

Perspectives on Institutional Reform and Development in Ethiopia: The Critical Role of Building Enabling Institutions for Economic Growth and Development *

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ABSTRACT: This paper provides some normative perspectives on sustainable economic and political reform in contemporary Ethiopia, by focusing on the need to establish enabling institutions for economic growth and development. The paper begins with the basic premise that poverty in Ethiopia is primarily a problem of *institutional failure*, and that a successful economic reform not only must be focused on poverty-focused economic growth in a country where about 50 percent of the population is below the poverty line, but it must also be accompanied with *institutional reform* and development that may result in a *positive-sum* outcome for all constituent groups of the country. The paper reviews some economic concepts of institutions and their role in development, and their implications for democratic institutional development and public policy reform. Some of the current institutional and structural roadblocks to a successful political and economic reform and transition to a market economy, including the appropriate role of government in this process and the potential role of the Diaspora in the development process are also briefly discussed. The paper is intended to contribute to a process of constructive dialogue that may inform current and future institutional and development policy reforms by raising some policy issues, and by providing normative perspectives that can be enriched by future empirical research based on actual realities in Ethiopia.

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Introduction: Objective and Assumptions

This paper provides some perspectives on contemporary political and economic development policy problems in Ethiopia. It is intended to provide a critical input to the process of policy dialogue that may lead to institutional reform aimed at the economic development of Ethiopia. First, it must be stated that a serious economic and political reform in Ethiopia is in everyone's interest regardless of political views and orientation. Such a move would be in the *enlightened self-interest* of the current government, the various opposition groups, and civil society groups and the general population in general. It would be a *positive-sum* move where every one will gain in the long run. Second, a serious and sustained institutional and policy reform must be one focused on a significant reduction of poverty, in a country where about 50 percent of the population is below the international poverty line, and with one of the lowest per capita income in the world¹

This harsh reality that Ethiopia finds itself is not because it lacks human resources. Ethiopia is a large nation of over 60 million people, the majority of whom are rural based and hard working. Persistent poverty is also not because Ethiopia lacks the necessary natural resources, because it is endowed with enough resources if properly managed and utilized. The recurring problem of food insecurity cannot be primarily attributed to draught, although it has some role. The discussion of this paper is based on the basic assumption that the poverty problem in Ethiopia is fundamentally a problem of *institutional failure* that has inhibited the country's human and natural resources potential to be realized or channeled toward productive activity.

Some Concepts of Institutions and their critical role in development

It is important to be clear about what is meant by "institutions" for the purpose of this paper. *Institutions* are rules of human behavior that provide incentives under which rational people act. They are accepted modes of behavior protected by *culture* (Powelson). They involve laws, social norms, traditions, beliefs and other established rules of human behavior. Institutions provide the carrots and sticks that direct all forms of human activity, including economic activity. Institutions and organizations are not same, although they are sometimes used interchangeably. Organizations operate within a set of institutions. Whether organizations and individuals can serve a constructive or destructive purpose depends on the institutional framework in which they operate.

¹ Ethiopia's GNP per capita was \$110 per year 1997 according to *World Development Report 1998/99*. The Country's Human Development Index, which is a composite index of GDP per capita, life expectancy, and education ranks fourth from the bottom or ranks 171 out of 174 countries listed according to the *Human Development Report 2000*, published by the UNDP.

For example, the market system is a set of institutions, so are the systems of democracy and socialism. A particular government or political party such as the Labor Party in the United Kingdom is an organization, which operates within the institution of the British democratic system. The World Bank and the IMF are organizations that operate within the global financial system, which can be regarded as a global institution (Ibid)

A critical task for any society is to develop a set of institutions that enable and constrain individuals and organizations to behave in constructive rather than destructive manner. Depending on the institutions that provide the incentive structure, individuals and organizations are capable of behaving and acting both in productive or unproductive manner. Van Den Berg captures this idea well when he states “ Economic disasters are caused by rational behavior reacting to incentives by faulty institutions” (Van Den Berg, P.409)

The challenge of overcoming poverty in any society is to develop institutions that support and promote economic growth. In order to promote economic growth, institutions should provide individuals to work hard, to save and invest, and for entrepreneurs to take risks and to actively pursue economic opportunities, for firms to improve their production methods, for governments to use public revenue efficiently to provide public goods and to design cost-effective programs to meet socially well-defined goals. Institutions that enhance human welfare are those that channel individual and organizational efforts to productive activities by encouraging innovation. Such institutions are best established in economies where: *property rights* are well defined and secured, and laws are clearly defined and fairly enforced. For agrarian economies like Ethiopia, the establishment of *secure and clearly defined land tenure system* becomes crucial due to the predominance of Agriculture in such economies.

One of the limitations of neo-classical economics in explaining the process of development is its lack of consideration of institutions in analysis. Yet, the development and effective functioning of the market or the capitalist system itself critically depends on institutions that establish and secure private property rights. Clearly defined and protected property rights are essential to motivate people to engage in voluntary efforts and exchange based on contracts that benefit themselves and also benefit others, often people they do not know. This basic idea was recognized as the *invisible hand* by Adam Smith who is regarded as the father of economics in his book The Wealth of Nations. The idea is not an abstract topic of relevance to big corporations or business only. It affects everyone’s daily economic life and activity of how to save and invest, whether one’s labor can be employed to best advantage, and whether one can thrive with one’s inspirations and resources.

According to Nobel laureate economist Douglass North, the primary causes of economic growth are institutions that lower *transaction costs*, and governments may not promote such institutions due to two reasons: First, the rulers may be able to increase revenue or income by restricting transactions, by undermining property rights, and by focusing on certain groups or regions easier to exploit or to tax to benefit others. Second, efficient institutions that minimize transaction costs may not benefit special interest groups that are vital for the survival of the rulers or the oligarchy (North, 1987). In sum, political expediency prevents the rise of efficient economic institutions that enhance economic growth and alleviate poverty.

The transition from totalitarian dictatorships to free enterprise economic systems has proved more difficult than it first seemed. A successful transition involves more than overthrowing a dictatorship. It involves more than the privatizing former state owned assets. It is one thing to privatize, but it is quite another to create a working market economy since that requires the creation of new institutions of property rights, business laws and contract enforcement mechanisms. One problem during transition is that *informal institutions* such as habits and networks lead people to behave in ways that is not compatible with the market economy. The culture of *corruption* and *rent seeking* may retard the development of market economy and economic growth limited by people's inability or unwillingness to adapt to a new set of institutions. For example in the post-Soviet Russia, Mafia type business networks and massive corruption have arisen to block and frustrate a successful transition to the market economy (Van Den Berg). In general, it can be said that the existence or the lack of efficient institutions explain why some nations are rich and others continue to be trapped in poverty.

Some quantitative studies of economic growth have tested some variables that represent institutions. These variables, which determine the economic "climate", include the incentive structure, the level of competition, and level of government regulation of markets. When these variables are considered as index of institutions and included a growth equation that relates data on growth of income to factors of production (labor, Land, capital) and institutions, they turned out to be statistically significant (Ibid).

Ethiopia's Institutional Problems

Economic decline and poverty has been primarily a problem of *institutional failure* caused by concentration of power or absence of *Power-Diffusion Process* as articulated in the book, Centuries of Economic Endeavor by John Powelson (2000). Institutions that sustain economic development are gradually created in the power-diffusion process, where power is defined as "the ability to influence or direct the behavior of others" (Powelson, p.4). At the center of the institutional failure in Ethiopia is the historic problem of governance, which has been characterized by a concentration of power among a few elite, engaged in arbitrary use of power over the silent majority of the population. The term *elite* refers to the small segment of society that has a monopoly of political power at the national, regional and local levels². Such power is most often gained through violent or non-democratic means. In this regard, the *Derg* and its disastrous policies of 1974-91, stands out as unparalleled in recent history of Ethiopia. The damage and the atrocities of this period on the human capital and economy of the Country are well known and need not be repeated here. But, it is fair to state that the extreme level of power concentration that led to the policies and institutions that prevailed during this period, are to large extent, responsible for persistent poverty and the related socio-economic and political problems that followed ever since.

² For an analysis of elites and *elitism* in Ethiopia, see Messay Kebede's paper, "From Marxism-Leninism to Ethnicity: The Sidelips of Ethiopian Elitism", in the *Proceedings of the EAF International Conference on Contemporary Development Issues in Ethiopia*, Western Michigan University, November, 2001.

The magnitude of economic and political problems of post-Derg or post-1974 Ethiopia cannot be equated with the pre-Derg period. Pre-1974 Ethiopia scored some major achievements both domestically and internationally that the current generation of Ethiopians should be proud of and take appropriate lessons from. For example, some of the most successful pan-Ethiopian economic organizations such as the Ethiopian Airlines, the telecommunication system, the national university, the banking system, and the agricultural research system were established during this period.

The institutional development experience of Ethiopia's has been categorized into three historically distinct periods by Bahru as follows: The period of institutional building, 1941-74, the period of distress, 1974-91, and the period of restructuring, 1991 to the present). About the pre-1974 period, he wrote, "*In retrospect, the period 1941-74 strikes one by the number of solid achievements that were registered in the realm of institutionalization. Quite a number of institutions that are still important to our life today, albeit battered and tattered, trace their origin to this period. These institutions span the whole gamut of public administration, finance, education and infrastructure*"³

The performances of some of these organizations were among the best in developing countries, and were unmatched in the rest of Africa. Although there was poverty and related economic problems during the Haile Selassie regime in areas such as land and wealth inequality that needed reform, the fact remains that Ethiopia was generally at peace and had a great potential for economic development. It was a strong and respected nation in the world, which the rest of Africa and black people elsewhere looked up to. Ethnic and nationalist movements were insignificant, and were largely contained at the time.

African nations had enough confidence in the country to give Addis Ababa a status of the nominal "Capital of Africa" by placing the Organization of African Unity (OAU) in that city when OAU was founded in 1963. Ethiopia was economically successful during this period, especially in the area of manufacturing with a great promise to become a middle income-developing nation at par with South Korea. While the late Emperor Haile Selassie was no democrat, he provided great leadership in promoting unity both in Ethiopia and the rest of Africa. The point here is not to glorify the Imperial period since it also suffered from concentration of power and corrupt rule that was insensitive to the basic needs of most Ethiopians, but to simply put it in relative context.

A critical historical accident took place in 1974 that led to the rise of the Derg, a vicious military dictatorship that took the country along the wrong path. The Derg copied totalitarian system of governance and developed a set of institutions and policies to support that system. The institutions established during this period provided the incentive structure for individuals and organizations to behave in a destructive rather than constructive manner. Individuals and organizations arose under the cover of 'socialism' leading to the destruction of the country's human capital, the suppression of civil society and economic initiatives, at the cost of huge human and economic loss to the country. An alien model of command socialism was forced on the population. The political/economic model such as that of North Korea was emulated. South Korea and Japan, would have been better models to adopt.

³ See Bahru Zewde's article, "The Problems of Institutionalization in Modern Ethiopia: A Historical Perspective", in the *Proceedings of the Ninth Annual Conference on The Ethiopian Economy*, edited by Alemu Mekonnen and Dejene Aredo, Friedrich Ebert Stiftung, Addis Ababa, September 2000, P.15

The difference in economic performance between North and South Korea, which are nations of the same people, is largely the difference in political and institutional structure. The reality, today, is that North Korea cannot even feed itself while South Korea is an emerging major industrial state. Although South Koreans started from a poorer industrial base and had to cope with a devastation of war in 1950s, they are now economically at least ten times better off than their northern compatriots who live under command socialism (*The Economist*, 22 February 1997, p.33). The same can be said about Germany, where starting from about the same low level of incomes after the war, the former West Germany had reached a much higher level of income than the former East Germany. After 40 years of development under different economic systems, the average income of East Germans was about 40 percent of their West German compatriots before the collapse of East Germany in 1988 (Kasper. P.415). The primary difference is that North Koreans and East Germans adopted command socialism along with the institutions that monopolize political and economic power the state, and suppress productive activity, while South Koreans and West Germans adopted a free market system along with the institutions that disperse political power to citizens and support productive activity. It is also noteworthy to add the fact that Ghana's per capita income at independence in 1957 was more than South Korea. Some 50 years later, Ghana has per capita income of \$370 per annum compared to South Korea's per capita income of \$10,550 (IBRD,1997). This is not to deny the role of other factors that account for these differences, but to underscore crucial role of presence of institutions that enable market-based and poverty focused economic growth.

A related and broader issue is whether economic freedom made possible by free market capitalism is related to political freedom that results from the development of democratic political institutions⁴. Since markets provide economic strength or power to the private sector, they serve as a check to political power of the state. The development of Markets separates economic power from political power needed for democracy and freedom. It is no accident that political freedom has historically occurred at the same time as the development of capitalism and market institutions in the Western World during the 19th century and early 20th century, with few exceptions. However, although capitalism is a *necessary* condition for democracy, it is *not a sufficient* condition since the historic economies of Nazi Germany, Fascist Italy or Spain, and Tsarist Russia were capitalist economies even though there was no democracy or political freedom in these societies. For both economic and political freedom to occur, it is necessary for the diffusion of political power to occur. A related issue is that of the problem of 'sequencing' or whether political freedom should come before economic freedom or vice versa. The answer to this question is complex, and poses a chicken and egg dilemma. But, the development of markets that may lead to economic freedom and growth is more likely to lead to political freedom. A simple reason is with a growing economy, it becomes easier for citizens to get along or to manage conflicts peacefully over distribution of wealth. In other words, it is difficult for a country to avoid a dictatorship in the midst of mass poverty. This may explain, in part, the historic lack of development of democratic institutions in Ethiopia.

⁴ For a good discussion on the relationship between economic freedom and political freedom or democracy see *Capitalism and Freedom*, by Milton Friedman, University of Chicago Press, 1982.

In retrospect, there was little justification for Ethiopian political elites of the time to throw out the whole system in 1974/75, which also undermined and destroyed some key pan-Ethiopian institutions, culture, and sense of national unity that was gradually emerging. Ethiopia could have avoided this grand failure of transition, by making a meaningful political reform along a constitutional monarchy such as Japan or Great Britain. It was not necessary to inject into the Ethiopian society and politics the alien ideology and institutions of Marxism and Leninism, the political and economic consequences from which the country has been suffering ever since.

During the Imperial era, it was possible to launch the country on an entirely different path with an institutional reform backed by an *enlightened leadership* and a constitution that allowed for a peaceful transition of political power. But, the lack of cooperation and conflict among the elites of that period, combined with the inaction of an aging Emperor made cooperation for institutional reform and peaceful transition impossible. Examples of such conflicts include: the conflict between the educated commoners led by the late prime minister Aklilu Habtewold and the Aristocrats led by Ras Asrate Kassa, President of the Crown Council in the Imperial government. There was also a conflict between the Emperor's daughter Princess Tenagne-work, who was influential with the Emperor and had an ambition to put her son Prince Eskinder Desta on the throne. Both Ras Asrate and Princes Desta, who had huge land holdings were strongly opposed to any kind of institutional reform including land reform. In revealing this conflict to the reform commission, the late P.M Aklilu commented " I could not carry out what I thought was good for the country because although I was the prime minister during the day, Princess Tenagnework was the prime minister at night"⁵. Moreover, the mental capacity of the aging Emperor may have also contributed to his inability to break such conflicts and to enable institutional reform of the monarchy aimed at peaceful transition during his final days. John Spencer, a long time advisor of the Imperial Government judged the mental capacity HaileSelassie as "senile" during his last days of his rule. In describing the Emperor's senility, Spencer in his book, *Ethiopia at Bay*, wrote: "*It became apparent to me during the course of our conversation that Haile Selassie was already retreating into a dream world. To me, who had known him for nearly 40 years, he appeared to have become disturbingly in articulateAt the state dinner in honor of President Mobutu of Zaire, Haile Selassie summoned a lackey to ask, fortunately in Amharic, who was the quest of honor sitting opposite to him!. During his first and only trip to China in 1973 he was constantly declaring that on a previous trip to China he had already seen the places he was visiting !*" (Spencer,1984. P.335). So, the political elites of the period acted in a selfish manner instead of acting with enlightened self-interest in order to reform the system. It was a *Prisoner's Dilemma* problem that resulted in *collective failure* among the elites of the Imperial Government of the time⁶.

⁵ Based on comments received from Paulos Milkias, September 2001, on the first draft of this paper.

⁶ A *prisoner's dilemma* is a situation in which two or more parties become worse due to the lack of cooperation, where each party decides to rationally act alone since the other party(s) cannot be trusted or cannot make credible commitments.

But, why did the Ethiopian leadership fail in the past or why did it not act in the enlightened self-interest in order to reform itself? The reason may have to do, in part, with lack of long-term vision in leadership. It is also a result of centralization of power or lack of “*power-diffusion*” to use Powelson’s term, and the behavior of individual involved in each of the regimes. During the Imperial era, political power concentration resulted in institutional failure that blocked successful reform and transition. Although there were individuals with leadership talent, they could not emerge because the Emperor did not allow for the necessary devolution of power and decision-making. The key mistake Haileselassie made was that he waited too long or until he became old and “senile” to make the necessary institutional reform involving the devolution and transfer of power along the lines of constitutional monarchy. By the eve of the revolution in early 1970s, it was too late. Refusal to make institutional reform and to share power was also a key feature of the Mengistu regime. Mengistu, in addition to unleashing terror of “rule by men” (not by the rule of law), also waited until he was just to be removed from power to undertake reforms of power sharing. Mengistu initiated market reforms in 1989. By then it was too little too late, since too much damage has already been done.

There is a critical distinction between *selfish* and *self-interested* behavior⁷. Successful modern economies are results of entrepreneurs who act in enlightened self-interest, and the institutions that support them to succeed so they can create wealth for themselves. By doing so they also create employment and income opportunities for others. For example, enlightened self-interest allowed Microsoft’s Bill Gates not only to become a billionaire, but also to make a major contribution to the global computer technology and at the same time create millions of jobs including creating several hundred other millionaires. Gates is also a major philanthropist who contributes millions of dollars to social causes such as education. His success would not have been without the enabling institutions of American capitalism and the free enterprise system.

It is not helpful or fair to blame a particular group such as the Ethiopian students during that revolutionary period of the 1960s and the early 1970s. There is plenty of blame to go around. The Ethiopian students were part of the revolutionary fervor of the time like students in other parts of the world including the United States in challenging the system that prevailed. But, in Ethiopia, the central government and the institutions were not able or willing to respond or address the students demands for basic expression of inequality and poverty such as the call for *land to tiller* question. The Ethiopian students also expressed their legitimate frustrations in the lack of democratic institutions in other areas such as the lack of political parties, lack of independent or free press to allow free expression of political views. What were lacking were flexible democratic institutions that could both address and absorb external political shocks to the central government, and implement appropriate institutional reforms needed at the time.

⁷ Economies generally grow by productive activities of individuals guided by self-interested (not selfish) behavior who create opportunities and income or employment for others. Institutions that support such activities are conducive to economic growth. Even individuals who may appear to be engaged in charitable activities can be regarded to be motivated by enlightened self-interest, since charitable giving makes them happier or feel better. For example, no one can accuse the late mother Theresa for being selfish, but her charitable activities is consistent with enlightened self-interest, since the many charitable activities she was engaged in made her happier and/or was consistent with her religious belief and value.

In other countries such as the United States, where democratic institutions have matured, legitimate grievances and demands are addressed and excessive or extremist revolutionary activity is legally and fairly contained without turning the basic apparatus of the state up side down. Ethiopia was not alone in this regard. There were other nations such as Iran for example, where the institutions of the Shah regime were swept away by the Islamic revolution of Ayatollah Khomeini. One can ask or wonder in retrospect whether Iranians are economically better off today than before the revolution? The point here is revolutions, however well intended they may be, do not always advance the human welfare for the better.

For Ethiopia, part of the challenge of a possible economic revival or renaissance may be whether she can overcome the massive misinformation and historical distortions, which has its origins during that period and which still haunts the political economy and the public policy environment of the Country. There is a critical need to inform current and future development policy based on the historical experience of the recent past, which carefully and objectively examines the record of achievements (positives) and failures (negatives) under each of the three regimes in recent history. Such a careful examination cannot, for example, simply dismiss the achievements of Pre- Derg Ethiopia and lump it with the Derg period. Some studies have argued that the “feudal” institutions of the Imperial period could not be reformed or modernized⁸. But, it is the view of this author that peaceful democratic institutional reform along a modernizing constitutional monarchy would have been possible if there was a strong will and a genuine commitment to reform and power sharing at the time. What was lacking was an institutional mechanism that allows for peaceful transfer of political power vested in the Emperor.

Even the Derg, which has the longest list of failures that primarily stem from arbitrary rule and use of power has at least a few positives such as the land reform, but failed in the process of implementation and is still in urgent need of reform. The Derg also reduced cultural and wealth inequalities. But, the Derg’s method of forced and reckless redistribution and confiscation of wealth and assets resulted in the redistribution of poverty over the population and undermined economic growth. So, in retrospect even the Derg, which is the worst of the Ethiopian regimes in recent history, could have reformed and taken a different turn had it began reforms earlier instead of rigidly clinging to misguided policies and institutions until it was forcefully removed. Rigidity, arrogance, and lack of political inclusiveness or refusal to share power combined with arbitrary use of power led to the inevitable downfall of that regime in 1991.

The necessity of peaceful political and economic reform then follows from recent historical experiences of Ethiopia. What is needed now may be to begin the tradition of peaceful political transition and reform. Future political transition must be peaceful. Violent removal of any regime is likely to produce another regime just as violent in the future. It is noteworthy point out here that even the final political transition in South Africa from the minority rule under Apartheid to the majority democratic rule did not involve violence. It took the great leadership of Mr. Nelson Mandela and his colleagues of the African National Congress (ANC), as well as the cooperation of the minority government of Mr. De Klerk to make the final transition to majority rule in 1994.

⁸ See for example, "Political Linkage: The Relationship Between Education, Educated Elites and the Fall of HaileSelassie Feudal Regime", Ph.D. Dissertation by Paulos Milkias, McGill University, 1982.

The final demise of Apartheid was, of course, preceded by sustained internal and external struggle of various forms against that system. Ethiopia herself was one of the key African nations that contributed to the anti-apartheid struggle.

Unfortunately, a handful of the 54 African states are currently making meaningful political reform and transition under democratic lines. These include, South Africa, thanks to the visionary leadership of Mr. Mandela. Botswana is a quiet nation blessed with a tradition of tolerance and democratic institutions nurtured by wise political leadership. In West Africa, Nigeria has recently taken the first step of conducting a successful election that may end the cycle of military coups and launch the country along a democratic path. But whether this will be sustained remains to be seen. Ghana is moving along the same line following peaceful transfer of power. In East Africa, Tanzania is moving in the right direction after years subjecting its economy to “Ujama” or African socialism. Uganda is opening up its economy and building the basic institutions of a free enterprise system, in spite of adopting a controversial “no party democracy”.

These are all positive moves that may contribute to what some have called a possible “African Renaissance” during the 21st century (Mbeki, 1998). But serious challenges in other states remain. Kenya appears to be reversing some of the economic achievements of the past due to failure to make a democratic political transition. Zimbabwe began with great promise at independence in 1980, but now suffers from inability to make peaceful and smooth democratic transition. The failure of institutional reform and transition has recently forced Zimbabwe to abandon market reforms and to go back to command socialism.

Institutional reform aimed at policies that attract foreign direct investment (FDI), not foreign aid, to enable economic growth is critical for African renaissance during the 21st Century. Currently, Africa is receiving about 3% of foreign direct investment flows to all developing countries compared East Asia, which is attracting 40% of the FDI flows. Sachs (1996) believes that economic growth can be achieved in many African countries with appropriate reforms⁹.

What does this mean for Ethiopia? The above examples are cited to simply point out that it is possible to move toward an inclusive and democratic political system under a visionary leadership committed to meaningful power sharing, and institutional reform in Ethiopia. This outcome is in the long run interest of the ruling party, the various opposition groups, and for the Ethiopian society in general. It is a *positive sum* outcome. The alternative is likely to produce a *negative sum* outcome, where every one losses as we ought to learn from Ethiopia’s recent history and the comparative experiences from the rest of Africa and other developing nations.

A key question is how a political leadership that commits itself to power sharing and/or peaceful transfer of power through open and free elections will come about. This is primarily an institutional problem of designing the political rules of the game or a constitution with checks and balances and proper enforcement incentives or mechanisms.

⁹ See “Growth in Africa: It can be done” by Jeffery Sachs in *The Economist*, June 29th, 1966, P.19-20. Sachs also points out in this article that with the exception of Botswana, Mauritius, and Uganda (since 1989), none of the 53 African states matched the 5% per capita growth, which was the average growth rate of all developing countries in 1995.

It is a problem of building institutions that allow for the diffusion and transition of political power. A visionary leadership may in principle be able to bring about this type of constitutional government by calling for national political reconciliation such as in the case of Mr. Mandela of South Africa. The new or post-Apartheid South Africa would not have been possible without his leadership; which brought national reconciliation among viciously antagonistic political forces in a highly differentiated ethnic and racial climate and laid the ground for a successful and free election. This process was complemented by “truth and reconciliation” hearings, which allowed South Africans of all races and ethnicity to openly discuss and admit the atrocities of the past and bury them behind in order to focus on solving development problems. Ethiopia may need to do the same in order to openly address hidden potential conflicts, and acknowledge past atrocities and mistakes once and for all, and move on to focus on current and future problems of eradicating absolute poverty.

Implications for Current and Future Institutional Reform

According to the official statements of the current ruling party, the Ethiopian People’s Revolutionary Democratic Front (EPRDF), Ethiopia is committed to adopt a market or a capitalist economy. In fact, from what one can gather from the international media, the recent power struggle within the TPLF/EPRDF has much to do with political and economic reform. Since 1991, certain economic liberalization policies have taken place such as the removal of price controls, promotion of limited private economic activity, the emergence of limited free press, and some level of decentralization¹⁰. These are important beginnings on which to build on. But, serious obstacles and institutional impediments to a peaceful transition to a market economy remain. If not removed or if rigidly retained, are likely to continue to trap Ethiopia in a continued state of poverty and political conflict. The next section will focus on two areas that need to be reformed in order to re-invigorate the institutional environment of Ethiopia aimed at promoting market-based economic development and transition.

Toward a Sustainable Federal System of Governance¹¹

Some of the most successful democratic countries around the world such as the Canada and the United States, comprise of non-ethnic federal states or provinces. Imposing a centralized unitary political system in Ethiopia, as has been tried under the previous regimes, is likely to be a failure. On the other hand, the top-down injection of ethnicity into federal political structure may do more damage to society than its benefits. Imposition of ethnicity into federal structure is likely to impede or retard the mobility of resources (labor and capital) required for markets to work and develop.

¹⁰ A recent study on macroeconomic performance in Post-Reform Ethiopia revealed that “ although the performance is very good, when judged in the context of the structural problems of the period under analysis, the sustainability of the results is highly questionable”, see *Macroeconomic Performance in Post-Reform Ethiopia* by Alemayehu Geda, 2001.

¹¹ Some of the views expressed in this action should be regarded as hypotheses that need empirical verification based on current realities and data from Ethiopia.

Politically, it is likely to be a breeding ground for inter-ethnic (among ethnic groups) and intra-ethnic (within each ethnic) conflicts. While some clever political arguments for sustaining such a system may be, it is unlikely to lead to stability and peace in the long run. It cannot, for example, be defended with the concept of “*national self-determination*” which is a term used by Joseph Stalin to impose totalitarian rule over various ethnic groups of the former Soviet Union. This term along with the other abused terms such as “*revolutionary democracy*” and “*democratic centralism*” have their origins in Marxist-Leninist-Mao Tse-Tung literature. When stripped of their jargon and in practice, they are nothing more than political justifications used to suppress dissent and to subordinate society to the tyranny of small political elites. In reality, democracy is an evolutionary process that must be adopted to the culture of a country. When it works, it allows for a peaceful transition of political power. Democracy is fundamentally based on personal individual freedom or individual self-determination with a freely elected representative government, and kept in check by the rule of law, peaceful political competition, and the independent judiciary and the free press. *Ethnic or group self-determination* does not necessarily lead to individual freedom or self-determination, which is the basis for a true democracy. The best way to protect group rights, ethnic or otherwise, is to protect the human and individual rights of citizens. The reverse may not be true. For example, the fact that an ethnic group has “self-determination” does not mean that individuals within that group have their basic human rights protected or have individual self-determination. Just the opposite may be the case. For example, saying that the Amhara, the Oromo, or Tigray nationals etc.. as a group have “self-determination” within their respective ethnic regions does not necessarily mean that individuals within these regions have their basic freedoms or civil liberties protected, in absence of democratic institutions that secure the personal and civil rights of citizens within their communities.

On the other hand, establishing an inclusive constitutional political structure that protects individual freedoms is more likely to also protect the ethnic rights or other group rights under a true federal structure. If one’s rights or freedoms are truly protected as an individual by the rule of law, there is no reason why one’s ethnic rights or one’s voluntary association with any group, ethnic or otherwise, will not be protected. But, the reverse is not true. A federal system that will allow for free mobility and association of people based on a mutually beneficial cultural, social and economic interests in pursuit of opportunity to work, to trade, and invest will be the way to move forward in Ethiopia. Such an institutional framework will also allow citizens to form associations based on ethnicity if they wish to do so. The key issue here is by whom, how or by what process decisions were made to create or sustain the institution of ethnic federalism. Have these institutions been a result of a free will of the silent majority of the Ethiopian population or do the political elites and cadres of various ethnicities impose them? Are these institutions imposed from the top-down to serve the same purpose as a totalitarian rule was imposed during the Derg era? These institutions, like command socialism, can be regarded as alien to the culture of Ethiopians. They fail to recognize the shared pan-Ethiopian cultural traits of a multi-ethnic society that has evolved over a long period. The *Killils* do not account for the heterogeneous nature of the major linguistic groups that they claim to represent since Ethiopians traditionally identify themselves by geographic locations or regions and sub-regions.

Moreover, such institutions fail to recognize the heterogeneous nature Ethiopian ethnic groups based on locations. For example, there are significant cultural differences among the Amhara from Gojjam, Gondar, Shoa, Welo etc.. inspite of the linguistic similarity. There are similar differences among the Oromo from Wellega, Harrar, Arsi, Welo, and Shoa, in spite of the general similarity in language. These are natural differences and should not be denied or exploited by politicians. Ethnicity is natural just like one's color and weight. It should not be used as a source of political conflict. Ethiopia is not different in this regard since such differences exist in any multi-ethnic country. They should simply be accepted, and ethnic and cultural inequalities that exist should be corrected through education and the rule of law when they are violated. The fact that such ethnic and cultural inequalities and abuses have historically existed in Ethiopia is a fact that should not be denied also. These should simply be acknowledged, and lessons should be drawn to avoid future problems.

It should be noted that absence of ethnic diversity or the presence of ethnic homogeneity does not prevent vicious political conflict and power struggle within the same ethnic group. For example, it has not prevented Somali political elites to commit massive atrocities to their people and to the collapse of the state of Somalia. But, the challenge of inter-ethnic or intra-ethnic reconciliation cannot be underestimated in Ethiopia, given the political climate of the last decade.

Non-ethnic based federal democracies are most successful in dealing with ethnic diversity. For example in the federal democratic political system of the United States, an individual's right is constitutionally protected regardless of his or her ethnic background. Imagine, for instance, the implication of an American politician that proposes to amend the U.S. constitution by suggesting that Americans of certain ethnicity to live in a particular part of the country or state such as, for example, German Americans to live in Pennsylvania, Dutch American to reside in Michigan, Italian Americans to leave in New York, African Americans to live in Mississippi or Georgia, etc. Such an ethnic based federal political re-structuring is likely to create political chaos and to rapid economic decline in the United States. The American Constitution and democracy resolves this by protecting individual freedom under the rule of law, which also protects voluntary association based on ethnicity if people wish to do so. The U.S. Constitution is based on the basic and key idea of "one nation, under god, with liberty and justice for all", which explicitly incorporates the national goals of unity within diversity and freedom under the law. It has no words such as "national or ethnic self-determination including and up to session", which directly contradict democratic unity within diversity. If some one is an American citizen of any ethnic background, his or her rights are constitutionally protected as an individual and that he or she can choose to live, work and invest where he or she chooses under the Country's democratic framework. The Constitution also allows and protects the voluntary association of citizens based on ethnicity or religion if they freely choose to do so. For example, if some one is a Polish American and wishes to live in a Polish community, to exercise his or her culture, to speak his or her language, to become a member of an association of Polish Americans, the individual is free to do so without coercion.

The individual's civil rights including his or her rights of voluntary association are fully protected by the Constitution¹². For example, there are more Polish people in the City of Chicago than in the city of Warsaw, simply by free choice, not because the Constitution or some political elites dictate that they should do so.

Another example, perhaps more relevant to Ethiopia, is Malaysia, a country which has managed ethnic diversity by adopting a working democracy and by focusing on economic development. Malaysia is a multi-ethnic nation with three major ethnic groups: the Malays (55%), the Chinese (35%), and Indians (10%). Malaysia adopted democratic governance, which allowed the Malays or the majority, to gain political power even though the Malays, who are mostly rural based, are relatively poorer than the other two groups. At the same time, the country made major investments on education, health and productive enterprises to achieve high level of economic growth and to reduce the incidence of poverty. The result has been a remarkable achievement in economic growth and poverty reduction over 20 years. Malaysia reduced poverty from 50 percent in 1970 to about 10 percent in 1990. The Country also avoided potential inter-ethnic and intra-ethnic inequality and conflict in the process. (IBRD, 1991, P.131). Ethiopia can do the same by adopting proper democratic institutions tailored to her culture and ethnic composition.

The above examples are to simply point out the problem with the political injection of ethnicity into federalism. A political reform that retains a system of multi-ethnic decentralization is a more viable option.

Under such a democratic federal institutional structure, the traditional provincial system can be retained or regions can be re-named geographically such as northern, northeast, southeast, midwest regional states, for example. The other alternative may be to simply use the existing provincial or zonal names.

It is also important to realize that the ethnic issue can be used as a political tool in a two totally opposite ways. One would be the suppression of the human need for free cultural and linguistic expression and ethnic identity in the name of national unity, and the other through a top-down creation of a structure under which political elites can exploit ethnic and linguistic differences. Both of these are a direct result of the problem of concentration of power. Ethiopia has experienced both. They are best resolved through a form of democratization that devolves political power to regions and local communities on a multi-ethnic basis.

A sustainable institutional reform on the ethnic issue in Ethiopia may have to follow an open and free public debate and dialogue on key policy issues by all parties concerned, such as civil society organizations, prominent individuals and independent scholars, and aspiring political groups and individuals. Such a dialogue should be inclusive, civil, honest, and peaceful. It should be a constructive dialogue aimed at addressing key public policy issues of alleviating mass poverty and sustaining unity within diversity, democratic justice and peace. It is unlikely to succeed by simply bringing together young and inexperienced political cadres of various political parties, with out including civil society group leaders, independent scholars, religious leaders, and local elders with long institutional memory and experience.

¹² For example, it is estimated that there are more Polish people in the City of Chicago than in the city of Warsaw, Poland simply by choice and circumstances, not because of any Constitutional or political mandate.

The role of local elders and leaders of faith-based institutions is especially crucial in such a conflict prone process. Local elders have traditionally been crucial in resolving conflicts among Ethiopians. It is necessary for all the stakeholders in Ethiopia to engage in this important process based on the experience of the past ten years.

In a comment received in the earlier draft of this paper, the following questions were raised: *Is the Ethiopian society a viable society after the experiences of the last 30 years.. Can the current challenges by ethnic- nationalist intellectual and political elites to the viability of Ethiopia as a nation state be underestimated? Are not the arguments for democratic institutional development and reform secondary to ethnic nationalism in general, and Oromo nationalism in particular?*

These are important questions for which there are no simple answers. It is a fact that Ethiopia has overcome many internal and external challenges through its long history. There is no reason to believe that future challenges will not be met if Ethiopians unite across ethnicity for the common good. But, the problem of ethnic nationalities in Ethiopia can be resolved by adopting democratic institutions based on the protection of individual rights and the rights of minorities and majority ethnic groups. The ethnic-national problem in Ethiopia is a disguised form of lack of democratic institutions, which guarantees the rights of individuals within their respective communities. For example, the Oromo national problem is best resolved by a true democracy based on “one person one vote” that automatically brings the majority to power. Other multi-ethnic societies such as Malaysia have done that, which also enabled them to significantly reduce poverty under democratic institutions. The Oromo people like many other peoples of Ethiopia have intermingled with other ethnic groups for generations. They have also played crucial role in the building of the modern Ethiopian nation state. Contemporary Ethiopia is not ancient Abyssinia. There cannot be a viable future state of Ethiopia without the Oromo people. Indeed, the modern Ethiopian state would not have been possible without the role of Oromo historic figures such as Fitawerari Habte Giorgis, Ras Mekonnen, Dejazmach Balcha, Ras Abebe Aregay etc., who have played crucial role in the state formation of Ethiopia over the last hundred years¹³. The challenge is to resist or correct the historical distortions and interpretations that demonize the role of such individuals in the formation of the modern Ethiopian state, and to advance the causes of democracy and equality within united Ethiopia in order to solve current and future problems.

Modern Ethiopia is a result of a long process of historical formation, a process shared by many nation states around the world. It is a multi-cultural society created out of centuries of war and conflicts and “grand failures” of institutional transition¹⁴. Ethiopia is also a nation that has evolved by shared experiences, trade, cooperation, mutually beneficial political alliances, and inter-marriages.

¹³ Individuals from other ethnic groups such as the Amhara, Tigrai, Gurage, Sidama, etc..have also historically played important roles in the formation of multi-ethnic modern Ethiopia.

¹⁴ See a paper by Merera Gudina entitled, “ The Elite and the Quest for Peace, Democracy and Development in Ethiopia: Lessons to be learnt” in *Proceedings of the EAF International Conference on Contemporary Development in Ethiopia*, Western Michigan University, November, 2001. This paper characterizes the political evolution of modern Ethiopia into “five grand failures”, which can be regarded as failures of institutional reform and transition toward democratization, according to views expressed in the current paper.

A recent book on the history of Ethiopia describes this historical process as follows: *“Historically, Ethiopia and its neighbors have lived together fruitfully when ideological and ethnic concerns have been muted. When, however, religion, politics, or economic factors have become dominating and unbalancing, the entire region has fallen into mayhem. Should the region split apart, the Era of the Ministates will make the Age of the Princes appear as a golden epoch! It may take several generations before the logic of geography and history works to recreate the larger political and economic sphere necessary for better future. In the end, Ethiopia will rise.”* (Marcus, 1994, P.220). It is important to draw useful lessons from history to avoid further internal balkanization and to forge regional economic cooperation in pursuit of peace and better future for the peoples of the region. For example, it should be clear that the break up of Eritrea and Ethiopia in 1993 has not produced prosperity, democracy, and peace that we were led to believe by Eritrean nationalist political elites¹⁵. Instead, what has resulted in the short history of the Country’s existence, is more misery and dictatorship that has led to a two-year vicious war and destroyed the lives of thousands of people in both countries. A recent book on the war describes it as follows. *“Isaias Afewerki sent his army unannounced across the border into Ethiopia in the first days of May 1998 and provoked a confrontation that turned into a war. When it reached its final stage in May-June 2000, this war briefly had the distinction of being the largest war anywhere in the world at that time. Fortunately, Ethiopian military prowess brought it to a swift end”* (Henze, 2001. P.VII).

Toward a Land Reform for economic development and poverty alleviation¹⁷:

The second policy area that calls for reform and action aimed at economic development and poverty alleviation in Ethiopia is that of land tenure. The 1975 land reform has not adequately answered the burning question of “land to the tiller”. The farmers of Ethiopia do not have a secure access or ownership of land, since land constitutionally belongs to the state, as it did during the Derg period. Such undefined and insecure property rights have negative effects on agricultural production and environmental protection. Since farmers do not have security of tenure, they are unlikely to invest on the land or to protect the soil by planting trees. They would have no *incentives* to do so. Would you take care of an automobile you lease or a house you rent the same way as one you own? Most people do not. Again at the very least, the land question should be addressed with serious empirical research.

¹⁶ For a perspective on Eritrean nationalism see, Mesfin Araya’s paper, “Nationalism as A Contingent Event: Some Reflections on Ethio-Eritrean Experience”, in the *Proceedings of the EAF International Conference on Contemporary Development Issues in Ethiopia*, Western Michigan University, November, 2001.

¹⁷ Some of the views in this section should be regarded as hypotheses that need to be empirically verified based on the actual data and realities in Ethiopia.

Currently, there is a dearth of empirical research on this issue¹⁸. There is a lack of clearly defined property rights in land or absence of formal legal markets both in urban and rural areas. This has resulted in illegal land markets and transactions, where land is “sold” in disguise through housing markets, leading to inflated housing prices in cities like Addis Ababa. If the government legalizes land markets, housing prices are likely to decrease since home construction is likely to rise. This will also reduce urban unemployment and poverty, and decrease home prices, and make housing affordable to citizens. This is again an institutional and public policy question that cries for reform. It should not be rigidly retained or defended for political and ideological reasons. The land policy also directly contradicts with the officially stated objective of the free market system, since capitalism is not possible without property rights including land rights vested in the private sector and citizens. In the rural areas, there are emerging land markets, which can simply be formalized by giving these markets legal or formal status. The question here may be how to privatize land in rural areas. This can be handled by simply securing the legal ownership of current holdings that have evolved since 1974/75 Land Reform with no further redistribution. The inequality of land holdings that may have evolved over this period, would not be a significant. Moreover, it is a result of voluntary transactions among farmers. This, again, is an issue that further empirical research can fully address.

One of the main arguments against giving farmers land ownership is the same one made during the Derg. It is the notion that if land is given back to farmers and formal land markets are permitted, this will bring back land concentration or the absentee landlords. This argument is flawed for at least two reasons: First, it undermines farmers' ability to make decisions in their best welfare by imposing a decision on the farmer in elitist manner. But, the reality is that farmers are revealing their true preferences and choices by engaging in informal land markets including rental markets.

Second, it assumes that the federal and regional governments cannot enforce laws and regulations that prevent land concentration or absentee landlordism, or that it does not have other policy instruments such as land taxation to prevent extreme land inequality or concentration. In assessing likely impact of state ownership of land during the post-Derg period, a scholar who has conducted substantial research in land issues in Ethiopia noted, “*I believe therefore that, though the political climate has changed to some extent, state ownership of land will recreate the conditions that made interventionism, management by fiat, land evictions and rural corruption possible in the Derg period*” (Dessalegn, 1994, p.2)¹⁹.

¹⁸ The few studies on land reform and land policy underscore the need to provide security in land vested to individual citizens and their communities. See for example, “Land Tenure and Land Policy in Ethiopia After the Derg”, *Proceedings of the Second Workshop of the Land Tenure Project*, edited by Dessalegn Rahmato, Working Papers on Ethiopian Development, N0,8,October 1994. Center for Environment and Development, The University of Trondheim, Dragvoll.

¹⁹ Dessalegn also proposes land reform vested in communities and individuals in what he calls, “associative ownership”, See Dessalegn, 1994, p 13-16.

In general, the current debate on land policy is influenced by three notions: 1. The fear of opening land markets that may lead to land concentration, 2. The need for land entitlement to meet food security needs of the farmer and reinforces state ownership of land. 3. The search for “equitable but efficient land tenure” centered on market-based land tenure system with a potential to contribute to agricultural transformation required for economic growth²⁰. The problem of the pre-1975 land policy was due to the inability and unwillingness of the government of the period to regulate extreme land concentration by applying policy instruments such as taxation to prevent land concentration and inequality. It was not a problem of private ownership of land. Not only does the current system undermine the regulatory or protective role of the government, but it also denies the state to collect public revenues from land or property taxes. More significantly, the system undermines the productive and sustainable use of land by discouraging investment and the protection of land resources such as soils and forests.

Ethnic Federalism, Land Tenure, Economic Growth, & Democratic Institutional Building: Are there links?

Ethnic federalism and land tenure are both linked to economic performance in terms of their potential impact on economic efficiency required for economic growth. Ethnic federalism affects efficiency by its potential to impede the mobility of labor and capital required for economic growth. For example, if a Gurage entrepreneur wishes to invest in the current Somale, Amhara, or Oromo regional states, he may not be confident to do so. But, investment activities of the individual concerned may significantly contribute to welfare of the people concerned regional state economy. This is not to suggest there are formal regulations or laws that prohibit cross-regional investments, but to simply point out that the structure of ethnic regionalism may provide incentives for local political elites to impede cross regional investments and/or to extract bribes from such outside investors. Similar impediments may exist in mobility of other forms of labor such as professional labor. So, the structure has the potential to contribute to economic stagnation or decline in some ethnic regions or *killils*. Whether this is actually happening is subject to empirical verification, but simple common sense and scant evidence suggests it is likely to be the case. Ethnic federalism also contributes to the lack of democratic institutional building, since political cadres may monopolize regional and local power by manipulating ethnic differences and by preventing the emergence of spontaneous democratic institutions and freely elected local and community leaders. This becomes a serious problem specially if political power is concentrated at the federal and regional levels that may prevent free political competition at the local and community levels.

Land tenure is also linked to democratization and economic growth. Private ownership of land contributes to efficiency in land use and agricultural growth. In the current state of agriculture, which is characterized by smallholder farming, the prevailing land policy creates what economists call *agency* or *principal-agent* problem, which arises from incentive problems of separation of ownership and management or use of land.

²⁰ See Tesfaye Teklu's paper, "Emerging Informal Rental Land Markets: A Quest for Equitable But Efficient Tenure Systems" in the *Proceedings of EAF International Conference on Contemporary Development Issues in Ethiopia*, Western Michigan University, Kalamazoo, November 2001.

The State becomes the monopolist owner of land or the only “land lord” or the *principal* in this case, and the farmer becomes the *agent* or the “tenant” of the state. A serious incentive problem is created since the farmer would have no incentive to take care of the land and soil by undertaking activities such as tree planting or making other appropriate investments. This would contribute both to production inefficiency and land or soil degradation. Moreover, the resulting absence of land markets locks farmers to inefficient use of land and prevents enterprising farmers to acquire more land to increase agricultural production. Of course, other factors such as improved technology, extension services, and appropriate price policies are important contributing factors. But, the presence of land markets is critical in taking full advantage of these other factors.

In addition to its impact on agricultural development and on economic growth for Ethiopia, state ownership of farmland has a serious impact on democratic institutional building. Under the existing land policy, farmers lack the economic power grounded on property rights to counteract the possible abuses of power by regional and federal officials. Farmers become, in effect, the tenants or employees of the government. So, it is impossible for them to form independent local community organizations that represent their interests or protect their welfare. In absence of political representation, farmers who challenge central or regional government policy or officials may simply be denied of land and therefore their livelihoods. So, the state can have an effective control over the political behavior and choice of farmers similar to its effective control of civil servants or government employees. This is why totalitarian regimes such as the former Soviet Union have historically denied ownership of land to their citizens and farmers i.e. it was consistent with their command economic policies. However, such land policy in addition to leading to economic stagnation, cannot be even be sustained politically in the long run, as demonstrated by the collapse of the former Soviet Union and most other such command economies. Democratic institutions and political parties that truly represent the interests of farmers, which is currently 85 percent of the population in Ethiopia, cannot emerge or grow under the state ownership of land. This may be why there is a lack of political parties that truly represent farmers’ interests in Ethiopia. The potential adverse consequences of opening up land markets such as short-term unemployment or migration can be addressed by promoting rural industrialization and providing private investment and employment opportunities in the non-farm sector.

The Appropriate Role of Government in a Market Economy

In the process of transition to a market economy, it is important to be clear about the appropriate role of government. Economies around the world have stagnated or declined because of both *market failure* and government or policy failure or both. Areas of market failure are those where the private sector cannot be relied upon to deliver goods and services such as in the areas of public health, public education, agricultural research and environmental protection. The proper role of government includes the provision of legal and institutional structure that support private sector and markets, as well as investments on public goods such as roads, public education and public health services. Government also has a legitimate role in rectifying extreme inequality of income and wealth through progressive taxation , not through confiscation or nationalization of wealth and property.

The prevention of *negative externalities* in terms of protecting of environmental damage such as the prevention of soil erosion and deforestation is an appropriate area of government activity. In general, a market is an institution that presumes that a government can keep law and order, enforce contracts, define and secure property rights, and provide for stable monetary framework. (Friedman, 1982)

The current *Agricultural Led Development Industrialization* (ALDI) strategy adopted by the Government of Ethiopia is generally the right strategy due to the dominance of agriculture in the country's economy. But, it is unlikely to succeed in transforming agriculture without policies and institutions that provide the security and access to farmland to enterprising farmers and to private investors. Problems of natural resource degradation such as soil erosion and deforestation are also best addressed by policies that provide security of land holdings vested to individual farmers and local communities in order to provide *incentives* to farmers to plant trees and to protect the soil by investing on land.

The role of the government is analogous to role of a referee in a sports game such as football. If the referee also becomes a player or tries enforcing the rules impartially the game will not be successful or the outcome of the game will be unfair. In extreme cases, fights may break out that stops the game. The key problem in such environment is to design institutions, which both enable and constrain a government to serve as an impartial referee in the economic game just like in sports game (Asefa and Reinert, 2001). Economies that fail in this regard suffer from *corruption* and *rent seeking*. They are those where the government has abdicated its role of being impartial and competent referee in the economic game. The critical issue here is the development of the rules of the game (institutions) that allow for the competent referee (i.e. a capable government) to emerge, and for changing the referee (i.e. power transfer). Such rules or institutions must be negotiated and agreed on by all interested parties. The market reduces the range of decisions that must be made by political means, thereby minimizes the extent to which the government needs to participate directly in the game.

Corruption and rent seeking activities in such environment cannot really be eliminated by punishing those that engage in corruption. Combating corruption is an institutional problem of designing the rules of the game with transparency and accountability. Corruption involves the illegal perversion of public assets and institutions for private benefit. It is best prevented by the rule of law with checks and balances, independent justice system, overseen by the free press that exposes corruption to the public. For example, in mature democracies such as the United States, elected public officials must declare their private wealth and place it into blind trust by law, in order to avoid a possible conflict of interest and corrupt behavior during their tenure in office. Economic power must be separated from political power to avoid corruption and to protect the freedom of citizens.

For markets to function and to enhance economic growth and development, goods must be produced supplied and demanded or sold. In a developing economy such as Ethiopia, production is critical. It allows for employment or income generation required to combat the poverty problem. But, for productive employment to occur, farmers and business entrepreneurs must invest on productive activities. Domestic investors should be given the level playing field under a fair institutional and legal system that both promotes and protects private investment.

Foreign investors can only be attracted if there is an investment climate that is less risky and allows them to make fair profits or provide a fair return on their investment. Most investors would not spend their money if they can get a better return elsewhere or face a lower risk of losing their money.

Anti-private sector and business sentiments often come from a narrow focus on *profitability* and failure to realize or to understand the other critical social functions of the private sector in modern economies in areas such as employment, training, and technology transfer, and philanthropic contributions.

Ethiopia is currently fortunate to have a massive injection of financial capital into the private sector by a single international investor and philanthropist, Mr. Mohammed Al-Amoudi. Several thousand Ethiopians are employed in his various MIDROC enterprises. According to recent report, MIDROC comprises of over 30 different companies and employs over 60,000 Ethiopians (Addis Tribune, September 14, 2001). Ethiopia should be highly thankful to his generous investments and charities. But, there is currently only one such person. Ethiopia needs to attract more foreign investors by creating an enabling institutional climate for massive international investment. Investment in agro-business and tourism are among key areas of such investment.

A discussion on economic reform cannot be complete without referring to the role of World Bank and the International Monetary Fund (IMF). These organizations have limited influence over the institutional environment of a country. But, their primary stated goal is to help promote economic reforms that make markets work aimed at enhancing economic growth and opportunities. The World Bank have given high marks to the Government in Ethiopia for adopting Structural Adjustment Programs (SAP)²¹. But, this does not consider whether the basic institutions that can support the market economy and sustainable economic growth are in place. Privatization and liberalization outcomes are not sufficient to create a working market economy. It is not enough to get prices right or even policies right. *Getting institutions right* is crucial²². If the basic institutions that support markets and private economic activity are absent or are not allowed to evolve, SAP and the related economic liberalization policies will have no effect or they may actually increase the level of poverty and inequality. Moreover, privatization can be abused or corrupted by the possibility that the same persons that run the state political machinery may also run or own the newly privatized firms. State owned monopolies may be converted to private monopolies with no transparency. So, the success or failure of the structural adjustment program (SAP) in reducing poverty critically depends on the institutional environment of a country that provides an effective and clear demarcation of economic decision making and political decision making.

Democracy is an evolutionary process that takes time to grow. It is a process of solving political and economic problems through peaceful dialogue and compromise. It must be nurtured and allowed to grow like a plant or a tree.

²¹ World Bank chief economist Nicholas Stern has recently praised Ethiopia's efforts toward a poverty reduction, a concept that now underlies most of the Briton Woods institutional lending. See *South Africa's National Financial Daily Business Report*, 21 October, 2001. See also the article entitled, "Thanks for Nothing" by former chief economist of the Bank, Joseph Stiglitz in the *Atlantic Monthly*, October 2001.

²² The entire volume of World Bank's most recent popular publication, *World Development Report 2002*, is devoted to the theme of "Building Institutions for Markets"

It must be adapted to a country's tradition and culture and draw from the experiences of other countries with working democracies. Institutions that support democracy and the free market system must be allowed to evolve. It is in enlightened self-interest of all stakeholders in Ethiopia, which includes the Government, the various opposition groups, civil society organizations and individuals to work together and allow democracy and the free enterprise system to grow by pushing forward for a peaceful democratic political and economic reform.

There is also a need in this regard, to begin the practice of peaceful and constructive partisan power politics. For this to occur, politicians must learn to change from a negative sum or zero-sum to positive-sum thinking mode of thinking. Specifically, the current political climate of Ethiopia must accommodate both the opposition parties and the ruling party under a level playing field. Such a view may be currently unpopular. But, the best way to move forward in the long run will be with an inclusive exercise of politics. There should be an institutional framework that allows all those who are part of the problem to also be part of the solution.

An institutional environment that moves away from a zero-sum or dysfunctional politics toward an environment which gives a clear voice and choice to the *silent majority* (both rural and urban citizens) based on peaceful political competition with proper checks and balances established under the rule of law, should be created. Political parties should be formed based on interest groups and policy differences by free association of citizens across ethnic lines. For example, since about 85 percent of Ethiopians are engaged in farming and related economic activities, why is there a dearth of political parties that truly express the interest of farmers? What this question refers to is not to political parties that claim to stand for farmers or the "masses". Even the Derg has done the same thing by claiming it stood for the "masses", which it used as cover or excuse to suppress dissent and freedoms of Ethiopians. What this refers to is the need for spontaneous political organizations rooted in local farm communities with significant influence on regional and national or federal level policies. It may well be that such pan-Ethiopian institutions are emerging based on experiences and the limitations of ethnic federalism of the past decade. It is in the interest of all constituents including current ruling party, the opposition, and civil society group to allow them to evolve peacefully.

Frankly, what may be required for a true democratic institutional building in Ethiopia is the emergence of at least one strong peacefully organized multi-ethnic political party that effectively competes in an open and free election with the ruling party in the next and future elections. Multi-ethnic parties are most viable in the long run, since ethnic based parties are likely to degenerate to inter-ethnic and intra-ethnic conflict as they have done during the last decade. But, opposition ethnic-based should also be allowed to exist and compete in their merit. The efforts of an opposition multi-ethnic party (s), if and when organized, should not be wasted on attacking the current ruling party programs and its leaders. Instead, it should be focused on building programs and policies that provides policy option for the Ethiopian people to choose. The ruling party should allow such party(s) to peacefully emerge and to function freely. It is in the interest of enlightened leadership to allow the devolution of power to local communities in order to create a level playing field for such a loyal opposition party(s) to emerge peacefully.

This would create an institutional mechanism for peaceful political competition and transfer of power. The outcome of such process would also advance the causes of democratic institutional building and result in a positive outcome for all constituents. It would be good for civil society groups, the opposition, the ruling party, and for the Ethiopian society in general. The alternative would be unsustainable in the long run. It is likely to repeat the institutional failure of transition of the past with unknown consequences. The development of such political culture is not just a problem of institutional design and development. It requires changes in behavior of individuals and organizations, including those in power and those that aspire for political power, to learn to be tolerant of diverse views, and to adopt the virtues of honesty, integrity, and accountability in their actions. It also requires for citizen and civil society leaders to stand up for the basic principles of decency, fairness and justice, and for citizens to defend them when such civil rights and liberties are violated.

What are the prospects for institutional reform in light of the experiences of the past decade? First, if the potential problem of ethnic federalism is addressed along the movement toward peaceful political competition, there may be a chance for a democratic institutional reform, and that the failures of transition of the past can be avoided. Second, the way to avoid possible future ethnic conflicts and retribution is to strength individual rights of all Ethiopians regardless of ethnicity, and to protect these civil and individual rights with the rule of law and constitution that also secures the rights of majority and minority ethnic groups. This author does not believe that the Ethiopian society will degenerate into ethnic cleansing that has unfolded in some societies such as Rwanda and Burundi, provided democratic institutions are built. Third, there are some institutional and economic improvements since the fall of the Derg in 1991 that should be acknowledged, sustained, and built on. These include the emergence of private initiatives and businesses, several independent newspapers²³, the resolution of political dissent through non-violent or peaceful means, the recent transfer of the largely ceremonial power of the Presidency, the recent reported relaxation of press restriction²⁴. Although the recent peaceful transfer of power from of the Presidency was perceived to be controversial, it is a step forward in the direction of the institutionalization and de-personalization of this office²⁵. Although much remains to be done, these are important incremental changes that can be the basis for democratic institution building.

²³ Several independent private newspapers have emerged since 1991. Papers such as the *Addis Tribune*, and *The Reporter* are among the successful ones.

²⁴ See the news article in Integrated Regional Information News (IRIN), by the *United Nations Office for Coordination of Humanitarian Affairs*, 11 October, 2001.

²⁵ The recent decision to provide the outgoing president, Dr. Negasso, with a pension and a home contributes to future institutionalization of this office by providing the incentive and security needed for peaceful transition of this office.

It is easy to undermine or trivialize these changes by focusing on individuals involved in the process, but it is important to realize that the culture of non-violent political dissent²⁶, independent press has never existed in the long political history of Ethiopia. But, the democratic institutional challenge of effective diffusion and peaceful transfer of power that allows for the institutionalization and/or de-personalization of key political offices required for sustainable democratic governance, still remains.

The Role of Informal Institution and Culture

This paper has so far primarily focused on the role of formal institutions for economic development in Ethiopia, with the belief that it may be easier to change these under a visionary leadership than to change culture and *informal institutions*. But, the role of informal institutions can be just as important. Informal institutions are unwritten rules of society such as culture, norms of behavior, and code of conduct.(Yeager,1999). Ethiopia is rich with such informal institutions and culture that span various aspects of social and economic life. They consume a large part of the daily social lives of Ethiopians. These institutions such as *Mahber*, *Edir*, and *Ekub* are indigenous institutions that have served important socio-economic functions ranging from savings (*ekub*), insurance (*edir*), and community self-help (*Edir*). Many of these institutions can be developed or adopted to formal institutional building, and should not be undermined by formal institutions. When there is a failure of formal institutions including states, these informal institutions keep communities in tact and viable. Some societies in Africa may be better off with informal institutions than a disabling formal state institutions. For example, it is noteworthy to point out that informal institutions in northern Somalia, appear to be working far better than during the days of the former President Said Barre, when the state of Somalia was in tact.

This is not to say that all informal institutions and culture are compatible with economic development. In Ethiopia, a large number of cultural ‘holidays’ compete with time that citizens can spend on productive economic activities. A hard working entrepreneur in Ethiopia pointed out to me, sometime ago, that he finds himself at odds with members of his family and his friends since he rarely attends social functions such as funerals, weddings, since these functions compete with the time he needs to creatively think and work on his business. So, he sometimes chooses to send his wife to such social events to the dis-satisfaction some of his friends.

Another cultural factor that blocks democratic institutional building is a simple lack of trust and flexibility among Ethiopians. Specifically, there is a serious behavioral problem of inability and unwillingness to tolerate a different point of view from one’s own. Some one has once said, “ we all seem to carry a little “zewd” or crown in our individual pockets!”

²⁶ It is noteworthy to be reminded that political dissent such as the one that occurred within the ruling party would have led to the possible killing of some members of the dissenting group during the Derg period. The fact that this purge was handled relatively peacefully is not a trivial event given in the recent violent political history of Ethiopia. For full political analysis of the nature of the recent dissent within the ruling party see the article, “Ethiopia, the TPLF and Roots of the 2001 Political Tremor” by Paulos Milkias, 2001.

This lack of tolerance along with a culture of cynicism evident in the Amharic saying “*Yalteretere Temenetre*” (those who are not cynical or suspicious are doomed), makes a constructive political discourse required for democratic institutional building difficult. But, it is unfair to say that such personal traits, that have their origin in culture and family upbringing, are unique to Ethiopians. But, such cultural traits interact with formal institutions in a significant way. Specifically, when external *formal institutions* and alien ideologies are injected to society they make these informal cultural traits such as mistrust, cynicism, and intolerance much worse. They create political personalities and organizations that refuse to share power and decision making because they mistrust others, especially those who do not completely submit to them, thus making peaceful and constructive dialogue impossible. One example is the negative impact of the terror years of Derg over some of the political and intellectuals elites that have survived that period. This has contributed to a conflict prone and cynical mentality that prevents peaceful, open, and honest political dialogue aimed at solving political differences and conflicts. Yet, such personal and cultural traits are essential to build democratic political institutions

The Role of the Ethiopian Diaspora

The Ethiopian Diaspora is a result of exodus of Ethiopians after the fall of the Haile Selassie’s regime in 1974. It should be recalled that very few, if any, educated Ethiopians remained abroad after they completed their studies in foreign lands prior to this period. In fact, those that completed their studies abroad could not even wait until graduation to rush home in order to take up the attractive employment opportunities that was waiting for them back home at the time. (i.e. Their degrees were mailed to them.)

The large exodus of Ethiopians began after the 1976/77-terror period, as young Ethiopians fled from political atrocities of that period. While there is no study of the Diaspora that I am aware of, it may be several thousand strong just in the United States. Many members of the Diaspora have achieved various levels of professional success in the United States, and other nations around the world. There are successful professionals: medical doctors, scientists, academics, lawyers, and entrepreneurs. The Ethiopian Diaspora may be among the most successful of the African Diaspora. However, because of the traumatic experiences many have undergone, it is divided, cynical and unable to come together to form a united front for constructive purposes, especially in relation to Ethiopia.

Although there are successful community and non-profit organizations that appear to be emerging, the collective strength of the Diaspora cannot be fully realized unless members unite around the idea of human development. For this potential to be fully realized, the Diaspora should engage in constructive dialogue on the various dimensions of development such as education, health, agriculture, natural resources, private sector development, and find concrete ways to assist in the development process of the homeland.

On the other hand, a constructive and enlightened policy in Ethiopia should consider the Diaspora as an important resource for development. The Diaspora should not be viewed with suspicion or hostility. Rather, it should be considered as an important external resource of human and financial capital that Ethiopia can benefit from.

The Diaspora can also be an important source of brain gain or a way of reversing the *brain drain*. For example, it may take 16 to 20 years for Ethiopia to train a successful engineer, agronomist, economist, biologist, etc or even more years to train a medical doctor. But, such persons are already in the Diaspora. What is needed is to create an inviting and an enabling policy environment for such professionals, across ethnicity and political views, for their contribution. In the area of business, the Diaspora should be encouraged and invited to invest in Ethiopia. The Diaspora can also be a major source of information for foreign investors. It can assist in supporting private colleges and in strengthening existing public institutions of higher education. Members of the Diaspora can provide valuable services in supporting distance learning and education. But, there must be cooperation to make this possible. Those individuals and groups that take such initiatives should be supported and encouraged on both sides.

The Diaspora can begin such initiatives by organizing itself and building a sense of trust, unity and community as it tries to collectively engage the development problems of Ethiopia. Such initiatives are most successful if they are based on local Diaspora communities. Once the task of coming together around human development takes place, the rest is likely to follow. Other Diaspora communities around the world such as the Chinese and Jews for example have done so. The Ethiopians Diaspora can also succeed in this regard with much good will and hard work.

Concluding Remarks:

Let me conclude with some remarks that flow from the views expressed in this paper.

The economic and political development problem of Ethiopia has roots in conflict over the last three decades among few elites who are unwilling and unable to work together. It is a problem of institutional failure and lack of political development or maturity among a very few of the country's population (perhaps no more than 5% of the population). It is a problem of finding institutional mechanism for diffusion and non-violent transfer of political power. The vast majority of Ethiopians, called the 'silent majority' in this paper, are quite clear about what they want in life. The great majority of Ethiopians has lived in unity within diversity for generations. They want to continue to do so to combat the poverty problem. Ethiopia needs an intellectual and political leadership that clearly expresses the will of the silent majority, by focusing and solving present and future problems, instead of promoting endless conflict about the past. The past is important for development to the extent correct lessons can be drawn or learnt from it in order to solve current and future human and economic problems. It should not be a source of conflict, political extremism and confusion.

Ethiopian elites should refrain from the exercise of partisan power politics based on hate, blame, conspiracy, and character assassination. Instead, individuals and organizations should respect their differences and pragmatically work together in areas of common interest. Disagreements on key political and public policy issues should be openly debated and discussed. Such discussion should be focused on ideas and policies, not on individuals and groups, no matter how much one may disagree with. The culture of blaming or demonizing individuals and/or countries for primarily self-inflicted problems should stop.

This culture of demonizing individuals appears to be one of the major stumbling blocks to healthy political dialogue and democratic institutional building in Ethiopia. It should be re-focused on the challenge of facing up to real problem of building institutions that allow for dispersion and transfer of political power aimed at solving the real problems of the country such as poverty. Individual political actors and their organizations are victims of institutions they create, some times with good intentions.

There should be periodic conferences and symposia for the purpose of open, honest, and constructive engagement of key public policy issues. Such conferences and symposia should lead to a *national consensus* on key policy issues based on the respect of the rights of persons, civil society groups, minorities, as well the full protection of political parties (both the ruling and opposition parties), governed by the rule of law and a constitution that contains provisions for unity within diversity, justice and peace.

It may be necessary to revise or amend the existing constitution to clearly build provisions for checks and balances, unity within diversity, and peaceful transition of political power by open and free national and local elections. For this to happen the Constitution must incorporate the basic rules of peaceful political transition practiced around world's working democracies such as, for example, term limits for key political offices. Key elected offices should be de-personalized and institutionalized by providing for personal security and safety of incumbent officials under the law after they leave office. Such provisions should be incorporated into the constitution to enable future peaceful transition of power or to avoid violence in transition.

Ethiopian elites should begin united around the idea of development both in Ethiopia and abroad. There should be periodic conferences that engage in healthy dialogue and activities focused on the development of people as well as the preservation and the development of pan-Ethiopian culture among the youth. Such conferences and symposia should not be captured by partisan politics from whatever corner that may come from. They should, however, provide free forums of all individuals and groups regardless of their political views and association.

The current and future of governments of Ethiopia should consider the Diaspora as an important external national resource or human capital that the country can benefit from. Members of the Diaspora should be invited and encouraged to invest, to teach, to conduct research, and to engage in constructive tasks in their motherland.

Ethiopia should provide an enabling environment for domestic and foreign investors, by dismantling domestic institutions that block the mobility of labor and capital, such as top-down imposed institutions of ethnic federalism and state ownership of land. Ethnic federalism should be allowed to die naturally or a political means such as a national referendum that expresses a free will of the people should be found for it's replacement with a true form of federalism based on regions and sub-regions. Land markets should be legalized or the private ownership of land must be allowed in order for farmers and entrepreneurs to invest in agriculture, and for citizens to invest on homes and real estate.

The problem of economic development does not have a simple and clear answer. But, the adoption of market-based institutions to Ethiopia's conditions will have the best chance of success. Both the historical and the comparative experiences of the world's economies suggest that the development and use of market institutions have been most successful in reducing poverty. Ethiopia has already tried the alternative institution of command socialism with miserable results.

In one of the comments received in the earlier draft of this paper, the following questions were raised. *Which social force will apply the reforms suggested? Can the current government do it along the ethnic paradigm? Is there a tacit consensus in this regard?* The suggested reforms are possible under the current government. In fact, the arguments made here imply that reforms would have been possible under any of the recent governments of Ethiopia. But, reforms did not succeed because of the lack of institutions that allowed for diffusion and peaceful transfer of political power. However, the benefit of the doubt should be given to the current government to undertake institutional reform, since it is the only organized polity with resources to implement reforms. Whether it is willing and able to do so is an open question that remains to be seen. Such reforms should not only devolve power to regions and communities, but they should also allow and encourage the formation of peaceful political competition, pluralism, and institutions that allow the market economy to develop and enable the non-violent transition of political power among competing parties in a level playing field.

There must be a balance and fairness and at the same time a firm stand on democratic principles. The extreme and blind condemnation of what has been achieved over the last decade without suggesting workable alternatives on the one hand, and apologetic or uncritical support of these policies on the other hand, will not advance the cause of democratic institutional building in Ethiopia. It is more likely to retard it. Such a view may not be popular at this time, especially by those who hold extreme views on both sides. But, it is the responsibility of independent scholars, civil society and opposition groups to provide critical input and offer alternative suggestions on important matters of public policy in Ethiopia, in order to make this possible. It is not clear whether a consensus is emerging in this regard. But, if the current generation of political and intellectual elites can form a consensus that provides leadership and clear voice along these lines, Ethiopia may have a chance to become among the few African nations to lead what has been termed as an emerging African Renaissance of the 21st century. But, whether this will happen remains to be seen.

In conclusion, many ideas have been covered in this paper; with a hope some of them may contribute to development policy dialogue in Ethiopia. There is no secret or simplistic formula for human development in general and economic development in particular. Economic success occurs when people learn to be fair and just, to be considerate to others, to solve conflict peacefully, to be held accountable for efficient use of resources (private and public); and to abide by rules of behavior (called *institutions*) acquired over time by learning from past and from other successful nations, and through peaceful dialogue among independent parties. This is the process of institutional building that advances democratic economic growth and development. The alternative is an institutional failure of development and transition that results in economic failure as expressed by a development economist who wrote, “*Economic failures such as hunger, poverty, war, and unemployment are results of institutions that provide rationale people with incentives to behave in a destructive than constructive manner*” (Van Den Berg, 2001). The history of Ethiopia is full of such failures. Let us hope the future will be different.

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