross-cutting issues on industrial policy & East Asian policy menu (2) Organizational arrangements for industrial policy formulation (3) SME policies in Japan	(1) Comments and feedback by the Policy Dialogue Steering Committee on Japanese presentations
Session 3 Nov. 2009	(1) Designing industrial master plans: international comparison (2) Industrial policy direction of Ethiopia: suggestions for PASDEP II	(1) Concept for the industrial chapter of PASDEP II and the formulation plan
Session 4 Mar. 2010	(1) Basic metals and engineering industries: international comparison of policy framework & Ethiopia's case	(1) Draft of industry sector for PASDEP II (2) Overview, contents of PASDEP II draft of chemical subsector
Session 5 July 2010	(1) Result of basic metal and engineering industries firm-level study – parts conducted by MPDC and JICA	(1) Report of <i>Kaizen</i> training in Osaka (2) Report of <i>Kaizen</i> training in Chubu (3) Current status of <i>Kaizen</i> project and institutionalization of <i>Kaizen</i>
Session 6 Oct. 2010	(1) Singapore's experience with productivity development: internalization, scaling-up, and international cooperation	(1) Contents of industry sector in GTP (2) Singapore's productivity movement and lessons learned
Session 7 Jan. 2011	(1) The making of high priority development strategies: international comparison	(1) Organizational structure of MOI and linkage with other ministries
Session 8 May 2011	(1) Ethiopia's industrialization under GTP (2) Achievements of <i>Kaizen</i> Project (3) <i>Kaizen</i> movement in Asia & Africa (4) Taiwan: policy drive for innovation	(1) MSE development strategy of Ethiopia (2) <i>Kaizen</i> dissemination plan (3) Botswana's productivity movement and its Implication for Ethiopia
<b>&lt;PHASE 2&gt;</b> Session 1 Jan. 2012	(1) Export orientation: 3 policy directions (2) Export promotion: JICA's experience (3) Export promotion center in Egypt	(1) Export promotion of Ethiopia (2) Assessing Ethiopian investment and export policies

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	<b>Presentations by Japan or Third Country</b>	<b>Presentations by Ethiopian Government</b>
Session 2 Aug. 2012	(1) Results of champion product seminar (2) Export promotion of Malaysia (3) Economic diplomacy in Thailand	(1) Performance of export promotion in Ethiopia (2) Export promotion by foreign mission
Session 3 Jan. 2013	(1) Proactive FDI policy (2) FDI policy experience of Malaysia (3) JICA's assistance in Zambia etc.	(1) FDI inflow into Ethiopia
Session 4 July 2013	(1) JICA's PSD assistance in Indonesia (2) FDI-linked technology transfer	(1) Malaysia's strategic FDI policy (2) Revision of Investment Proclamation
Session 5 Feb. 2014	(1) International comparison of manufacturing performance (2) Handholding programs	(1) Sectoral institutes: roles & performance (2) <i>Kaizen</i> in GTP II and long-term vision
Session 6 Aug. 2014	(1) FDI-led industrialization in East Asia (2) FDI inflow into latecomer Asia	(1) Proposal for key ideas in GTP II (2) Current status of Ethiopian FDI
Session 7 Jan. 2015	(1) Modality & key points of Japanese-run industrial zones in Vietnam & Thailand (2) Industrial zones & foreign currency issues in Myanmar & India	(1) Productivity & competitiveness chapter, industry chapter & <i>Kaizen</i> in GTP II
Session 8 Oct. 2015	(1) Remaining industrial issues ahead (2) Industrial zone experience in Cambodia	(1) Discussion on GTP II draft (2) Ethiopian wage & labor productivity survey
<INTERIM> July 2016	(1) Japan's alignment to Industrial objectives of GTP II	(1) Macro issues related to GTP II (2) Industrial Policy of GTP II (3) Hawassa Industrial Park
<PHASE 3> Session 1 Feb. 2017	(1) Japan's industrial cooperation for GTP II (2) Asian experience of high growth & income polarization/equalization	(1) Anti-export bias & effects of export incentives (2) Youth Revolving Fund (3) Impact of urban job application assistance
Session 2 Nov. 2017	(1) Productivity in Ethiopia & Sri Lanka (2) Productivity issues in Vietnam	(1) Productivity of garment & metal sectors (2) Mini review of productivity studies & data

Source: Prepared and updated by the authors based on JICA and GRIPS Development Forum (2016).

Prominent features of Ethiopia-Japan industrial policy dialogue are as follows. First, many of the proposed policy actions were actually adopted, either partially or fully, by the Ethiopian government. Second, from the beginning, Ethiopian leaders wanted Japan to be direct and frank rather than polite and diplomatic, and discussion has always been held in this spirit. Third, the Japanese side often stressed quality over speed in policy making, an idea which Ethiopians did not accept. This different stance over policy speed was never resolved, and we now accept this tension as given. Fourth, topics were selected carefully and interactively to cover the burning issues of the day rather than setting many topics in advance. Fifth, Japanese resources and concrete industrial projects were mobilized to realize some—but not all—of the proposals made during dialogue sessions, so talk actually led to action instead of remaining just talk (next section). This makes both parties more serious and committed to the policy dialogue. Sixth, past East Asian experiences have increasingly become pertinent to Ethiopia as it focuses on skills, productivity, value creation, and attracting high-quality manufacturing FDI. Seventh, Japanese policy support has been conducted within a broader network of private and public actors from Japan and other advanced or emerging economies because, unlike in Southeast Asia, Japan is a small player in Africa and cannot achieve its cooperation purposes by bilateral efforts alone.

An essential element of Ethiopia-Japan industrial policy dialogue is seriousness and eagerness of national leaders to learn from the experience and advice from East Asia. The learning proceeded under strong country ownership—not by uncritically emulating foreign practices or fulfilling externally imposed conditionalities—and was followed by practical actions to promote localization. It is under this context that Ethiopia-Japan industrial policy dialogue began and evolved. To support the Ethiopian efforts for local learning, the bilateral industrial policy dialogue has emphasized combining policy advice with concrete industrial cooperation, as will be explained in the next section.

#### **4. Evolution of Dialogue Agenda**

The Ethiopia-Japan industrial policy dialogue has covered many topics (see Table 8.1). At any time, more than one issue were discussed at the high, middle, and operational levels. As circumstances surrounding Ethiopia and the attention of policy makers shifted, topics also evolved from basic learning from each other to implementation of concrete policy

ideas and tools. New topics are suggested either by Ethiopian request or Japanese recommendation. As mentioned above, many policy proposals were followed up with concrete bilateral industrial projects including *Kaizen*.<sup>13</sup> One cannot expect all policy suggestions to be accepted, but many ideas raised in the policy dialogue were seriously considered by Ethiopian authorities and shaped their policies.

In the first phase of industrial policy dialogue (2009-11), both sides deepened knowledge about each other. Ethiopians explained existing policies such as ADLI and PASDEP while the Japanese side explained how East Asia and the rest of Africa designed and implemented policies and how they made necessary institutional arrangements for policy coordination. Mr. Newai, Chief Economic Advisor at the Prime Minister's Office, was deeply interested in practical aspects of the formulation of a master plan, to which the Japanese side responded by offering an international comparison of industrial master plans with close attention on the methods of drafting and stakeholder consultation during several sessions of the High Level Forum. Prime Minister Meles additionally requested detailed information on many industrial subjects he wanted to investigate, and they were compiled and sent to him.<sup>14</sup>

As Japanese *Kaizen* cooperation started simultaneously with policy dialogue, much time was spent on how it should be localized and expanded in Ethiopia (Box 8.1). Separately, in response to another Ethiopian request, Japan and Germany conducted a joint survey on the current status of the Ethiopian metal and engineering industries. Advice was also given on the preparation of the five-year development plan (GTP I). Many ideas were offered, including quality and productivity targets, but the final document contained none of these. This was questioned by the Japanese side, and Ethiopian leaders subsequently promised that this would not

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<sup>13</sup> Apart from *Kaizen*, implemented proposals include (i) metal and engineering industry survey; (ii) export promotion by creating champion products with national brands; (iii) business climate survey; (iv) technical assistance on investment promotion; (v) support in business development service (BDS); (vi) drafting of the Ethiopia Productivity Report; and (vii) automotive policy support.

<sup>14</sup> Information packages prepared for Prime Minister Meles included Japanese technical education, rural life improvement movements in East Asia, steel industry, chemical industry, international comparison of industrial policy methods, and how Japan and Korea absorbed technology through foreign-aided industrial projects. Additionally, two *Kaizen*-related documents were produced (GRIPS Development Forum 2009; JICA and GRIPS Development Forum 2011b).



happen again. In April 2013, Prime Minister Hailemariam requested that the GRIPS team assist in the formulation of the next five-year plan (GTP II).

The second phase of industrial policy dialogue (2012-15) began with a proposal to enhance export promotion. This was to be done through the creation of culture-laden, high-quality champion products with new branding (Ethiopian Highland Leather). JICA's champion product project was launched, and Ethiopian private firms enthusiastically welcomed the idea. Japan's intention was to broaden the scope of Ethiopian policy making. *Kaizen* had become popular by then but it only dealt with supply-side efficiency while demand-side attention, especially customer orientation, was missing. Another important theme was improving FDI policy because manufacturing FDI was accelerating into Ethiopia. International experiences and JICA's standard cooperation in this area were reported. In 2013, a large Ethiopian delegation, headed by a State Minister of Industry and including a person who was later appointed as the Commissioner of the Ethiopian Investment Commission, was dispatched to Malaysia to learn FDI and export promotion methods. In Addis Ababa, related issues such as one stop investor service, SME handholding support, and FDI-local firm linkage creation were also studied. The Japanese team also advised on the proposed content of GTP II as requested by Prime Minister Hailemariam. Unlike the previous plan, many recommendations actually made it to the final document including the light manufacturing vision, *Kaizen* philosophy and targets, and an extensive use of the phrase 'quality, productivity and competitiveness'<sup>15</sup> throughout GTP II. A paper summarizing remaining industrial policy issues, as seen from the Japanese side, was drafted at the end of the second phase (JICA and GRIPS Development Forum 2016).

The third phase starting in 2017 turned to productivity and the attraction of Japanese FDI as core issues. The important link between labor productivity and wages and related Asian experiences had already been discussed in the second phase. Additionally, Ethiopia's past productivity tools—*Kaizen*, benchmarking, and twinning—were critically assessed; the manufacturing census database was checked, cleaned, and

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<sup>15</sup> Even though 'quality, productivity and competitiveness' (QPC) were highlighted in GTP II, the government admitted that it was not sure what these exactly meant or what policies were needed to achieve them. Japan was asked by the Ministry of Industry to become a lead donor on QPC promotion.

re-formulated into a panel dataset; and an apparel sector survey was conducted in Bole Lemi, Hawassa, and Mekelle. These works led to the joint drafting of the Ethiopia Productivity Report by the Policy Studies Institute (PSI), a government think tank recently created by merging two existing institutions, and the GRIPS Development Forum in 2020. This was Ethiopia's first such report applying standard scientific analyses to Ethiopian productivity such as TFP and two decompositions of labor productivity growth, which identified both achievements and challenges. Enhanced involvement of Ethiopian researchers in industrial policy dialogue as well as productivity research was another feature in the third phase.

The policy dialogue team also assisted Japanese investors interested in Ethiopia by offering policy information, organizing workshops to interact with relevant Ethiopian officials, and providing the Ethiopian side with concrete policy advice to bring and retain Japanese and other investors. This work was intended to help investors already seriously interested in coming to Ethiopia, not to nudge firms still undecided about investment. The support is not triggered unless there is a specific Japanese firm wanting such official assistance, and so far there have been two such cases in the automotive and apparel sector.<sup>16</sup> By mutual learning and adjustment, it is hoped that Ethiopia will recognize and prepare conditions conducive to high-quality FDI, and Japanese investors in turn will have deeper understanding of Ethiopia's policy and build a fruitful relation with the host country.

As mentioned earlier, the combination of policy dialogue with concrete follow-up actions, often through JICA's industrial cooperation projects, has been a key feature of this bilateral industrial policy dialogue. Based on its own catch-up experience, Japan attaches high importance to 'learning

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<sup>16</sup> The Japanese dialogue team organized a seminar on international comparison of apparel sector development at the Ministry of Industry chaired by the State Minister and presented by Itochu, Japan's top apparel trading firm, in August 2018. This led to the signing of a memorandum of understanding among the Ethiopian Investment Commission (EIC), the Ethiopian Textile Industry Development Institute (ETIDI), Itochu, and the Japanese government in August 2019 to cooperate for the quality and productivity improvement of the Ethiopian textile and garment industry. Japanese experts were dispatched to garment factories in Ethiopia, which was partly supported by the Japanese Ministry of Economy, Trade and Industry (METI). Itochu's motive was to secure a new apparel supply base to the Japanese market while contributing to the development of the host country (Ohno and Uesu 2020).

by doing' with concrete targets through a trial-and-error process. High Level Forums and other policy discussions were used to share policy knowledge from Asia, as well as to deliberate on actual problems that arose from implementing foreign methods in the Ethiopian context. This approach contributed to linking researchers with policymakers in achieving concrete results on the ground.

Thus, by the third phase, Ethiopia-Japan industrial policy dialogue grew to cover wide policy areas combining talk with official cooperation projects and business actions of Japanese firms. JICA now provides an array of industrial cooperation projects in Ethiopia including advanced *Kaizen*, industrial park management, investment promotion, export promotion, business development service (BDS), start-up business competition, and support for Japanese SMEs interested in Ethiopia. For the Japanese government, this is the broadest industrial cooperation menu in Africa, which is similar to typical Japanese industrial cooperation in latecomer economies in Southeast Asia. Time is ripe for Japan to re-arrange these many project components into an integrated whole with clear objectives, internal linkage, and alignment with Ethiopia's development plan.

Additional remarks on *Kaizen* are warranted. Japanese industrial cooperation in Ethiopia began with *Kaizen*, and policy dialogue initially discussed various practical aspects of *Kaizen* (Box 8.1). But as experience and knowledge accumulated, day-to-day management and troubleshooting were delegated first to JICA experts, then to the Ethiopian *Kaizen* Institute (EKI). Ethiopians can now not only manage their own *Kaizen* activities but also teach *Kaizen* to other Africans bilaterally and through the New Partnership for Africa's Development (NEPAD), which is a great achievement. Even so, policy concern on *Kaizen* of both Prime Minister Meles and Prime Minister Hailemariam remained considerable, and *Kaizen* was deliberated at almost each dialogue session with Prime Minister Hailemariam.

Among many issues, the most crucial was how *Kaizen* should be transformed from a superficial tool to be abandoned quickly to a deeply ingrained national spirit and philosophy so it would forever be practiced willingly and without external coercion or official instruction. Prime Minister Meles emphasized in the policy dialogue that *Kaizen* was not just a one-time breakthrough but an incremental societal movement involving all stakeholders including rural communities (Ohno 2018,

19). Similar views were expressed by Prime Minister Hailemariam who argued that *Kaizen* was a philosophy for societal transformation and not limited to the economic sphere (Ohno 2018, 20). Foreign techniques may be adopted formally and superficially but its underlying spirit is harder to learn. This we call the mindset problem. A national productivity movement recommended by Japan is a partial answer to this. Introduction of the Kaizen Month was one proposal accepted by Prime Minister Hailemariam, and September was designated as Ethiopia's *Kaizen* Month when *Kaizen*-related awards and events are organized (unlike in Japan or Singapore where November is the Productivity Month). A city-wide *Kaizen* movement, launched by Ethiopian initiative in 2016, is another important drive. But more needs to be done to solidify *Kaizen* in the minds of all Ethiopians.

**Box 8.1. *Kaizen*: Combining Policy Dialogue with Concrete Industrial Cooperation**

The combination of policy dialogue (talk) and JICA-supported concrete projects (action) has been a key feature of Japan-Ethiopia industrial policy dialogue with the intention to support 'learning by doing' through a hands-on approach. One example is linking JICA's *Kaizen* projects with policy discussion. In introducing and institutionalizing *Kaizen* in Ethiopia, in the first phase, there was close interaction among Ethiopian policymakers and practitioners, and the Japanese policy dialogue team and *Kaizen* consultants, as follows (Ohno 2018).

1) Understanding *Kaizen* in the Ethiopian context

In the initial stage of introducing *Kaizen*, basic information was provided to both Ethiopian policymakers and practitioners on the history of quality and productivity improvement in Japan, together with examples of JICA projects in other developing countries. This was done in various forms including information kits for Prime Minister Meles; open seminars inviting policymakers, practitioners, the private sector, etc.; a study tour to Singapore; and publication of reports and pamphlets. Because the Ethiopian government had already introduced other productivity tools such as benchmarking and business process re-engineering (BPR), active discussions took place on how *Kaizen* differed from these western instruments, and to what extent they were substitutes or complements. A question

was also raised whether *Kaizen* was applicable to Ethiopia, which had a different culture from Japan. The Japanese team explained that *Kaizen* had been successful in many societies with very different cultures from Japan's such as India and Latin America. To respond to these questions, the GRIPS Development Forum produced a booklet *Introducing KAIZEN in Africa* (GRIPS Development Forum 2009).

2) Sharing progress and bringing issues to policy attention:

The industrial policy dialogue provided opportunities for both Ethiopian and Japanese sides to examine JICA *Kaizen* projects from a policy perspective. Initially, the High Level Forum discussed the progress of *Kaizen* implementation in pilot companies and the results of counterpart training in Osaka and Chubu, Japan to which members of the *Kaizen* Unit and pilot companies were dispatched. Subsequently, the High Level Forum deliberated on a plan to institutionalize the government's *Kaizen* support as presented by Mr. Getahun Tadesse, then head of the *Kaizen* Unit of the Ministry of Trade and Industry who later was appointed as the first Director General of the Ethiopia *Kaizen* Institute. Implementation problems were discussed including the lack of incentives and a high attrition rate of Ethiopian *Kaizen* consultants as well as factory workers where *Kaizen* was introduced. In response, the government took remedial measures such as increases in *Kaizen* budget and salaries and benefits of *Kaizen* consultants, opportunities for advanced training, and academic degrees for *Kaizen* instructors.

3) Sharing international experiences of *Kaizen* institutionalization

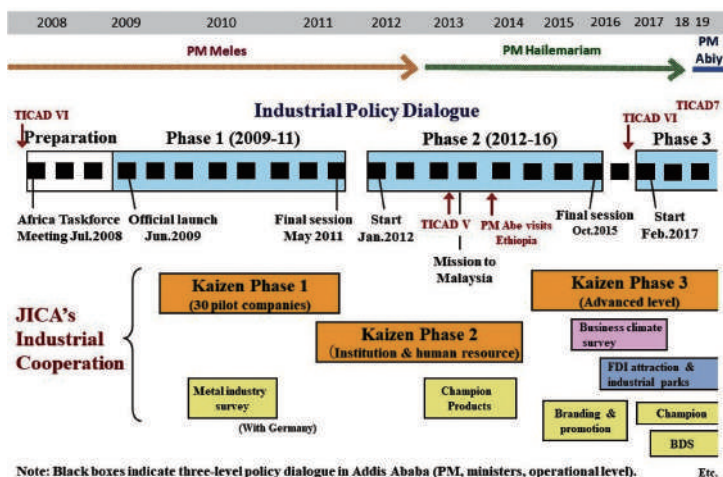
At High Level Forums and on other occasions, the Japanese team presented concrete cases of national productivity movements in various countries and diverse options for *Kaizen* promotion bodies. Ethiopian officials showed great interest in the Singaporean experience, where a government-led productivity movement was carried out in the 1980s under the strong leadership of Prime Minister Lee Kuan Yew. The Singaporean model was emulated, with local modifications, in establishing the Ethiopia *Kaizen* Institute in 2011.<sup>17</sup> The Japanese side compiled a study on *Kaizen* national movements

<sup>17</sup> For details, see also Volume II of this research project, *Promoting Quality and Productivity Improvement/Kaizen in Africa* (Jin and Ohno 2022). This report includes case studies of Singapore (Chapter 2) and Ethiopia (Chapters 3 and 4).

(JICA and GRIPS Development Forum 2011b) which contained information from Japan, Burkina Faso, and Botswana in addition to Singapore. Prime Minister Meles was greatly concerned about the weak private response to his industrial policy and sought ideas from Asia. The Japanese team recommended upgrading ongoing *Kaizen* efforts to a comprehensive national movement to transform the mindset of people and foster private sector dynamism.

Many international cases were studied as possible policy components, policy discussions were often followed up by concrete actions, and operational issues were brought up from the ground level to high policy attention. All this constituted practical hands-on support for policy learning. In the subsequent phases of industrial policy dialogue, a similar approach was taken in such areas as export promotion (creation of national brands and champion products), FDI promotion (industrial park management), and enterprise diagnosis and management consultancy (Business Development Services).

### Ethiopia-Japan Industrial Policy Dialogue and Industrial Cooperation



## 5. Development Partnerships for Industrial Cooperation

It is important to note that only a few donors in Ethiopia prioritized industrial promotion as of 2008 when Japan began to prepare the industrial

policy dialogue and *Kaizen* project. They were the United Nations Industrial Development Organization (UNIDO), the United States Agency for International Development (USAID), Italy, and Germany. This was partly because the focus of the global aid community was poverty reduction and governance at that time, but also because there were contested views among donors about the role of government in private sector development and the extent of donor engagement in industrial policy discussion with the host government. Some donors contended that support should focus on improving the business climate generally while others wanted to do more to develop certain sectors with high growth potential. During the first phase of industrial policy dialogue, the Japanese team met three times with a group of donors interested in private sector development (PSD) and also had numerous bilateral exchanges with individual donors, to explain that the purpose of Japan's industrial support in Ethiopia was to enhance the government's policy capability in supporting private sector development (JICA and GRIPS Development Forum 2011).<sup>18</sup>

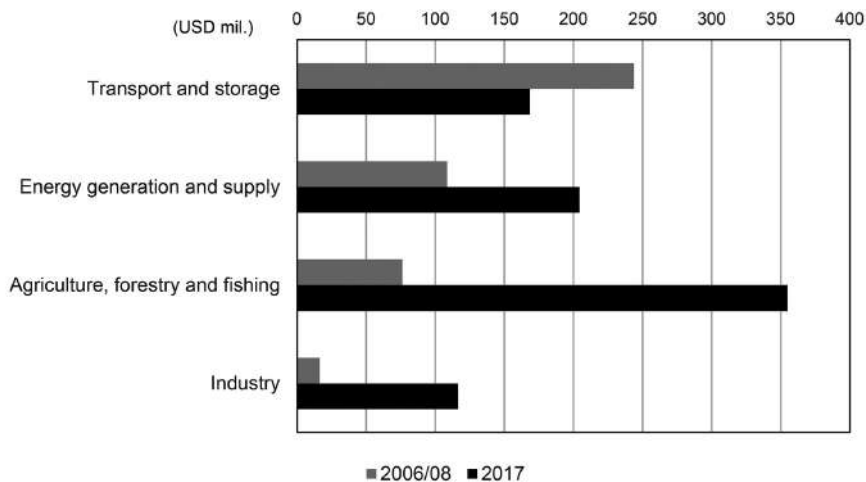
Around 2010, there was a shift in global business trends which prodded development partners toward more active support for industrialization. Ethiopian development plans, GTP I and II, also stressed the need for industrial growth and economic transformation. This was a major departure from the previous plans (such as SDPRP and PASDEP) which primarily aimed at poverty reduction, and development partners came to recognize the need to re-align their cooperation to the priorities shown in GTP I and II. For these reasons, an increasing number of donors joined the support for industrial development, including the United Kingdom (UK), the EU, and Sweden. Development partners that had hitherto approached industrial promotion cautiously, such as the World Bank, greatly expanded the scope of their industrial support. Trade-related ODA to Ethiopia doubled between 2006-08 and 2017. Moreover, as Figure 8.2 illustrates, the composition of trade-related ODA to Ethiopia changed significantly during the same period toward industry, agriculture, and energy.

It is important to recognize that Ethiopia is learning from many nations, not only from Japan or East Asia. Officials, businesses, and

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<sup>18</sup> Two donor meetings were organized by the JICA Ethiopia Office (September 2009 and May 2011) and one meeting was organized by the Japanese Embassy in Ethiopia (July 2010).





Source: Ohno and Uesu (2020) (calculation based on Aid for Trade database, OECD-WTO).

**Figure 8.2. Major Components of Trade-related ODA to Ethiopia (disbursement basis)**

experts from the West and emerging economies are also mobilized to Ethiopian learning. Germany can teach vocational training and business associations, Italy teaches leather and fashion, France brought wine to the Rift Valley, the Netherlands has assisted with floriculture, the USAID can help Ethiopians to reach the American market, and the UK and the EU have relatively large budgets for industry-related projects and research. India helps Ethiopia's sectoral institutes such as leather, textile, and metals and engineering through a twinning arrangement, while Sri Lankan apparel experts know how to achieve quality and ethical standards simultaneously. International organizations also support Ethiopia in the areas of their expertise. The World Bank, which previously promoted private sector capacity building through a matching fund, now offers a broader range of support to Ethiopia including state-owned enterprise (SOE) reforms, industrial parks, women entrepreneurs, and job creation for refugees (in cooperation with the UK and the EU). The International Labor Organization (ILO) is actively engaged in projects related to Decent Work in partnership with European donors and FDI firms. The UNIDO has designated Ethiopia as a model partner country for inclusive and sustainable industrial development.

Three things can be said about this situation. First, while virtually all bilateral donors now engage in industrial support unlike in years past,

most newcomers have little concrete knowledge of industrial sectors on the ground and rely heavily on NPOs, businesses, and matching funds for project implementation. This is not the case with JICA or German Corporation for International Cooperation (GIZ) which have extensive hands-on industrial promotion experience around the globe. Second, as exemplified by *Kaizen*, Japanese industrial advice is often unique and different as it stresses (some say excessively) quality, productivity, and on-time delivery while European buyers and donors are more worried about labor and environmental conditions at factories than perfect stitching and packaging of the product. This partly reflects the nature of Western and Japanese markets where the former emphasizes strict compliance with social and environmental standards. Such features are evident in the recently expanding development partnerships for sustainable apparel and textile global value chains in Ethiopia (see Ohno and Uesu 2020 for the details). Ethiopia needs to understand this dual requirement by foreign buyers, and hopefully learn both. Third, industrial strategies in East Asia are not one; policies across countries and over time in the region have both commonalities and differences. Japan does not represent all of East Asia, and it only practices and teaches models derived from its own history and social structure. Even so, the Japanese catch-up model should be enlightening to all latecomers as it was the first non-Western model to succeed in full-scale industrialization and has also been applied to many other countries. Furthermore, over the past 60 years of ODA and industrial cooperation, Japan has built extensive human and organizational networks with Asian partners. By partnering with advanced East Asian economies that were aid recipients in the recent past, Japan can offer intellectual support and engage actively in policy dialogue with latecomer Asian countries as well as developing countries in Africa.

## **6. Development Policy of Prime Minister Abiy Ahmed<sup>19</sup>**

Since 2015, Ethiopia faced increasingly violent anti-government protests which forced the government to declare a state of emergency. Prime Minister Hailemariam announced his resignation in February 2018 and was succeeded by Abiy Ahmed in April 2018. Soon after assuming power, Prime Minister Abiy surprised the nation by making peace with Eritrea, for which he received the Nobel Peace Prize, and starting to reform state monopolies through privatization and/or increased competition.

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<sup>19</sup> This section was written based on the information upto October 2020.

He also urged national unity, talked with dissent groups, and released political prisoners. However, domestic unrest did not subside even under his leadership and culminated in a military confrontation in Tigray. Externally, Prime Minister Abiy enhanced diplomatic and economic relations with neighboring countries, the Middle East, the West, international organizations, and Ethiopian diaspora. Tree planting and beautifying Addis Ababa were also initiated by the current government. In 2020, Ethiopian Airlines was mobilized to deliver medical supplies from China to COVID-19 affected African countries.

Meanwhile, the development strategy of the Abiy administration was slower to emerge. This was partly due to mounting issues in domestic politics and partly due to his working style. Unlike the two previous prime ministers, and more like other heads of state, Prime Minister Abiy does not directly manage economic policies himself, but delegates them to the Macroeconomic Team, a group of selected officials from the Office of the Prime Minister and various economic ministries and agencies. Their ideas and proposals are submitted to him for deliberation and approval.

This is not to say that his government has not initiated any economic actions. On the contrary, it has already launched bold state monopoly reform mentioned above, with technical and financial backing of the World Bank and a few bilateral donors. The World Bank and the International Finance Corporation (IFC) also assist Ethiopia to improve its Ease of Doing Business ranking. Another problem that the government is tackling is the severe and chronic shortage of foreign currency. Ethiopia negotiated with China for debt relief and requested other donors for financial support. The above-mentioned World Bank program also contributes to narrow Ethiopia's payments gap.<sup>20</sup> Ethiopia also agreed with the IMF on a three-year program of 2.9 billion US dollars. Besides these, Ethiopia seriously resumed accession negotiation with the World Trade Organization. However, these are macroeconomic or structural policies that affect all sectors, not targeted promotion of key real-sector activities.

In the spring of 2019, Prime Minister Abiy and his Macroeconomic Team drafted a one-page policy matrix entitled 'A New Horizon of Hope.' This

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<sup>20</sup> To be fair, all these efforts regarding SOE reform, World Bank ranking, and debt relief were started by Prime Minister Hailemariam. Prime Minister Abiy inherited them with vigor and activism.

was followed by a longer document, Homegrown Economic Reform Agenda (HERA), in September 2019. The content of the latter only partly overlaps with the former. HERA defines actions that must be executed in the next three years (2020-22), preparing the way for the Ten Year Perspective Plan (to be finalized in 2021) and the Five Year Development Plan (to be prepared subsequently). After reviewing the current situation of Ethiopia,<sup>21</sup> HERA presents three policy pillars (which are called ‘reforms’) consisting of macroeconomic stability, structural reforms, and sector-specific promotion. According to a senior advisor to the prime minister, macroeconomic stability means implementing the IMF and World Bank programs to overcome economic challenges at hand. Structural reforms mean breaking state monopolies in telecom, power, logistics, etc. through competition or privatization. Sector-specific promotion means productivity enhancement in five targeted sectors: agriculture, manufacturing, mining, tourism, and ICT. The senior advisor noted that the first two had already been initiated in the first year of the Abiy government, but productivity enhancement was a long-term objective that must be continued into the Ten Year Perspective Plan. He added that this was an area that required additional international knowledge and technical support (interview at the Office of the Prime Minister, February 21, 2020).

The three policy pillars of HERA are highly standard and should be regarded as an appropriate policy framework. The key question is not the framework itself but what concrete ingredients will go into these pillars and whether they will be implemented effectively to produce results. Among the three pillars, macroeconomic stability is a common goal for all nations and its success depends very much on the technical competence of fiscal and monetary authorities. SOE reforms are also greatly needed in Ethiopia, provided that they will be handled in a proper manner and speed. Both are already being assisted by the IMF and the World Bank. By contrast, as the senior advisor admits, how to promote real-sector activities—desirability, feasibility, and proper method of promotion—has been a subject of long, heated global debate since the late 1980s.

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<sup>21</sup> The situation analysis of HERA touches on past achievements such as high growth and poverty reduction, then turns to the remaining problems. They include growth heavily dependent on public investment, excessive expansion of construction and services, performance indicators much lower than the average of lower middle-income countries, lack of industrial transformation (especially weak manufacturing), many impediments to productivity increase, inflation, external debt, and crowding-out of private investment.

On the one hand, there is the Washington Consensus that views liberalization, privatization, global integration, and a good business climate as crucial preconditions for growth, and opposes targeted industrial promotion because governments are generally regarded as technically incompetent and prone to political pressure (Krueger 1997). On the other hand, there is the typical East Asian approach that combines private dynamism and official intervention to promote selected sectors, orchestrated by a wise or learning government. According to this view, the speed of economic liberalization must be decided by how fast domestic competitiveness improves. The first regards government as a fair and detached referee of an economic football match while the latter expects it to be a passionate and competent coach for star players.

Prime Minister Meles rejected the Washington Consensus and embraced the Eastern way (Zenawi 2012), and Japanese industrial cooperation assisted his policy learning. One problem with his approach was that the priority sectors such as garment, leather, food processing, etc. did not emerge strongly despite much official support they received. Another problem was that Prime Minister Meles not only denied immediate economic liberalization but also refused to even set a long-term liberalization schedule. Ethiopia does not need a big-bang liberalization now, but it should have a plan to deregulate, privatize, and globally integrate its economy in proper pace and steps in a way consistent with the rise of its industrial competitiveness.

The framework of HERA, as currently presented, is general enough to harbor various approaches in industrial promotion. It also has the potential of generating a strategy more balanced than the Washington Consensus or the Meles way, by merging selective industrial promotion with the steady liberalization of the domestic economy under a government that engages in serious policy learning. At this moment, how the Ethiopian government will proceed is not clear as the targeted five sectors are very broad and still without implementation details. Moreover, political and ethnic stability is imperative in executing economic strategies. Things should become clearer as concrete policy measures in the Ten Year Perspective Plan begin

to be introduced.<sup>22</sup>

## 7. Ethiopia and East Asia's Flying Geese

East Asia is unique because it has attained economic development through the very existence of the East Asian region as a powerful arena for policy learning, business cooperation, and fierce competition among its member countries, and not by the effort of each country alone. One by one, countries in different development stages accelerated growth by participating in the dynamic production network created by the region's multinational corporations. Linked by trade, investment, and human exchange, and assisted by economic integration and cooperation, a regional division of labor with clear order and structure emerged. Industrialization proceeded through geographic diffusion on the one hand and structural deepening within each country on the other. This multifaceted supply-side phenomenon is called the flying geese pattern of economic development, by which East Asia has become the factory of the world. No other developing region has attained a similar collective growth mechanism.

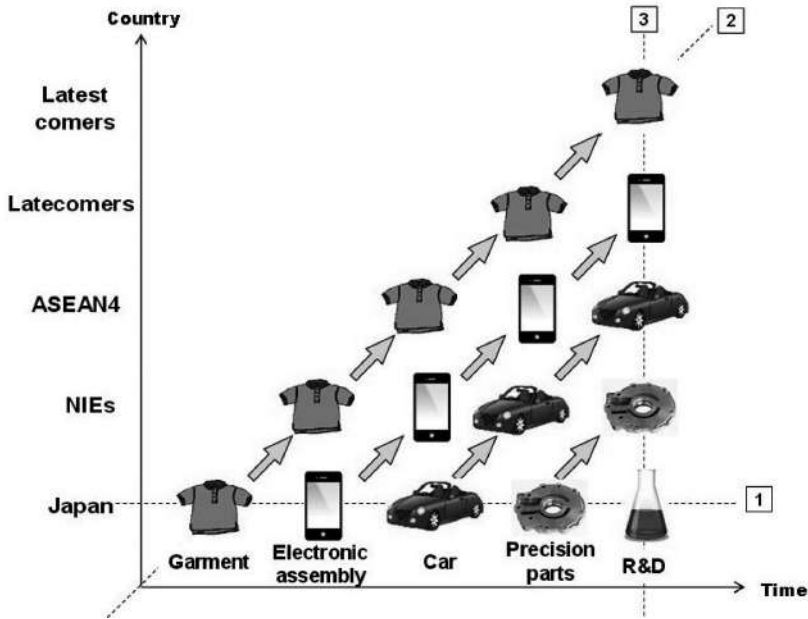
For any economy in East Asia, development means jumping into this regional network and becoming one crucial link in it, receiving competitive pressure as well as models and cooperation from others, and upgrading industrial capabilities along the technological ladder. Over time, industries have been passed from advanced countries to less advanced ones through FDI, so all latecomers crave to absorb as much manufacturing FDI as possible.

Figure 8.3 illustrates industry passing within East Asia's flying geese formation. If we fix a country (say, Japan), we can observe the transition of main activities along the time axis (direction 1). If we fix a product (say, garment), we can diagonally trace shifting production sites across countries (direction 2). If we fix a time (say, now), geographic distribution of activities within East Asia can be explained (direction 3). While

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<sup>22</sup> According to sources close to the prime minister, Abiy will inherit the development strategy of Prime Ministers Meles and Hailemariam but details must be adjusted as situations change. He remarked that he could not adopt the approach of the past two prime ministers in directly managing economic issues and talking to producers and investors. He also stated to the Parliament that the automotive industry was an important sector for promotion.

reality is a little more complex than this, this picture can give an initial approximation on how regional industrialization has proceeded with order and structure in East Asia.



Source: Prepared by the authors based on JICA and GRIPS Development Forum (2016).

**Figure 8.3. Structural Transformation in East Asia**

As mentioned earlier, Ethiopia began to attract light manufacturing FDI from emerging economies starting around 2008. Rising wages in source countries exert pressure to find alternative locations for labor-intensive production, and Ethiopia was chosen as one of them. Ethiopia receives investments not only from East Asia but also from India, Turkey, EU, US, Middle East, and so on. This can be interpreted as Ethiopia becoming the latest member of the (enlarged) flying geese pattern. Although neither Ethiopia nor source countries are physically confined to East Asia, the mechanism of industry passing via technology upgrading and wage pressure, clear order and structure, and FDI as the means of geographical diffusion are basically the same as the original East Asian model. Thus, Ethiopia has entered an era in which the past and current growth experiences of East Asia—both successes to emulate and failures to avoid—are highly relevant to its policy formulation. There is no other country in Africa to which this statement more aptly applies.



## 8. Remaining Challenges

Apart from political and macroeconomic stability, which are prerequisite for growth, there are four challenges Ethiopia must face to preserve and accelerate its growth momentum. These challenges were identified during our bilateral industrial policy dialogue over a decade.

First, Ethiopia began development from a very low level socially and economically. Despite recent high growth, Ethiopia is still a low-income country on a long journey to full industrialization. The private sector is weak, and industrial policy is unsophisticated by the East Asian standard even with the serious learning by national leaders. Many common weaknesses of countries in an early stage of development are visible, including the lack of labor skill and discipline, low productivity, and stagnant output and trivial export of manufactured products. The business climate is unfavorable, ranking 159th among 190 economies in the World Bank Doing Business ranking in 2020. National aspiration for economic development is high but current achievement is limited. This hard fact must be acknowledged, and policy must be drafted in a pragmatic way to overcome this reality. Leapfrogging to the technology frontline is difficult unless human resource and institutional foundations are first laid.

Second, there is a continuous need to strengthen the capacity of technocrats who are charged with putting policy ideas into practice. Policy is often made hastily at a high level without deep consideration of the detailed design or suitability to Ethiopian reality. Speed is stressed over quality. Top leaders are dedicated to national development and extremely busy. But, unlike successful East Asian economies which had a cadre of technocrats to support national leaders, there is only a thin layer of middle managers in the ministries, which prevents effective policy formulation and implementation in Ethiopia. In high-performing East Asian governments, policy decisions are made interactively in both top-down and bottom-up directions. A vision is handed down from the top, then details are researched and filled by competent mid-level officials. Ministers are briefed on the essence of proposed policy and approve the final document. A thick layer of professional and politically insulated technocrats contributed greatly to high growth in such countries as Japan, Singapore, Korea, and Taiwan (World Bank 1993; Campos and Root 1996). In Ethiopia, where such interactive decision making is absent, all substantive work must be done by the minister or state ministers. This

situation is surely not unique to Ethiopia; many developing countries face the problem of weak bureaucratic machinery. Ethiopia needs a bold administrative reform that boosts the capacity of bureaucrats significantly while reducing their number.

Third, Ethiopia's industrial growth is taking place in Africa where conditions are quite different from East Asia. The principal difference is the absence of the regional flying geese pattern with a leading nation generating structured layers of follower nations as explained above. Africa generally lacks sufficiently strong intra-regional trade, FDI, technology, and aid linkage among its member countries.<sup>23</sup> The relatively low income and small market size of Africa compared to Asia is another negative factor, which directs most exports to the EU or US markets using trade access privileges such as the Everything But Arms (EBA) and the African Growth and Opportunity Act (AGOA). This implies that Ethiopia must industrialize as a solitary bird, openly facing the pressure and competition of the global economy without intra-regional cover, linkage, or learning models. This calls for adjustments in adopting East Asian lessons, especially regarding the formation of foreign partnership in global marketing and knowledge transfer.

Finally, the same thing can be said in a brighter tone. Africa's different situation may offer new opportunities Ethiopia can capture as deepening globalization changes the path and style of economic development. Due to technological progress and reduced transport and communication costs, production processes are increasingly fragmented over many countries. Global value chains are formed and re-formed by multinational corporations which allocate research and development (R&D), design, materials, components, assembly, marketing, and branding functions in different countries for optimal sourcing (Bernhardt 2013). Under such circumstances, the absence of African flying geese may no longer be a serious disadvantage for Ethiopia because it can directly participate in global value chains by becoming one crucial chain in the area

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<sup>23</sup> The launching of the African Continental Free Trade Area (AfCFTA) in 2019 was a good start, but it will take much time to make this framework truly work to overcome the recognized problems. The Association of South-East Asian Nations (ASEAN), established in 1967, is regarded as a successful regional economic mechanism, but it took a few decades for ASEAN to begin a formal process of regional economic integration, and another few decades to implement proposed integration and facilitation actions, even in the strong presence of the flying geese pattern.

where the country excels (AfDB, OECD, and UNDP 2014). Yet, facing global competition alone is an enormous challenge for any latecomer. Government, enterprise, and citizen capabilities must be upgraded to global standards. This is a tall order in comparison with the world where latecomers can learn and prepare in steps within the region before jumping into the global scene. Geography and distance have become less critical than in the previous centuries, but whether they have become irrelevant for economic development is an open question.

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