FDI Center

IAIP INVESTMENT PROMOTION AND MOBILIZATION STRATEGIES – INCENTIVES

Phase 2 – final report

Report prepared by FDI Center for UNIDO

JULY 30, 2021

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LIST OF ABBREVIATIONS

Abbreviation	Meaning
AIIB	Amhara Industry and Investment Bureau
CAGR	Compound Annual Growth Rate
EIC	Ethiopian Investment Commission
EU	European Union
FAO	Food and Agriculture Organization of the United Nations
FDI	Foreign Direct Investment
GiZ	German Corporation for International Cooperation
GoE	Government of Ethiopia
IAIP	Integrated Agro-Industrial Park
IFC	International Finance Corporation
ILO	International Labour Organization
IPA	Investment Promotion Agency
MoA	Ministry of Agriculture
MoTI	Ministry of Trade and Industry
OECD	Organisation for Economic Co-operation and Development

Abbreviation	Meaning
RIC	Regional Investment Commission
RIPDC	Regional Industrial Parks Development Corporation
RTC	Rural Transformation Center
SME	Small and Medium-sized Enterprises
SNNPR	Southern Nationals Nationalities and Peoples Region
TBD	To be determined
UNIDO	United Nations Industrial Development Organization

1. INTRODUCTION

INTRODUCTION

This is the final report on incentives, which is part of phase 2 of the project to support UNIDO and the Government of Ethiopia with the development of an investment promotion and mobilization strategy for three pilot integrated agro-industrial parks (IAIP) (i.e., Yirgalem IAIP, Bulbula IAIP, and Bure IAIP). This report has been discussed and endorsed by UNIDO and all relevant regional and national stakeholders during the virtual validation workshop “Pilot-IAIP investment promotion strategy validation workshop” held on July 15, 2021.

Incentives can play a key role on influencing investors’ location decisions and are hence an important part of a successful investment attraction strategy. The Ministry of Trade and Industry and the Ministry of Agriculture and Rural Development conducted a report on incentives for the agro-industry in 2009. The EIC is currently reviewing its own incentives package.

The first section of this report presents the methodology used for this study. Section 3 introduces a framework for thinking about different types of incentives. Section 4 covers examples of agro-business oriented incentive programs of other regions around the world. Section 5 of the report reviews the current incentive package available to domestic and foreign investors. Section 6 and 7 identify suitable incentives based on the needs of the identified target groups and compares this with the existing framework to identify current limitations. Section 8 recommends modifications and additional incentive measures tailored towards the identified target groups of agro-industrial investors. Section 9 offers advice for negotiating with an investor on incentives.

The research and analysis for this report were conducted in June and July 2021. A list of all the sources used for the analysis is provided in the annex.

2. METHODOLOGY

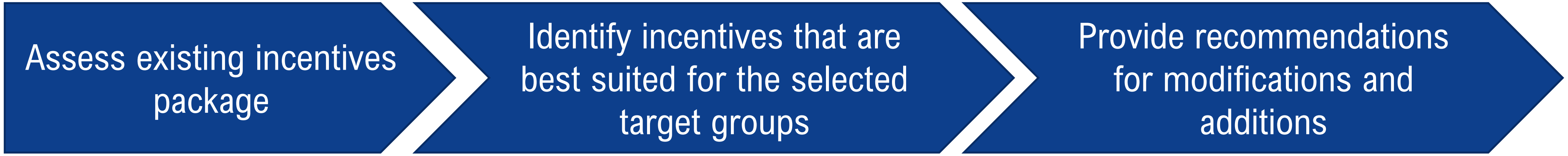
METHODOLOGY

Overview

Our approach for this report is divided into three main segments:

- Assessment of the existing incentives package.
- Identification of incentives that are best suited for the selected target groups in phase 1 of this project.
- Recommendations for modifications of existing incentives and addition of new incentives.

The following pages lay out our view on the key success factors of an incentive package and provide more details on the methodology underlying these three steps.



METHODOLOGY

Key success factors for successful incentives programs

Government financial support has always played an important role in corporate location and economic development. Commonly referred to as government incentives, the practice of providing public financial support to investors continues to be a prominent feature of the investment attraction landscape in most parts of the world. Incentives are often a controversial topic and there is an ongoing debate about how necessary and effective they are.

Despite this debate, it is clear that incentives can play a significant role in stimulating a location's economic development. There are many examples of countries and regions that have used incentives successfully to attract investment and strengthen their economies. Besides the obvious financial value, incentives can also be beneficial to companies by enabling or facilitating investment projects that may otherwise not have been possible. The careful use of incentives can serve as a powerful economic development tool, promoting growth in targeted areas and strengthening the ties between governments and corporate investors.

Based on our experience working with corporate investors and government investment promotion agencies worldwide, we believe that the most successful incentive programs share certain characteristics.

- The incentives are **attractive** to corporate investors, meaning that they provide a true benefit that reflects the investor's specific needs.
- The incentives are **targeted** towards specific sectors or types of investment that the location is trying to attract, rather than identical for all companies.
- As the name implies, the incentives have an **incentivizing** effect, meaning that they lead to an incremental outcome, rather than simply providing a benefit to an investment that would have happened anyway.
- The incentives are **realistic**, meaning that the location is actually able to provide them in a reliable manner without creating unnecessary risks.
- The process of awarding incentives is **transparent**, based on well-defined and objective guidelines that are clear to both companies and stakeholders.
- The process for granting incentives is **efficient** and not unnecessarily bureaucratic, despite the need for careful evaluation and rules.
- The incentives are **beneficial** to the location itself, providing a clear and quantifiable economic return on the use of government funds.

With these principles in mind, we reviewed the existing incentive packages, identified limitations, and provide suggestions on additional incentives packages that will support the involved agencies to attract investors to the IAIPs.

METHODOLOGY

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Review of existing incentive packages

We start out by reviewing the existing incentive framework. This is essential to ensure that the project moves in the right direction without overlooking critical factors.

In order to identify potential limitations and required modifications we were guided in our review by the following questions:

- What does the existing Incentive Framework include? How was this developed and how much of it should be retained?
- What other incentives programs currently exist in Ethiopia? Will these continue to exist?
- What is the legal framework for developing new incentives? Will new legislation be required?
- What types of incentives are generally within the scope (e.g., tax exemptions, cash grants, equity participation, workforce training)? Are certain types of incentives preferred or excluded?
- Should the incentives be 'as-of-right' (i.e., available to all investors that meet certain requirements) or 'discretionary' (i.e., provided only in some cases at the discretion of the agencies and its stakeholders)?
- To what degree should the incentives be based on additionality (i.e., attracting companies that would not otherwise have invested in Ethiopia)?
- What is the maximum available budget for the incentives and the source of these funds? For how long will funding be available?
- How many types of incentives should the new framework include? Is the aim to have a single program or a range of different benefits to offer investors depending on their needs?
- Should the incentives only focus on attracting new investment or should expansions of existing investors be eligible too?
- Will the incentives be available to investments throughout Ethiopia or only in the dedicated IAIPs?
- What is the status of the new IAIPs, RTCs, and RIPIDCs? Will these organizations have a dedicated incentives department?
- What other stakeholders or strategic partners should be involved and consulted in the development of the new incentives?

METHODOLOGY

Identification of suitable incentives & recommendations

In the broadest terms, most companies have the same requirements and benefit from incentives in the same way. However, different companies have very diverse operational and financial needs depending on the sector, the situation of the company, and the type of activity that is being planned.

For example, companies in sectors where profit margins are very high will place a high value on corporate income tax incentives whereas these are less important for projects that will not generate profits for several years. In some capital-intensive projects, investors may be more interested in sales tax reductions for equipment and machinery. Projects with high upfront capital expenditures may be more interested in cash grants whereas highly technical projects can benefit from support with transportation infrastructure or utilities. Given the global shortage of talent across different sectors, companies are increasingly also interested in government support with recruiting and training qualified workers. In the United States, where incentives are arguably more sophisticated than in other parts of the world, there is definitely a shift towards workforce-related incentives, and these have been instrumental in winning several large projects recently (e.g., Amazon’s “HQ2” project in Virginia).

In order to identify suitable incentives for investors in the target groups we were guided in our analysis by the following questions:

- What are the key requirements of the priority target groups defined in phase 1?
- To what degree are these requirements shared across target groups?
- What types of incentives are likely to provide the greatest value to each target group?
- To what degree should the incentives be tailored to the needs of each group?
- Should the incentive programs be mutually exclusive, or can companies apply for more than one program?

Based on the information obtained, we developed specific recommendations on the incentives packages that can be provided to investors in the defined target groups. The incentives are described in detail in section 8. It may be necessary for a legal firm in Ethiopia to ensure that the incentives are in line with and reflect Ethiopian law.

3. INCENTIVES FRAMEWORK

INCENTIVES FRAMEWORK

Overview

Investment incentives are benefits provided to companies that are planning new investments or expansions. They are generally available to both local and foreign investors, although often targeted at achieving policy objectives. The majority of incentives are front-end grants (meaning they are provided at the beginning of an investment project) and tax incentives. Incentives can be categorized into two main groups: financial (“hard”) or non-financial incentives (“soft”). There are also many types of “non-traditional” incentives being experimented with, especially in the US (e.g., access to renewable energy, support with attracting talent, university partnerships). Soft and non-traditional incentives are increasingly important for inward investors as they directly address their key operational needs and allow locations to differentiate themselves.

Some examples of incentives:

Hard incentives	Soft incentives
• Cash grants, generally for capital investment, job creation, or R&D. • Tax exemptions and other fiscal incentives, including in SEZs. • Training and labor market financial assistance. • Provision of loan guarantees, cheap loans, and equity finance. • Exemptions from regulations such as licenses or FX restrictions.	• One-stop-shop services (e.g., building permits, working permits, visas). • Site-visits. • Property assistance, including site and infrastructure provision. • Recruitment and immigration services. • Consulting services. • Support making incentives/funding applications. • Property searches. • Market intelligence. • Supplier and real estate databases. • Partnering/matchmaking services (sometimes including M&A). • Introduction to networks and multipliers. • Aftercare / BRE services.

INCENTIVES FRAMEWORK

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Objectives of an incentive programs

Why should a government offer incentives? Which goals can be achieved with it? Some of the most common objectives of incentive programs include:

- Mitigating existing constrains
- Overcoming a competitive weakness vis-a-vis competing locations
- Promoting FDI towards underdeveloped parts of the country
- Attracting target industries in line with the national industrial policy
- Changing the international image of a country towards “being open for business”

In all cases, it is important to compare the costs and benefits of offering an incentive package.

INCENTIVES FRAMEWORK

Characteristics of effective incentive programs

Effective incentive programs share common characteristics, including typically the following aspects:

- Reflect economic development priorities (e.g., promoting specific economic objectives, sectors, regions, or types of activities).
- Solid legal basis.
- Well-defined eligibility criteria and guidelines, including strategic (e.g., target sectors, potential for linkages, and technology transfer) and quality criteria (e.g., wage-level of jobs, type of business activity).
- Efficient application and approval process.
- Transparent and reliable decision-making.
- Structured disbursement and monitoring process.
- Clear (and reasonable) claw-back provisions.
- Ongoing impact and cost-benefit analysis.

INCENTIVES FRAMEWORK

The role of incentives in attracting investment

Incentives are playing the following roles in attracting investment:

- Companies are conditioned to expect incentives.
- Many large corporations have incentives specialists.
- Most projects would go ahead without incentives.
- Cases where incentives are required:
  - Large projects that may not otherwise be feasible (e.g., battery pack assembly facilities, large pharmaceutical factories, semiconductor foundries).
  - New and unproven technology or processes (e.g., hydrogen plants, passenger drone facilities).
- Incentives should not play a role in location decisions for most projects. However, incentives play a relevant role in many cases when selecting a new location.

INCENTIVES FRAMEWORK

Incentives during the location decision process

Incentives during the location decision process

Initial planning

- Incentives are typically one of the criteria used by companies to develop a longlist.
- The availability of incentives is assessed at a very high level to screen locations.

Location analysis

- Other (operational) factors are typically more important while companies are in the process of evaluating incentives.
- Information on the approximate value of incentives is included in the evaluation (usually as part of an overall cost analysis).

Final decision

- Incentives can play a decisive role in deciding between finalist locations and sites.
- Companies usually require a preliminary incentives offer and detailed information on terms and conditions.

INCENTIVES FRAMEWORK

The investor perspective on incentives

In order to develop a successful incentive package, we need to understand the perspective of investors towards incentives. These are the aspects of incentives that companies typically value:

- “Cash-is-king”.
- Tax incentives for high-margin businesses.
- Infrastructure support for complex projects.
- Workforce support (recruiting and training).
- Anything that reduces red-tape and speeds up time-to-market.

However, it is important to keep in mind that each project is different and has specific drivers and requirements and that agencies should be able to provide a range of support to meet different requirements.

INCENTIVES FRAMEWORK

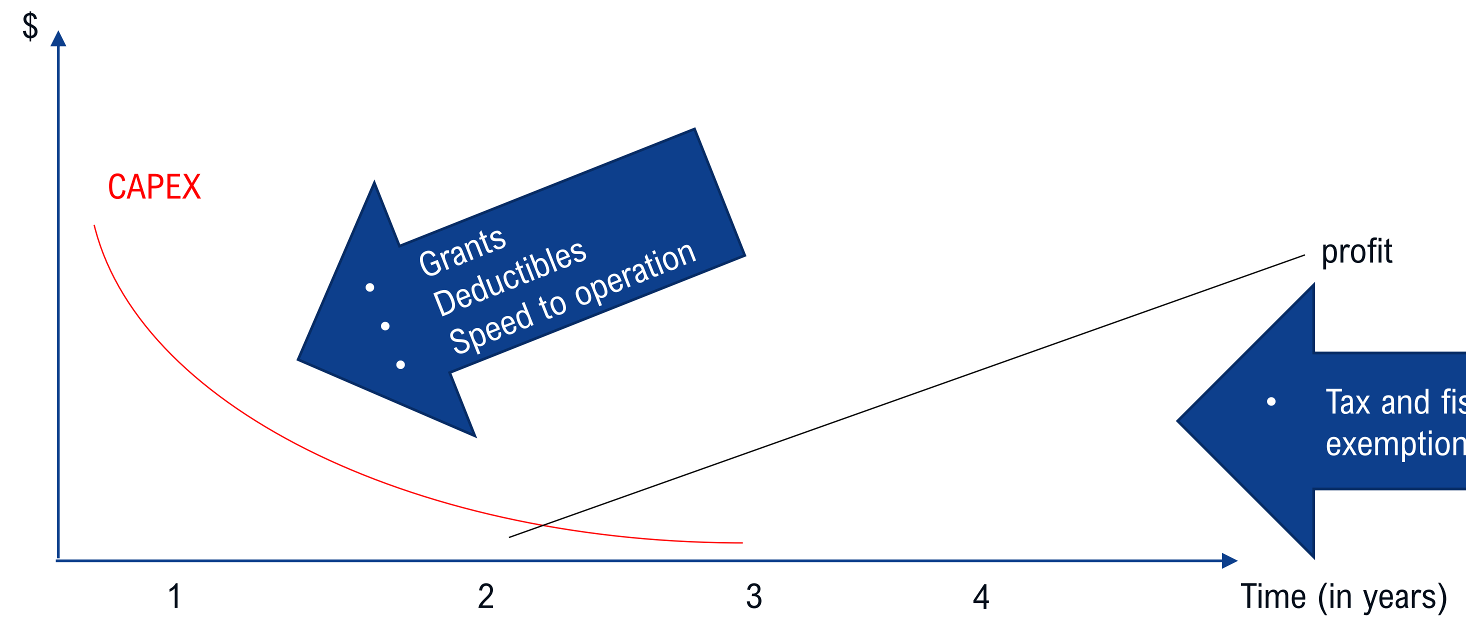
The different roles of incentives

To better understand the usefulness of incentives it is helpful to categories FDI projects into two general groups:

- Market seeking: the investor decides to establish a facility in a country with the aim to serve the local market. Incentives have a limited effect in this case, as establishing itself in the country is oftentimes a precondition for serving the domestic market.
- Efficiency seeking: an investor is seeking the best location for producing his product or service to then sell into the international market. As the investor can choose from different countries to locate his facility, incentives are especially valuable as they can swing the balance from one country to another.

The effectiveness of incentives also differs across different stages of the FDI lifecycle. This is illustrated in the graphic below:

The role of incentives over the FDI lifecycle:



INCENTIVES FRAMEWORK

OECD checklist

The OECD developed a checklist for assessing incentive policies, which is based on the following guiding questions:

1. Are FDI incentives an appropriate tool in the situation under consideration?
2. Are the linkages between enabling environment and incentives sufficiently well understood?
3. What are the clear objectives and criteria for offering FDI incentives?
4. At what level of government are these objectives and criteria established, and who is responsible for their implementation?
5. In countries with multiple jurisdictions, how does one prevent local incentives from canceling each other out?
6. Are the linkages between FDI attraction and other policy objectives sufficiently clear?
7. Are effects on local businesses of offering preferential treatment to foreign-owned enterprises sufficiently well understood?
8. Are FDI incentives offered that do not reflect the degree of selectiveness of the policy goals they are intended to support?
9. Is sufficient attention given to maximizing effectiveness and minimizing overall long-term costs?
10. Are programs being put in place in the absence of a realistic assessment of the resources needed to manage and monitor them?
11. Is the time profile of the incentives right? Is it suited to the investment in question, but not open to abuse?
12. Does the imposition of spending limits on the implementing bodies provide adequate safeguards against wastefulness?

INCENTIVES FRAMEWORK

OECD checklist (continued)

13. What procedures are in place to deal with large projects that exceed the normal competencies of the implementing bodies?
14. What should be the maximum duration of an incentive program?
15. Have sound and comprehensive principles for cost-benefit analysis been established?
16. Is cost-benefit analysis performed with sufficient regularity?
17. Is additional analysis undertaken to demonstrate the nonquantifiable benefits from investment projects?
18. Is the process of offering FDI incentives open to scrutiny by policymakers, appropriate parliamentary bodies, and civil society?
19. Have authorities ensured that their incentive measures are consistent with international commitments that their country may have undertaken?
20. Have authorities sufficiently assessed the responses that their incentive policies are likely to trigger in other jurisdictions?

4. CASE STUDIES FROM COMPETING LOCATIONS

CASE STUDIES FROM COMPETING LOCATIONS

Ethiopia is competing with other locations around the world to attract investors in the agro-industrial industry. It is helpful to understand which incentives other competing agro-industrial locations around the world are offering specifically for the selected target groups. The table below provides three brief case studies of incentive programs specifically for agro-processing investments:

Country/region	Description of incentive package
South Africa	• 20% to 30% cost-sharing grants to a maximum of US$1.5 million over a period of 2 years. • Additional 10% grant for projects that meet all economic benefit criteria such as employment, transformation, geographic spread, and local procurement. • The minimum qualifying investment size is US$70,000 for projects in all agro-processing sectors.
Ghana	• Reduced corporate income tax rate for entities involved in the production of livestock, fish, and other cash crops: 1% corporate income tax rate for five or 10 years; possible 5%-20% rate for further five years. • Investors located in a free zone are eligible for a 10-year tax holiday. • Exemption from customs import duties for plant, machinery, equipment, and parts. • 10-30% of salaries of recent graduates from local universities are tax deducible. • A 100% deduction is available for corporate income tax purposes for training expenses.
Western Australia	• Value Add Investment Grants for facilities that process fresh produce into value-added products (up to US$3 million on CAPEX). • Grants for building export competitiveness. • Vouchers worth US$500,000 are available for manufacturers to engage business consultants or technical experts.

5. EXISTING INCENTIVES FRAMEWORK

EXISTING INCENTIVES FRAMEWORK

Overview

Currently, the focus of Ethiopia’s incentive regime is oriented more towards hard incentives (i.e., financial incentives). There are three main types of incentives offered:

- Income tax incentives
- Customs incentives
- Financial incentives

These incentives aim to encourage private investments and attract foreign capital and transfer knowledge and technology into Ethiopia’s economy. The following pages provide more details on each of the available incentives as of July 2021.

EXISTING INCENTIVES FRAMEWORK

Income tax incentives

Incentive name	Brief description	Awarding authority
Business income tax exemption	• Duration of 5-15 years. • Available for companies in a variety of sectors such as manufacturing and agricultural sectors listed under the Investment Regulation, ICT development, electricity generation, Hotel and Tour operations (in non-traditional tourist destinations), development of industrial parks, and pharmaceuticals. • The duration can be extended by 2-4 years for companies meeting specific export targets.	• EIC (for international investors). • RIC (for domestic investors).
Loss carry forward for up to five years	• Loss incurred during the income tax exemption period can be carried forward for half of the exemption period after expiry, the maximum limit being five income tax period. • For investment sectors listed under the Investment Regulation.	• Ethiopian Revenue and Customs Authority (for international investors). • Regional Revenue Offices (for domestic investors).
Personal Income Tax (PIT) exemption for expatriate employees	• Up to five (5) years for expatriate employees of sourcing companies. • Limited to manufacturing companies located in industrial parks.	• EIC

EXISTING INCENTIVES FRAMEWORK

Customs incentives

Incentive name	Brief description	Awarding authority
Exemption from customs duties and other taxes	• Applicable for imported capital goods, construction materials, spare parts, vehicles, raw materials and accessories (including packaging materials) used for export processing, raw materials needed for test-run production, personal effects by industrial park residents. • Mainly applicable for the manufacturing sector. • The leather and textile industry is automatically eligible for customs exemption on spare parts.	• EIC (for international investors). • RIC (for domestic investors).
Customs duty reduction on imported raw materials	• Applicable for import substitutors in the manufacturing industry. • Companies must fulfill a minimum value addition threshold ranging from 5-41% depending on the sector.	• Ministry of Industry.
Export duty exemption	• Zero export duty rating for all export products except semi-processed hides and skins.	Not specified

EXISTING INCENTIVES FRAMEWORK

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Financial incentives

Incentive name	Brief description	Awarding authority
Skills development and retention cost-sharing grant	• Only for domestic investors. • Grant covering 85% (first year) to 25% (fourth year) costs of training local personnel and recruiting expatriate workers. • Limited to textile and leather manufacturing firms located in industrial parks.	• EIC
Export credit guarantee	• Guarantee by the Development Bank of Ethiopia (DBE) covering 80% of loan and interest provided by commercial banks to exporters • All industries except coffee exports.	• Development Bank of Ethiopia
Subsidized loans	• Repayment term of up to 20 years; and interest rate ranges between 9%-9.5% depending on export capability; longer grace period (up to five years). • Domestic investors in agriculture, agro processing, manufacturing, and extractive industries. • Debt: equity ratio for project finance to domestic investors located outside of industrial parks (75:25) – 85:15 for projects located within the industrial parks.	• Development Bank of Ethiopia / National Bank of Ethiopia (for very large loans)
Lease financing	• Applicable for machinery purchases by domestic SMEs in agriculture, agro processing, manufacturing, tour operations, mining and quarries, and construction sectors.	• Development Bank of Ethiopia.
Subsidized land lease and shed rental	• Industrial park developers as well as industrial park-based enterprises receive land/sheds at subsidized rates. • For each park, there are criteria regarding sectors and export performance.	• EIC.
Supplier's credit	• Available for import of goods of export-oriented companies. • Subject to assessment by the National Bank of Ethiopia that the investment will generate forex.	• National Bank of Ethiopia.

EXISTING INCENTIVES FRAMEWORK

Financial incentives (continued)

Incentive name	Brief description	Awarding authority
Franco-Valuta privilege	• For import of capital goods, raw materials, spare parts, and other accessories. • For capital goods, limited to domestic, and diaspora investors. • For spare parts and accessories, limited to the manufacturing industry and the conditions that the items are not available domestically. • For labels and packaging materials, only as inputs to export products.	• Ethiopian Revenue and Customs Authority. • EIC.
Priority forex access	• Limited to manufacturing and construction industry.	• National Bank of Ethiopia.
Export earnings retention	• Retention of 30% of export earnings for an indefinite period of time; and retention of 70% of export earnings for 28 days. • Applicable for all sectors.	• National Bank of Ethiopia
Access to foreign loan markets	• Foreign investors can raise up to 60% of their finance through a loan from foreign markets. • Domestic investors engaged in export-oriented businesses that generate forex can access foreign loans. • All sectors for foreign investors; only applicable for export businesses for domestic investors.	• National Bank of Ethiopia.
Reduced charge for opening Letter of Credit	• Reduction from the regular rate of 3.5% to 0.5%. • Limited to the manufacturing sector.	• Commercial Bank of Ethiopia, Development Bank of Ethiopia.

EXISTING INCENTIVES FRAMEWORK

Key findings

The existing incentives framework shows some general characteristics:

- Many of the incentives are oriented towards export-oriented light-manufacturing in the industrial parks
- Nonetheless, some of the incentives are also applicable for agricultural activities
- Mostly hard incentives – potential to further develop soft incentives

There remain some open questions that need to be clarified in regard to the IAIPs:

- Is agro-processing included in the manufacturing subsectors?
- Are the IAIPs considered as industrial parks for incentives eligibility?

The 2009 agro-industry policy report proposes one financial incentive specifically for the agro-industry: a 3.75-4% per annum back-ended interest subsidy for the first 5 years. To the extent of our knowledge, this proposal has not been implemented.

6. KEY INCENTIVES LEVERS FOR THE IDENTIFIED TARGET GROUPS

KEY INCENTIVES LEVERS FOR IDENTIFIED TARGET GROUPS

Introduction

In phase 1, we identified the target groups with the highest potential at the moment to attract investments for the three IAIPs. These target groups and their key locations requirements will now serve as the basis for identifying suitable incentives that support the investment attraction efforts to each IAIP. The key location drivers and the responding incentives levers are listed on the following page.

Besides these target group specific incentives, there are also some general incentives that will be valuable for the companies in the target groups:

- Import tariff exemption for capital good imports.
- Preferential access to foreign exchange.
- Eased work permits for expatriate plant managers (as long as experienced experts are not yet locally available).

Many of these are already covered by the existing incentives framework.

KEY INCENTIVES LEVERS FOR THE IDENTIFIED TARGET GROUPS

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Overview

Target groups	Selected key location drivers	Appropriate potential (new/soft) incentives
Coffee processors	• Ability to source raw materials • Ability to reach export markets conveniently	• Support in securing feedstock • Support in export promotion
Avocado processors	• Ability to source raw materials • Ability to reach export markets conveniently	• Support in securing feedstock • Support in export promotion
Pineapple processors	• Ability to source raw materials • Ability to reach export markets conveniently	• Support in securing feedstock • Support in export promotion
Tomato processors	• Ability to source raw materials • Attractive local market to supply	• Support in securing feedstock • Business matchmaking services with local off-takers
Dairy processors	• Ability to source raw materials • Attractive local market to supply	• Support in securing feedstock • Business matchmaking services with local off-takers
Industrial bakeries	• Ability to source raw materials • Attractive local market to supply	• Support in securing feedstock • Business matchmaking services with local off-takers
Livestock processors	• Ability to source raw materials • Availability of cold chain logistics	• Support in securing feedstock • Offer cold-storage in the IAIP
Producers of consumer goods from maize	• Ability to source raw materials • Attractive local market to supply	• Support in securing feedstock • Business matchmaking services with local off-takers

7. LIMITATIONS OF EXISTING INCENTIVES PACKAGE

LIMITATIONS OF EXISTING INCENTIVES PACKAGE

The current incentive package is very comprehensive and serves a good job to strengthen the value proposition of Ethiopia as an attractive investment location. However, keeping in mind that this package had been designed before the IAIPs started to promote themselves to domestic and international investors there are a few limitations. We especially identified the following ones:

- While the incentive package covers nearly all common financial ("hard") incentives ranging from tax holidays and tariff exemptions on capital goods imports, there is still room to add more soft incentives for investors (e.g., support to secure feedstock, business match making services, and support with training needs).
- Further, the current incentives measures have been designed with the industrial parks in mind. It is unclear if all of them will also be applicable for investors in the IAIPs. The material published on the IAIPs suggest that the IAIP investors will benefit from the same incentives as investors located in industrial parks managed by the Ethiopian Industrial Parks Development Corporation (IPDC). If this is the case, we recommend updating this on all relevant publications that an investor might consult (e.g., on the EIC's website). In case this is currently not the case, this should be resolved and made sure that the key hard incentives will also be applicable for investors in the IAIPs.
- There are currently no discretionary incentives available to secure strategic projects. Incentives (e.g., cash grants) that can be awarded on a case-by-case basis can have the advantage of providing a special offer to strategic projects that will offer large benefits for the country. Currently, all incentives are offered to all investors. This has the advantage to limit possibilities for corruption or other unfair market manipulations. On the downside, this might increase costs (or forgone revenue) as incentives are awarded to all projects, including projects that would have gone to Ethiopia anyway.
- The incentives package currently does not offer aspects of training, workforce, and R&D activity for foreign investors (the skills development cost-sharing grant is limited to domestic investors in the textile and leather sectors).
- There are currently no incentives to specifically encourage the development of linkages. The current package is based on import, assemble, and export manufacturing model. The IAIPs on the other hand are explicitly designed to foster linkages and technology transfer with the existing agricultural sector.

8. RECOMMENDATIONS

RECOMMENDATIONS

Modifications of the existing incentives

Based on the limitation listed in the previous section we recommend the following modifications to the existing incentives package:

- Make sure that all the relevant incentives for industrial park investors apply to the IAIP-investors as well (both domestic and foreign) per default.
- Incentives such as the existing skill development cost-sharing grant should be updated to also cover agro-industrial activities and should also be made available for foreign investors.
- There is currently a multitude of awarding agencies – providing a central point to support with applications can be useful.
- Not all of the currently existing incentives are relevant for potential IAIP investors or conducive towards achieving the policy objectives. These incentives do not need to be offered to them. These include:
  - Customs duty exemption or reduction for the import of raw materials

The next page will provide recommendations on new incentives that should be added to the incentive package.

Additional incentives

In order to account for the needs of the agro-industrial investors in the identified target groups, we recommend adding the following additional incentives:

- Support with securing feedstock: the ability to secure feedstock (raw materials) has been identified as a key location driver for all target groups. Currently, the production of raw materials is still fragmented among numerous mostly smallholder farmers and cooperatives. This may pose a serious challenge for investors to secure a steady supply of feedstock in a fast and efficient manner. Practical support by the relevant government agencies can be especially valuable to make securing feedstock fast and easy. We recommend holding talks with cooperatives, smallholder farmers, and commercial farms (if applicable) about their interest in supplying an investor with their crops. These commitments can be written down in MOUs and collected in a supplier database. An investor can then simply plug into these supplier agreements. This will save potential investors time and money and start up operations faster. Potential implementing agencies for this soft incentive are the RICs in cooperation with the Bureaus of agriculture.
- Export promotion: around half of the promoted investment opportunities are export-oriented in nature. Many companies will probably bring their initial sales contracts abroad with them once they decide to invest in Ethiopia. However, there is always potential to further grow the topline. By providing investors access to Ethiopia's export promotion support services, they can further grow their business and access new markets for their products made in Ethiopia. Anticipating this will make Ethiopia a more attractive investment destination for export-oriented investors and will help already established investors to expand their operations in the country. This incentive will require the cooperation of the investment promotion agencies with the Ethiopian Export Promotion Agency.
- Business matchmaking services with local off-takers: other investment opportunities depend on the ability to serve the domestic market. Key potential off-takers here are retail chains, restaurants, hotels, and large wholesalers. Especially for foreign companies planning to enter the Ethiopian market with the aim of selling to domestic consumers, finding the right off-takers will take time and effort. Proactive support here can convince investors off entering the Ethiopian market and will save them valuable time to market. This service can be best provided by maintaining a database of potential off-takers and providing introductions on-demand and through match-making events. This service can be best provided on a national level by the EIC.
- Dedicated training and skills development program for the agro-industry: talent availability plays a key role in attracting investments also in the agro-industrial and agro-processing industries. Especially vocationally trained talent is key for establishing manufacturing facilities. The availability of higher skilled talent such as in commercial, engineering or R&D functions can incentivize companies to expand their operations and to add business functions with a higher value add. This incentive can include training and skills upgrading grants for new investors to train their workforce. This can encompass cooperations with already existing initiatives such as the TVET training program. Further, hiring local high-skilled talent, and by way of this also located higher value add activities, can be made more attractive for investors by providing incentives for hiring graduates from local universities by covering part of their salary for the first year. To be administered by RICs.

RECOMMENDATIONS

Additional linkage-specific incentives

One of the key policy objectives of the IAIPs is the development of linkages from the investors with the existing agricultural industry. The following incentives are aimed at encouraging the development of these linkages. The following recommendations are partially informed by a study from the World Bank published in 2020:

For investors:

- Extension of income tax exemption conditional on local sourcing and/or technology transfer: 3-year extension of business income tax for companies sourcing at least 75% of their raw materials domestically. This can be extended by another 3 years for firms that fulfill criteria for technology transfer and agricultural extension. Additionally, it is possible to extend this incentive by covering 50% of the labor costs for a manager whose full-time job is to train local suppliers. To be administered by the Ethiopian Revenue & Customs Authority.
- Cost-sharing grants for the first year of local sourcing: the first step towards local sourcing is the most challenging one due to uncertainty of the quality, timeliness, and quantities that local suppliers will be able to provide. In order to mitigate this obstacle to initiate local sourcing, a cost-sharing grant shall be offered to investors during their first year of local sourcing. The cost-sharing grant will cover 15% of the costs for sourcing local raw materials. (This may need to be adjusted based on the commodities and their price differential between Ethiopia and the world market.) To be administered by the RICs.

For farmers and aggregators:

- Supplier development program: supplier development programs are most suitable and most common incentive program to increase local linkages. As part of such a program the government provides training and advisory support to suppliers to upgrade their capacity to meet the requirements of international customers. This requires a high level of capacity on the site of the implementing agency. To be implemented by the RICs (might require prior capacity-building efforts.)
- Subsidies for investments required for upgrading their level: cooperatives as well as aggregators might require investments into their equipment and assets to deliver the quality required by the IAIP investors. To support this upgrading the government can offer a fund, which subsidizes these types of investments. It is advised to install a cap on the maximum eligible subsidy per beneficiary. To be administered by the RIC.

VAT is already refundable for raw materials used as input in Ethiopia – otherwise, that is a common incentive.

9. NEGOTIATING INCENTIVES

NEGOTIATING INCENTIVES

Based on our experience working with governments worldwide, we provide here a guideline for negotiating incentives with investors:

- Do not lead with incentives (i.e., do not offer them immediately).
- If the company asks for incentives, understand why.
- Assess whether alternatives to incentives would address key issues.
- Ask the company to demonstrate the case for incentives.
- If incentives are required, provide offers quickly and be specific.
- Lay out the application and approval process.
- Ensure that offers are comprehensible (i.e., a company can understand a decision).
- Define clear and realistic performance requirements and milestones.
- Provide application and implementation support.
- Utilize enforceable “clawbacks” in case of non-performance (ability to be re-paid for incentives if performance requirements are not met).

ANNEX

Interviews and Sources

ANNEX

Interviews to date

- Ms. Ruchika Bahl, Chief Technical Advisor, ILO Ethiopia
- Mr. Ayalu Admass, National project coordinator, ILO Ethiopia
- Mr. Giacomo Casari, FAO Ethiopia
- Ms. Mercedes Marin Nortes, Delegation of the European Union to Ethiopia, Green Deal Team – Agro-industrialization
- Mr. Christian Dohse, Project Manager – Special Initiative on Training and Job Creation, GiZ Ethiopia
- Ms. Ludovica Marangoni, Agro-Component Manager – Sustainable Training and Education Program (STEP), GiZ Ethiopia
- Mr. Andrea Limiroli, Programme Coordinator, Italian Agency for Development Cooperation
- Ms. Senidu Fanuel, Senior Private Sector Specialist, World Bank
- Mr. Temesgen Zana Jaffo, Regional coordinator for Amhara, UNIDO
- Mr. Filippo Brasesco, Partner (Co-Founder), Scio Network
- Mr. Massimo Pera, Project Coordinator/AgrInvest, FAO
- Ms. Milica Petruljeskov, Consultant, FAO
- Mr. Ayalew Ferede, FAO
- Mr. Olijira Kuma Addamo, Project Coordinator, UNIDO
- Mr. Andrea Ghione, Chief Technical Advisor, UNIDO

ANNEX

Interviews to date

- Mr. Aschalew Tadesse, Director for Investment Promotion, EIC
- Mr. Techane Adugna, Director ACC, ATA
- Mr. Biru Wolde Gujo, CEO, SNNP RIPDC
- Mr. Ayalneh Abawa, IAIP Director, MoTI
- Mrs. Haymanot Asfaw, General manager of Ethiopian Millers Association

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