

Creating Sustainable Development Zones in Ethiopia

Proposal for a bankable “SME City” pilot project as a model for optimized local governance for all social groups including Internally Displaced Persons (IDPs)

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EXECUTIVE SUMMARY / INTRODUCTION

UN Habitat is continuing its efforts to contribute to the work of the Ethiopian government, supported by the international community, to identify durable solutions for the rising numbers of IDPs in Ethiopia. Wherever returns to places of origin are not possible, these efforts have a special focus on upgrading, or, alternatively, redeveloping existing planned and informal IDP settlements to foster local integration. The following proposal is part and parcel of these efforts. It is about the redeveloping option.

According to the intention surveys available, local integration, with or without prior relocation, seems to be preferred by most of the over 2 million IDPs in Ethiopia. It is therefore the preferred policy option, at least for the purposes of this proposal. According to IOM figures¹, 90% of the IDPs live either with host communities and families or in spontaneous informal settlements in and around villages, towns and urban centers. It can be assumed that a significant part of these IDPs are already locally integrating, especially in places with similar socioeconomic and cultural characteristics. Approximately 10% of the IDPs are in more or less formal settlements or camps with so far little local integration. Practically all IDPs are depending on jobs in the informal sector of the economy and to a limited extent on humanitarian aid.

This dependency on the informal sector of the economy is not only typical for IDPs. It is also typical for millions of other Ethiopians living in informal settlements. This reality makes it important to widen the perspective: in order to provide dignity and economic opportunities, it is vital to formalize the informal livelihoods of all vulnerable groups by providing formal documentation, access to finance (“bankability”), land tenure, business skills and market linkages.

This becomes possible by widening the perspective even further and by better connecting the vulnerable groups in the informal sector with the “original” residents and, in particular, formal-sector housing and employment opportunities. Making this connection depends upon a conducive regulatory and administrative environment that reduces the difficulty of acquiring housing, accessing services, finding employment, and starting and operating micro-, small-, and medium-sized enterprises (SMEs) in the formal sector. As a result, the gap between humanitarian assistance and actual development could be bridged (fully in line with the government of Ethiopia’s exemplary policies when it comes to refugee-integration through the “Ethiopia Jobs Compact”).

To achieve this goal, this proposal foresees a pilot project in a defined area of approx. 500 hectares (ha) which would have a mixed population, including IDPs, and a mixed economic profile. Adjacent land should be available for future expansion of the pilot location.

In the defined area, a Sustainable Development Zone (SDZ) would be created. An SDZ is a significantly different project from conventional approaches. It involves the creation of a new special-status area with a special legal framework. An SDZ makes it possible to overcome the existing high barriers between the informal and the formal sectors and to come to a win-win situation for all groups including the municipality, the region, and the national government.

The SDZ pilot project would be called “SME City” to signify the importance of facilitating life for businesses and creating jobs in the formal economy, fully in line with Ethiopia’s Growth and Transformation Plan. The selection of the location of SME City, and potential subsequent SDZs, would be based on suitability criteria as explained in this proposal. A development

¹ IOM Displacement Tracking Matrix (DTM) Ethiopia, September-October 2018

company (“SDZ Developer”) would initiate the process by developing a plan for one or more locations that it presents to a committee with representatives of local, regional, and national government; civil society; and other international and domestic stakeholders. Subsequently, the committee would have the option to accept or decline the plan and form an agreement with the SDZ Developer.

To illustrate the SDZ concept, this proposal identifies three potentially suitable sites in the Oromia region, near the towns of Legetafo, Bishoftu and Sululta, all of which host existing IDP camps. The optimal site should be determined by proximity to infrastructure and labor, availability of land, legal and political considerations, and other factors. Further discussion with key stakeholders and analysis is needed to assess the suitability of these potential sites identified here and other sites.

The legal framework proposed for the SDZ builds on Ethiopia’s Industrial Park Proclamation and new supplementary legislation -- a “Special Administrative Areas Proclamation.” This new legislation would accommodate the unique competencies needed to form an effective SDZ, by allowing the SDZ to perform certain functions on behalf of the local, regional, and national governments. An SDZ would therefore be both an industrial park and a special administrative area (SAA). As an industrial park, the SDZ would benefit from certain legal privileges, especially regarding land tenure rules. As an SAA, the SDZ would develop institutions and procedures that are optimally suited for the development of a thriving formal-sector urban economy and society for people of all income levels.

The SDZ Developer for the pilot SME City would adopt a blended-finance approach including development financing with grants and concessional loans as well as private financing with Corporate-Social-Responsibility (CSR), social-impact and market-return-on-investment layers. In addition to the project proponents, government entities at the national, regional, and municipal levels, and SDZ residents would all have equity stakes in the SDZ Developer.

- The SDZ Developer would purchase the land lease from the government, develop a masterplan and cadaster, and provide for infrastructure and basic services. The SDZ would regulate activities within the zone and formalize the tenure of existing informal residents and informal businesses by offering registration, subleases, and business licenses subject to standards that are conducive to low-income communities.

The SDZ would be bankable primarily through the revenue generated by the subleases to residents and businesses, which should enable the Developer to generate a modest return on investment. The subleases would be subject to a regular reassessment and adjustment of the rental price to reflect true land value. By generating income, the project becomes an excellent opportunity for new partnerships between national and international investors, including in particular CSR- and social-impact investors, apart from the bankability of certain basic services and infrastructure packages.

Existing residents and enterprises of the area would benefit from an administration that overcomes the barriers to living, working, and operating successfully. Moreover, such residents would be shareholders in the SDZ Developer, entitling them to a share of its profit.

In particular, low-income residents (including IDPs, and others) and small businesses would benefit from formal documentation, legal protection, access to finance (“bankability”) and social services. Services would include education, social services, and skill development, including in new technologies, especially for young people and women. They would also benefit from affordable rents and access to rights and social services through one-stop-shop referral centres and social outreach mechanisms.

Municipality, region, and the national government would also benefit and generate substantially more revenue under this project than against the baseline. Their revenue would include profit distributions as shareholders of the SDZ, and increased tax revenue, especially if they decide to concede tax collection on their behalf to the Developer. In addition, and depending on the duration of the lease to the Developer, the SDZ could be seen as a build-operate-transfer project that will eventually fall back into the public domain in any case.

Given the now rapid rate of urbanization in Ethiopia and the profound changes in its socio-economic fabric, the proposed SDZ, if successful, could also serve as a model for optimized local governance and city management in an era of all-encompassing transformation. Such a model is needed all the more since it could prove that urbanization is not the problem, but one of the solutions to the IDP crisis and related crises.

Potentially, *scaled* SDZs could also serve as “building blocks” for national and regional urban planning and urban development in Ethiopia. This aspect is not discussed in this proposal, but it could be explored.

For implementation of this proposal, two next steps are recommended:

1. Development of a pre-feasibility study to present a detailed description of the project including its institutional, legal and political features and an indication of its economic and financial impact.
2. Obtaining “in principle agreements” from the relevant national and regional authorities.

For these two steps, a timeframe of up to 6 months is foreseen. After that, other steps would follow as explained in this proposal. For these steps a timeframe of up to 12 months is foreseen until establishment of the first SDZ.

CHAPTER 1: ETHIOPIA’S CURRENT POLITICAL AND SOCIO-ECONOMIC LANDSCAPE

Section 1.1: Positive Developments

Ethiopia underwent a peaceful power transition in April 2018.² The ascension of Abiy Ahmed as prime minister has ushered in a wave of national optimism. The new prime minister has moved quickly to open political space, promote human rights, and negotiate peace with neighboring Eritrea.³

Ethiopia’s economy experienced strong, broad-based growth averaging 10.3% a year from 2006/07 to 2016/17, compared to a regional average of 5.4%. Ethiopia’s gross domestic product (GDP) is estimated to have rebounded to 10.9% in 2017. Agriculture, construction and services accounted for most of the growth, with modest contribution from the manufacturing sector. Private consumption and public investment explain demand-side growth, the latter assuming an increasingly important role. Higher economic growth brought with it positive trends in poverty reduction in both urban and rural areas. The share of the population living below the national poverty line decreased from 30% in 2011 to 24% in 2016. However, Ethiopia remains one of the poorest countries with a per capita income of \$ 783.⁴

² See for this and the following: Draft ToRs for Solutions and Resilience Working Group for IDPs in Ethiopia, chaired by Ethiopian Government / NDRMC (“Draft ToRs for Solutions and Resilience WG”)

³ See for this and the following: Field Report from Refugees International / Mark Yarnell “The Crisis Below the Headlines: Conflict Displacement in Ethiopia”, November 2018

⁴ World Bank, “Ethiopia Overview”, available at <https://www.worldbank.org/en/country/ethiopia>.

Against this background, the new government is pushing Ethiopia's economic transformation from a state driven economy to a somewhat more liberal economy with space for the private sector. This move is based on the current Growth and Transformation Plan (GTP II 2015-2020)⁵, which pursues the country's vision to become a lower middle-income country by 2025, where democracy, good governance and social justice are maintained.

In the context of economic transformation, the country's socio-economic fabric is changing, in particular with regard to urbanization. The rate of urbanization in Ethiopia, compared with the average for sub Saharan Africa, is still low. However, the growth rate is one of the highest. Existing cities and new urban areas that emerged as a result of rapid rural and agricultural development are expanding rapidly. It is predicted that the country's urban population will triple between 2010 and 2040.⁶ This, on the not-positive side, has resulted in high unemployment, since neither the formal nor the informal sector of the economy can match the influx with jobs and livelihoods.

It is clear to all stakeholders that such rapid urbanization must be well-planned in order to unleash the opportunities it brings (at least in principle) to support growth, industrialization and structural change in the economy. To realize this, the government is aiming to arrive at integrated national and regional spatial plans covering all urban and rural development centers.

In this context, and relevant for the purposes of this proposal, Industrial Parks are seen as key for attracting both export-oriented Foreign Direct Investment (FDI) and domestic investment. GTP II states that "the expansion of special economic zones or specialized industrial parks with the required infrastructure and streamlined public procedures as well as fiscal and trade policy incentives to attract export-oriented FDI and domestic industrial investment, and clusters that provide the advantages of agglomeration will be given utmost emphasis."⁷ The Industrial Parks Proclamation allows for both public-sector and private-sector developed industrial parks. The public-sector industrial parks are developed and managed by the state-owned Industrial Parks Development Corporation (IPDC), which has two big parks currently operational -- Hawassa Industrial Park and Bole Lemi I Industrial Park. IPDC also has eight parks that are upcoming and in different states of development -- Dire Dawa, Adama, Mekelle, Kombolcha, Kilinto, Arerti, Bole Lemi II and Debre Berhan).⁸

Notably, GTP II anticipates the establishment of medium-size industrial parks at the regional level, which will be based on the experiences and in collaboration with the industrial parks at the federal level. These parks are mainly foreseen to serve small- and, in part, medium-scale industries owned by domestic investors and entrepreneurs. Regional governments and city administrations are called upon to construct such medium size industrial parks, supported by "innovation technology incubation centers" for training and research, in selected towns and cities. Special financing programs including micro finance institutions are foreseen to provide credit for the youth, women and domestic investors who will work in medium size industrial parks.

⁵ See for this and the following: Federal Government of the Democratic Republic of Ethiopia, Growth and Transformation Plan II (2015/16-2019/20), Volume I: Main Text, National Planning Commission, Addis Ababa, May 2016 ("GTP II")

⁶ United Nations 2014. World Urbanization Prospects: 2014 Revision. United Nations Department of Economic and Social Affairs. New York, New York.

⁷ GTP II, page 106

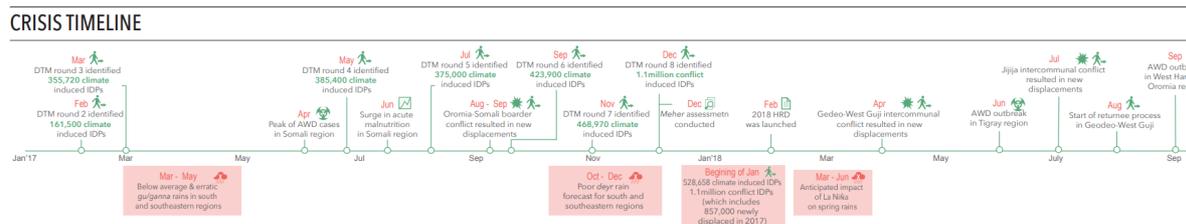
⁸ Ethiopia Investment Commission, "Extensive Development of Industrial Parks"

<http://www.investethiopia.gov.et/investment-opportunities/strategic-sectors/industry-zone-development>

Section 1.2: Pressing Humanitarian Concerns

The socio-economic fabric of Ethiopia is not only changing with regard to the ongoing economic transformation and rapid urbanization. Sadly, conflicts between different communities recur intermittently, affecting an increasing number of Ethiopians.⁹ Since 2016, inter-ethnic and inter-regional violent communal clashes have escalated, particularly along the border areas of Amhara-Tigray, Benishangul Gumuz-Amhara, Somali-Oromia and SNNPR-Oromia regional states. In addition, large segments of rural communities in North-eastern, Eastern, Central and South-eastern parts of the country have been striving to recover from severe droughts and floods associated with El Nino, La Nina, and Indian Ocean Dipole weather phenomena from mid-2015 through 2017. The intensity and frequency of both man-made and natural disasters have sharply increased affecting the well-being of millions of Ethiopians.

One of the adverse effects of these recurrent disasters is the rapidly increasing number of Ethiopians who are being forcibly displaced from their homes, land, assets, livelihood and community, known as Internally Displaced Persons (IDPs). According to the International Organization for Migration’s (IOM) Displacement Tracking Matrix (DTM), the total number of IDPs increased from 291,104 in July 2012 to 2.8 million in July 2018. Recent DTM figures are lower, but still over 2 million.¹⁰ 80% of the current IDPs in Ethiopia are conflict induced. For example, the recent Gedeo-Guji communal conflict in March 2018 and the Oromia-Somali border conflict in August-September 2017 have displaced 958,175¹¹ and 857,000¹² people respectively.



Source ACAPS

To add to these challenges, Ethiopia serves as a generous host to almost 900,000 refugees, primarily from neighboring South Sudan, Somalia, and Eritrea.¹³

Can the positive developments regarding peace and prosperity including the reduction of poverty be leveraged to find durable solutions for the IDP crisis -- i.e solutions beyond humanitarian assistance? If so, can such durable solutions contribute to the larger context of a society in transformation, and can the crisis possibly be turned into a development opportunity (similar to the principles guiding the “Ethiopia Jobs Compact”¹⁴)? The following chapters will address these questions.

⁹ See for this and the following Draft ToRs for Solutions and Resilience WG

¹⁰ IOM Displacement Tracking Matrix (DTM) Ethiopia, September-October 2018

¹¹ IOM UN Migration, “UN Migration Agency Releases Detailed Assessments of Displacement Sites in Ethiopia’s Gedeo, West Guji”, www.iom.int/news/un-migration-agency-releases-detailed-assessments-displacement-sites-ethiopia-gedeo-west-guji

¹² Ethiopia Humanitarian Disaster and Resilience Plan 2018, available at: www.humanitarianresponse.info/sites/www.humanitarianresponse.info/files/documents/files/ethiopia_2018_humanitarian_and_disaster_resilience_plan_2.pdf

¹³ See UNHCR Ethiopia Country Refugee Response Plan, January-December 2018

¹⁴ World Bank, “Ethiopia Jobs Compact Project”,

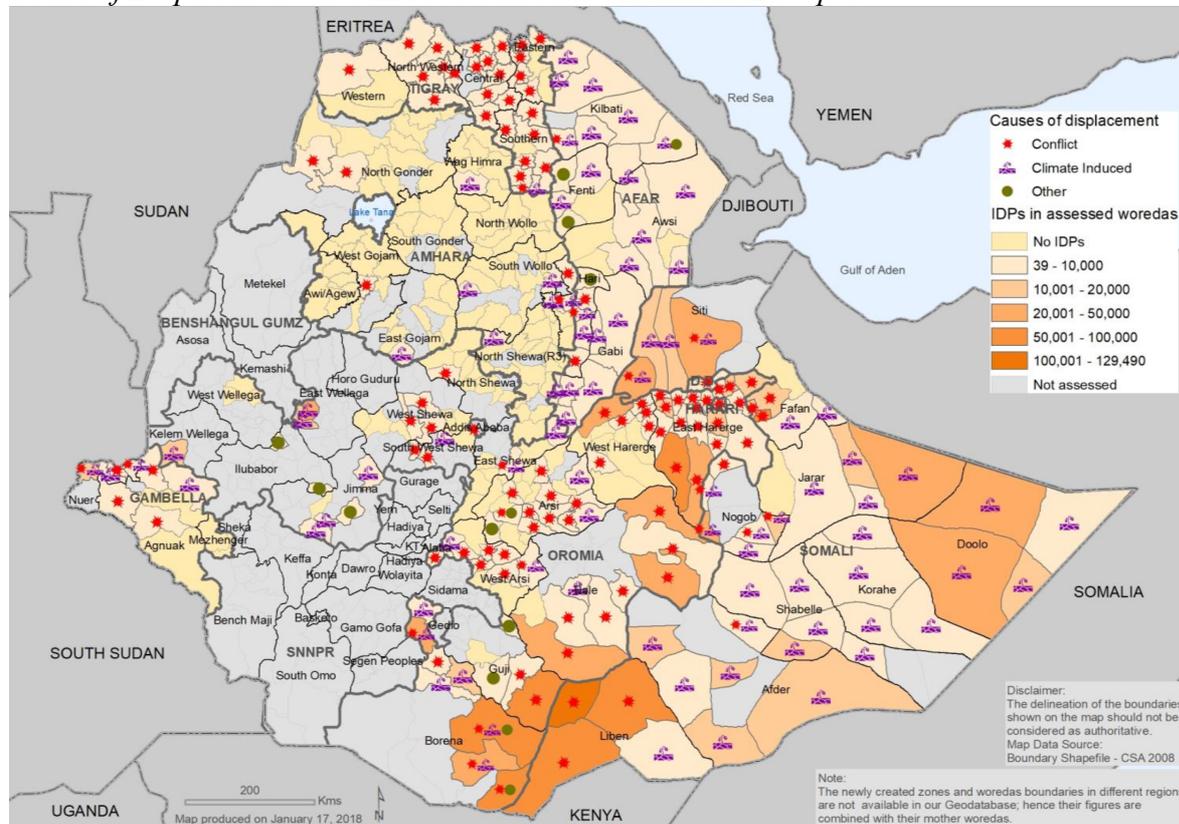
<http://documents.worldbank.org/curated/en/580241499855149882/Ethiopia-Jobs-Compact-Project>

CHAPTER 2: CHARACTERISTICS OF EXISTING DISPLACEMENT

Section 2.1: Geographic Distribution

Internal conflict related displacement is occurring in mixed settlement areas often in or near the population centers, providing opportunities to traders and service providers from all regions of the country. Displacement is linked to ethnicity but clearly also to economic competition, exacerbated by protracted drought and shifting seasonal patterns. The main areas of conflict and displacement are placed along the Great Rift Valley reaching the Tigray region at the border to Eritrea and in the Jijiga/Dire Dawa Axis where most of the Oromia/Somali clashes occurred. IDPs are accommodated in over 900 camps and settlements. More recent and active conflicts are occurring in the South with the Gedeo-Guji conflict in the border regions to Kenya and in the West at the South Sudan border. Refugees from South Sudan, Somalia and Eritrea are hosted in camps near the South Sudan border in the Gambella region, in Dolo Ado and Jijiga at the border to Somalia and the North at the border to Eritrea.

Cause of Displacement and IDPs in assessed woredas in Ethiopia



Source: IOM 05/10/20

Section 2.2: Drivers of Displacement and Mobility

Besides Natural Disaster-induced Displacement (NDID) closely related to the movements and needs of pastoralist communities (15% of the population) and direct Conflict-induced Displacement (CID), the phenomenon of Development-induced Displacement (DID) is an important factor due to the eviction of slum dwellers in the course of urban renewal, relocation of village populations during urban expansion, dam construction, commercial farm

development, and railway and road construction.¹⁵ The stressors for movement are therefore socio-economic as the ongoing transformation of the economy creates push and pull factors for populations and often induces conflict. If Ethiopia maintains its current rate of growth (3.02%), the population will cross 188 million by 2050 from approx. 108 million in 2018. Urban centers will double, from being the home to some 20.3% of the population to more than 40% of the population in 2030, leading obviously to additional tensions and resource competition along with greater wealth and prosperity. Therefore the current displacement situation in Ethiopia is multi-dimensional and requires solutions beyond a solely humanitarian approach.

IOM sees four main drivers of conflict-induced displacement¹⁶:

- Resource scarcity (through droughts, shrinking sizes of available grazing and cultivation land, pastoralists vs. farmers);
- Administrative border issues between regions, zones, woredas etc.;
- Cross-border (boundary) ethnic violence; and
- Conflict management mechanisms (challenges to mediation roles played by customary conflict resolution mechanisms).

Section 2.3: Socio-Economic Profiles and Related Needs

The socio-economic characteristics and core needs of IDPs and host communities differ, depending on the causes of internal displacement and the situation in the areas of the host communities and destinations.

IDPs displaced due to NDID are primarily pastoralists. They move either to other rural areas to seek assistance or work in wage-earning farming activities; to urban areas to seek government assistance or a new activity; or resort to begging. They need long-term assistance that can reestablish and develop their livelihood sources and build their community assets. Interventions should focus on building their resilience to natural disasters or to integration in new more sustainable environments, while paying attention to the mitigation of possible conflict. The skill levels as regards urban employability are generally low.

IDPs displaced by DID are the most invisible and the majority are affected by failures of institutionalized assistance and relief and are rarely receiving fair compensation for their loss of property or livelihood. Reinsertion and resettlement support when available, often results in significant economic household security decline as settlement and housing schemes offered are not providing easy access to services and economic opportunities. Their profile varies depending on the circumstances, but financial assistance, insurance systems, and access to legal aid have become critically important, in addition to the need for political and judicial accountability of those causing or expected to mitigate the impact of displacement. Many become informal settlers, squatters or move to slums.

In the case of CID, IDP's urgent and key needs revolve around physical security and the desire to avoid threats to their lives and physical well-being besides receiving survival assistance. Most have been displaced from peri-urban or rural village areas in the disputed regions, representing a wide range of basic skills, but often not adapted to the new more urban environments such as Addis Ababa, Jijiga, or Hawassa or other centers where many are

¹⁵ Edited Excerpts Working Paper- Stiftung Wissenschaft und Politik German Institute for International and Security Affairs , Mehari Taddele Maru

¹⁶ IOM Paper for Solutions and Resilience WG submitted on 18th December 2018

expected to remain. A considerable number of Oromo IDPs for instance have been traders and smugglers in the Somali Region with few other skills such as Carpentry or Masonry.

Access to the formal sector in regularising businesses, land tenure and finding formal employment through lack of skills remains a key challenge for the displaced in search of durable solutions, the rural-urban migrants and informal settlers

CHAPTER 3: THE HUMANITARIAN RESPONSE, THE HUMANITARIAN-DEVELOPMENT NEXUS, AND PEACE AND RECONCILIATION EFFORTS

There are currently over 80 humanitarian organizations operating in Ethiopia supporting the government-led response. These include 6 UN agencies, 59 INGOs, ICRC, IFRC, the Ethiopian Red Cross, and IOM. At least 7 national NGOs are conducting and supporting humanitarian operations, including faith and community based organizations, who have the multiplier effect of ensuring assistance reaches those in the remotest areas.^{17 18}

The Government of Ethiopia and humanitarian partners began 2018 with the launch of the Ethiopia Humanitarian and Disaster Resilience Plan (HDRP) for 2018 which sought US\$1.66 billion to reach 7.88 million people with emergency food or cash and non-food assistance. The Mid-Year-Review (MYR) of the 2018 Humanitarian Disaster Resilience Plan identified a funding requirement of \$1.494 billion to meet the needs 9.45 million people with non-food support in the second half of the year. The number of people targeted for relief food and cash support in the beginning of the year remained largely unchanged. This was due to the significant spike in internal displacement since April 2018 despite the general good performance of belg/spring rains. As of 10 December 2018, the funding status for the 2018 annual appeal was at 75 per cent, including resources provided by the Government of Ethiopia. The current humanitarian funding shortfall is estimated at US\$ 367 million.¹⁹

In October, the National Disaster Risk Management Commission established the National Durable Solutions Working Group, co-chaired by IOM and UN Resident Coordinator's Office, to coordinate the implementation of this strategy, as discussed below in Chapter 4.

The complexity and numerous drivers leading to conflict, displacement and migration requires, according to a number of observers, not only adequate resources, but a much stronger operational and geographical coordination of the emergency that is leading to overlaps in assistance to some areas and little reaching other areas.

In general it is clear that the best strategy to contain conflicts and subsequent displacement is local and cross-regional economic development, resulting in inclusive and sustainable economic growth.

However, community based conflict-management and resolution processes can also play a significant role. In this context, it is a step in the right direction that the new Minister of Peace, overseeing the Federal Reconciliation Commission, will engage in dialogues with all parties, including regional Peace Conferences, and that traditional concepts, like consulting the Elders, are also addressed.²⁰

¹⁷ UNOCHA Ethiopia <https://www.unocha.org/ethiopia/about-ocha-ethiopia>

¹⁸ UNOCHA Ethiopia WWW Matrix

https://reliefweb.int/sites/reliefweb.int/files/resources/14_3W_ETH_123118_A4_0.pdf

¹⁹ UNOCHA Ethiopia Humanitarian Bulletin Issue 71 | 24 December 2018 - 7 January 2019

²⁰ Assessment is based on interviews with various interlocutors in December 2018

Apart from that, Prime Minister Abiy Ahmed undertook a nationwide reconciliation tour in the first month of his premiership, visiting the Ethio-Somali, Oromia, Tigray, Amhara and Southern Nations regions, and delivering a message of forgiveness and unity in three languages, Afaan, Oromo, Tigrigna and Amharic. His message was to immediately stop ethnicity-based displacements.²¹

CHAPTER 4: STRATEGIES FOR DURABLE SOLUTIONS

In order to respond to the IDP crisis, the Government of Ethiopia, with the support of the humanitarian community, has responded by providing life-saving assistance. However, there is a recognition amongst all stakeholders that concerted efforts are required to address the root causes of displacements, and provide longer-term prospects and durable solutions for the displaced and their host communities. This effort is aligned with recommendations from the 2016 World Humanitarian Summit, as outlined in the New Way of Working (NWOW), as well as relevant national instruments.²²

Section 4.1: Global and National Frameworks

Neither the UN Global Compact on Safe, Orderly and Regular Migration nor the UN Compact on Refugees, as adopted in December 2018, are about IDPs. The same is true for the “Ethiopian Jobs Compact”, which was announced at the Refugees Leaders’ Summit on 21 September 2016 in New York.²³ The Compact is supposed to match international support for job creation in Ethiopia to the gradual relaxation of the limitations on labour market access for 30,000 refugees. The job creation elements of the Compact focus on Ethiopia’s ambitious industrialisation plans. It is meant to support improvements in the investment climate, investment promotion, and improving environmental and social standards in the manufacturing sector. This should create over 100,000 jobs, mainly for young women, in global value chains such as garments and textiles. Support to refugees will include the necessary legislative changes but also training, relocation, rehousing and protection measures for this vulnerable group. It is anticipated that some (but not all) of these employment opportunities for refugees would be in the manufacturing sector. For many, other sectors may be more appropriate and support for matching to these opportunities is to be provided.

While none of these commitments are directly about IDPs, theory and practice on how to support host communities and displaced people alike can be applied to the IDP context as well. In other words: it is argued here that the exemplary approach which the government of Ethiopia is taking towards refugees can and in fact should be applied to the current IDP situation. As stated above, such application would also be fully in line with the results of the World Humanitarian Summit, including on overcoming the chronic humanitarian-development divide.

Section 4.2: Current Efforts by Ethiopia

In line with the government of Ethiopia’s acknowledgement that concerted efforts are required to address the root causes of displacements, and provide longer-term prospects and durable solutions for the displaced and their host communities, it has convened a multi-stakeholder

²¹ Chatham House, “Ethiopia’s Prime Minister Shows Knack for Balancing Reform and Continuity” (27 April 2018), available at: <https://www.chathamhouse.org/expert/comment/ethiopia-s-prime-minister-shows-knack-balancing-reform-and-continuity> (Quote from: “Towards durable shelter and livelihoods solutions for IDPs in Ethiopia” paper (provided by UN Habitat), page 1)

²² Draft ToRs for Solutions and Resilience WG, page 1,2 (includes links to relevant documents)

²³ See for this para DFID paper on “Ethiopia Jobs Compact Business Case” as approved in 2017, page 2

Working Group.²⁴ This Working Group functions as a national platform, in line with relevant international, regional and national frameworks²⁵, with a focus on local integration, return or relocation as main options. The guiding principles of the Working Group are as follows (highlighting by the authors of this report):

- The primary responsibility to provide durable solutions for IDPs needs to be assumed by the national authorities. International humanitarian and development actors should support the efforts of national and regional governments;
- The authorities concerned should grant and facilitate a collaborative effort by both humanitarian and development actors to meaningfully assist IDPs towards achieving durable solution;
- The needs, rights and legitimate interests of IDPs as well as host communities should be the primary considerations guiding all decisions and interventions solutions;
- All relevant actors need to respect the right of IDPs to make an informed and voluntary choice on what durable solution to pursue and to participate in the planning and management of durable solutions;
- An IDP's choice of local integration or settlement elsewhere in the country, in the absence of the option to return, must not be regarded as a renunciation of his/her right to return should that choice later become feasible;
- Under no circumstances should IDPs be encouraged or compelled to return or relocate to areas where their life, safety, liberty or health would be at risk;
- IDPs seeking a durable solution must not be subject to discrimination for reasons related to their displacement;
- Similarly, hosting or receiving communities that (re-)integrate IDPs and whose needs may be comparable, must not be neglected in comparison to the displaced;
- IDPs who have achieved a durable solution continue to be protected by international human rights, and where applicable, humanitarian law.

The Working group will also promote the practice that **any durable solution efforts for IDPs, to the extent possible, aim to create favorable conditions that guarantee IDPs with long-term safety and security; adequate standard of living; access to livelihoods and employment; mechanisms for resolving housing, land and property issues; documentation; family reunification; participation in public affairs; and remedies, reconciliation and justice.**

Accordingly, any policy on durable solutions for IDPs must be based on Intention Surveys. For some places, like Gedeo-Guji, such surveys are not (yet) available, so durable solutions can not (yet) be discussed. Recent available surveys and data can be summarized as follows:²⁶

Intention surveys by IOM in Somali region showed that at 99.71% of sites IDPs prefer reintegration as a durable solution to their displacement while at 0.29% of sites they prefer return. In Oromia region at 28% of sites IDPs prefer reintegration as a durable solution to their displacement while at 17% sites they prefer return and at 55% sites, relocation.²⁷ Those that intend to return to places of origin tend to be those that have significant assets at the places of origin and

²⁴ See for this and the following: Draft ToRs for Solutions and Resilience WG; guiding principles: pages 2,3

²⁵ IASC Framework on Durable Solutions for Internally Displaced Persons (2010), Decision of the Secretary General on Durable Solutions for displacement (2011), and FDRE Constitution article 44 (2) and 89 (3)

²⁶ See Mission Report Ethiopia, Addis and Jijiga, 18-20 July 2018
Dyfed Aubrey UN-Habitat Inter-regional advisor, page 1ff.

²⁷ IOM DTM 10 Oromia/ Somalia Regions Ethiopia, April 2018

those displaced from or within the Oromia - Somali regional borders.²⁸ Integration and relocation from temporary settings has been supported by both regional governments. In Oromia 11 sites have been established with the intention of absorbing 1000 IDP households in each, providing shelter, future tenure security and basic services, while in the Somali Region the regional government is building a large site accommodating 3200 IDP households and 93 Waradas have been tasked to absorb 120 households each.²⁹

The authors of this proposal had the opportunity to also interview a number of IDPs from three of the 11 sites in Oromia where relocation has already taken place, namely in Legetafo, Bishoftu and Sululta. All the interviewed made it very clear that they would like to stay and locally integrate.

Against this background it can be concluded that local integration, with or without a prior relocation, is preferred by most IDPs in Ethiopia and should therefore be pursued as a primary policy approach, at least for the purposes of this proposal.

Nevertheless, other solutions including returns should be pursued wherever feasible and desired.

As mentioned above, it is argued here that the creation of an SDZ, i.e. the creation of a new special-status area with a special legal framework, is an adequate tool for local integration of IDPs and other vulnerable groups. An SDZ will make it possible to overcome the existing high barriers between the informal and the formal sectors, as analyzed in the next Chapter, and to come to a win-win situation for all groups including the host community.

CHAPTER 5: MAJOR BARRIERS TO FORMAL SECTOR INCLUSION IN ETHIOPIA

Bridging the gap between the informal and formal sectors within a sustainable development zone requires analysis of the main barriers SMEs and informal settlers in Ethiopia face when seeking to enter the formal sector. The legal and administrative framework of the zone can be tailored to address these obstacles. This Chapter groups the barriers into two types: barriers to developing legal housing and business facilities in the formal sector; and barriers to legally starting and operating a business.

Section 5.1: Barriers to Accessing Finance

The inability to access finance is both a central cause and effect of informality in Ethiopia. When individuals and entrepreneurs cannot access finance, they must operate in the informal housing and business economy. And the assets of informal houses and businesses cannot be used as collateral to access finance.

5.1.1: For Businesses

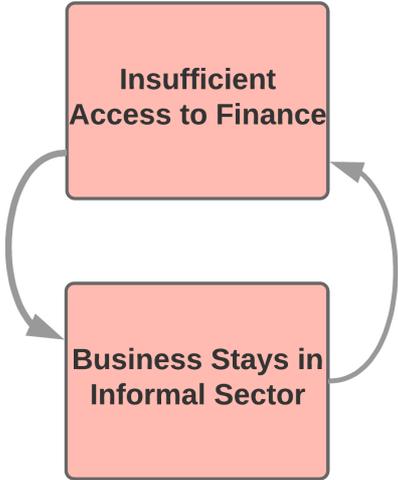
Lenders, including microfinance institutions, are normally unable to reach businesses in the informal sector, cutting those businesses off from the financing they need to grow. The inability to grow normally means these businesses never achieve the resources to overcome the

²⁸ Meeting of Meeting of UN-Habitat with Deputy Chair of Oromia Region Disaster Risk Management Commission, June 2018

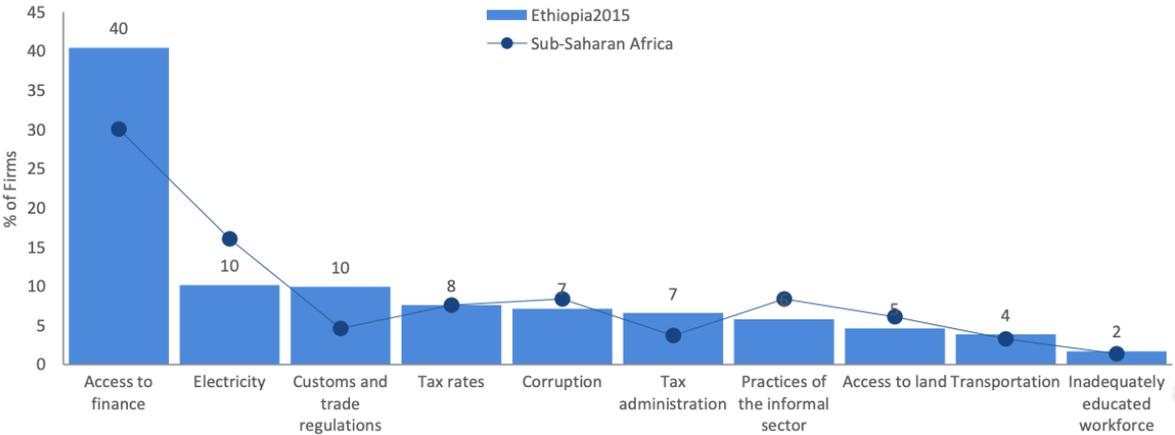
²⁹ Meeting of UN-Habitat, IOM, OCHA with Head of the Somali Region Disaster Preparedness and Prevention Bureau (DPPB) June 2018

bureaucratic and cost obstacles to become legal. Because they never become legal, it remains difficult to obtain financing, thus creating a vicious cycle.

While informal businesses face the most acute problems with accessing finance, most of Ethiopia’s formal-sector SMEs also have difficulty. According to the most recent World Bank Enterprise Surveys of Ethiopia, 40% of formal-sector businesses reported access to finance as the number 1 barrier to doing business.³⁰ Ethiopia ranks 175th out of 182 economies in ease of accessing credit according to the World Bank Doing Business Report.³¹ This ranking is mainly a result of the laws not adequately protecting creditors and the lack of any system for storing credit information, such as with a credit registry or credit bureau. As a consequence, businesses are normally forced to self-finance instead of relying upon a bank or other financial services provider. According to the World Economic Forum, 83% of investment for purchases of fixed assets are financed internally in Ethiopia, compared with 70% on average for Sub-Saharan Africa.³²



Top 10 Business Environment Constraints in Ethiopia - % of Firms (Survey Response)



Source: World Bank Enterprise Surveys (2015)

³⁰ See 2015 World Bank Enterprise Surveys: Ethiopia 2015 Country Profile (collecting responses from a broad sample of formal-sector businesses, primarily small enterprises (5-19 employees)), available at <http://www.enterprisesurveys.org/~media/GIAWB/EnterpriseSurveys/Documents/Profiles/English/Ethiopia-2015.pdf>

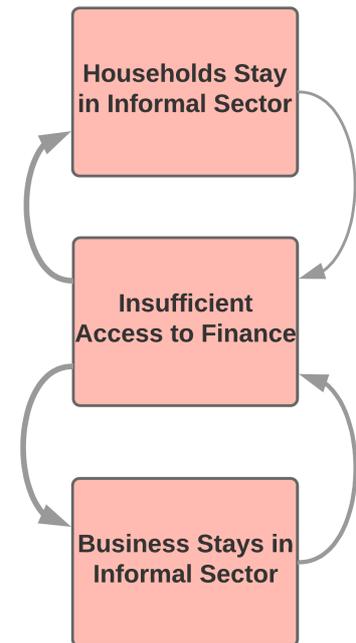
³¹ See World Bank, Doing Business 2019 Economy Profile: Ethiopia, available at <http://www.doingbusiness.org/content/dam/doingBusiness/country/e/ethiopia/ETH.pdf>

³² See World Economic Forum, Global Competitiveness Report (2018).

5.1.2: For Homes

Home finance is very limited in Ethiopia. High interest rates force most people to pay cash for their homes rather than obtaining a mortgage. The government offers subsidized mortgages for its low-income housing projects with down payments of 10%-40%, however there are not enough of these units for the number of low- and middle-income residents who need them.

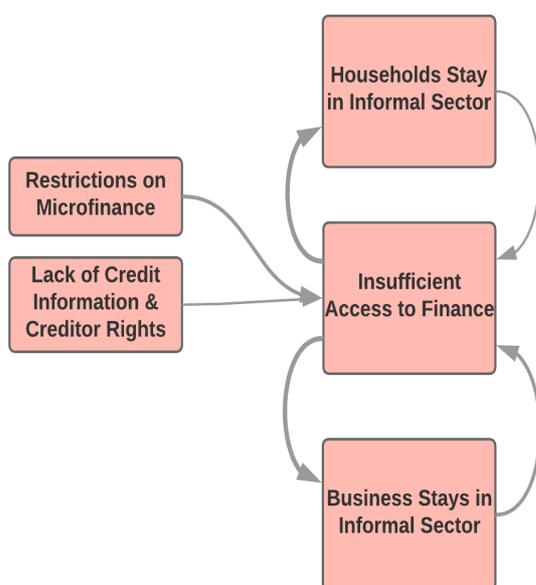
As a result, most people must pay the entire cost of their home up front in cash. In this context, people seek informal housing because it is cheaper and more abundant. But living in informal housing prevents them from using their homes as collateral for other loans, creating a vicious cycle similar to the one faced by businesses.



5.1.3: Microfinance Constraints

Access to finance for individual homeowners and small businesses is limited in Ethiopia primarily because most lenders perceive the risk of lending to be too high and because of lack of experience in the Ethiopian market.³³ High perceived risk leads to very high interest rates or lack of entry into the market at all.

Some of the major reasons for the high perceived risks for lending to small businesses and individual homeowners are:



- Many assets cannot be used as collateral because they are in the informal sector (e.g. by informal businesses or informal homeowners, as discussed above).
- Ethiopia lacks formal systems for providing credit information, such as a credit registry or collateral registry.
- The legal framework for protecting creditors' rights is insufficient.³⁴

One solution to breaking down barriers to finance is microfinance. Microfinance institutions (MFIs) provide relatively small loans to traditionally “unbankable” people, though the use of non-traditional practices. Unfortunately, MFIs face several regulatory obstacles in Ethiopia, such as the lack of a tiered approach to regulation, the inability to upgrade large MFIs into banks, overly cautious

³³ See Centre for Affordable Housing Finance in Africa, “Housing Finance in Ethiopia”, available at <http://housingfinanceafrica.org/countries/ethiopia/>.

³⁴ See World Bank, Doing Business 2019 Economy Profile: Ethiopia.

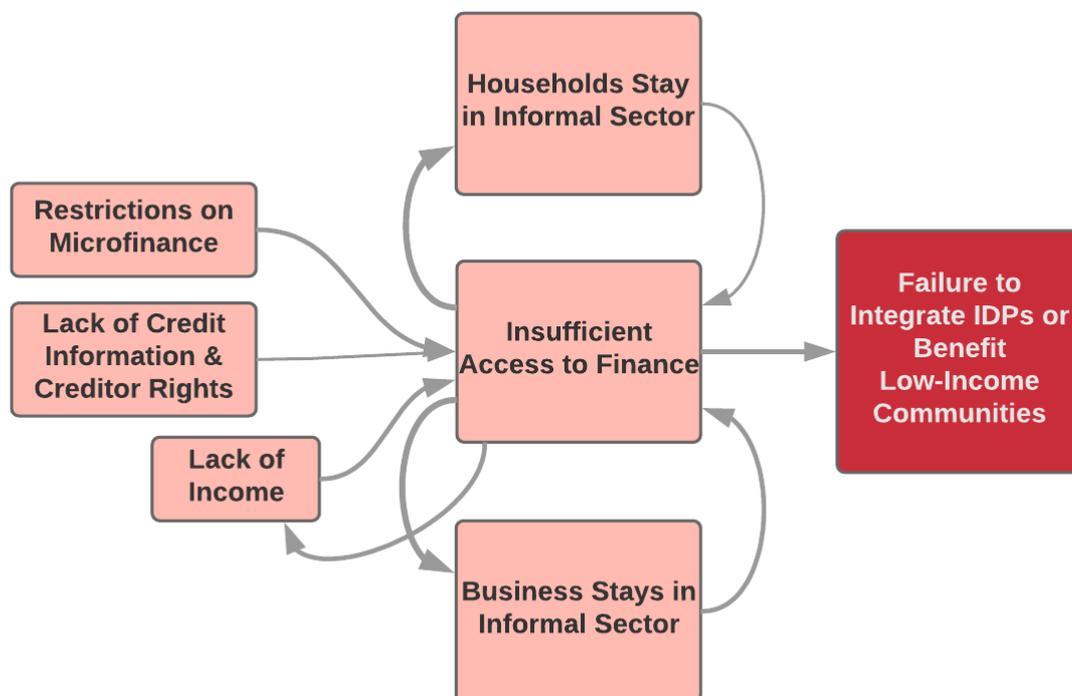
regulations that limit loan amounts and terms, and others.³⁵

Opening up finance for SMEs in an SDZ would require addressing some of the regulatory issues impacting financial services and a focused effort to attract MFIs. For instance, an SDZ should adopt a special credit registry for its residents and special laws affecting creditors' rights and making the rules for MFIs more flexible. These institutions could be a model or test case for future nationwide reforms.

Equally, if not more important, however, is addressing the root causes of housing informality and business informality. Unless SMEs and individuals move into the formal sector, financial institutions will still have a very hard time reaching them, because of the lack of registered collateral and documentation.

Poverty, or lack of income, also naturally reduces access to finance because individuals lack the general resources to leverage for loans and activities. Poor access to finance also reinforces poverty by failing to supply capital that people can leverage to earn income. Poverty is best addressed in an SDZ through improving employment and employable skills and through equipping people to operate their own businesses. These can be best achieved through reducing barriers to doing business. Poverty is also of course addressed through humanitarian aid, including cash transfers and other forms of social assistance, if it is built upon an environment that supports and encourages private-sector employment and business formation.

Causes of Insufficient Access to Finance in Ethiopia³⁶



³⁵ See Peter Mackie, et al. and Tegegne GebreEgziabher, *Microfinance and Poverty Alleviation in Ethiopia*, Cardiff University School of Geography and Planning (June 2015), available at https://www.cardiff.ac.uk/_data/assets/pdf_file/0010/581509/Ethiopia-Report-Jun-2015-FINAL.pdf

³⁶ Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.

Thus, access to finance will only be achievable in an SDZ if the barriers to formal sector housing and development and formal sector business and labor are substantially reduced. This is the focus of the rest of this Chapter.

Section 5.2: Barriers to Building Formal-Sector Housing and Business Facilities

Ethiopia is characterized by a high level of informality in the land and housing sector. By some estimates almost 100% of the recently developed housing stock in some areas was done without following formal processes.³⁷ For a typical Ethiopian, formal-sector housing can be bought from developers, land for the construction of housing can be secured through public lease auctions, or condominium housing can be purchased from the government. Formal-sector rental housing is available in older areas, but the construction of new formal sector rental housing is not permitted and the supply is limited.³⁸

5.2.1: Availability of Formal-Sector Housing

Most Ethiopians find land and housing in the informal sector because the formal sector does not produce enough of it or produce it at prices that the average Ethiopian can afford. Thus, a shortage of supply of formal-sector housing is the primary driver of informality. This has three main causes:

- Inflexible tenure laws
- The land lease system
- Shortage of government housing

Inflexible tenure laws prevent the direct sale or transfer of leases and limit the expansion of the stock of rental housing. This particularly limits the number of affordable older units that are available for sale or rent. More cheap older housing would allow new households to establish themselves in the city, whether through rental or purchase.

The land leasing system in Ethiopia is the main mechanism for securing formal sector land. Under this system the public sector lays out a plan for an urban area, pays compensation to the existing landowner, parcels and services the land, and then auctions 99-year leases for individual parcels. In practice, the supply of leased land is far below market demand, and most of the land produced by the system is given at below-market prices to favored tenants such as co-op housing associations. The remaining land is very costly (due to the supply shortage) and often is not the shape, size, or location that the buyer wants. Nothing is available for low-income people, most middle-class buyers, or buyers with limited savings.

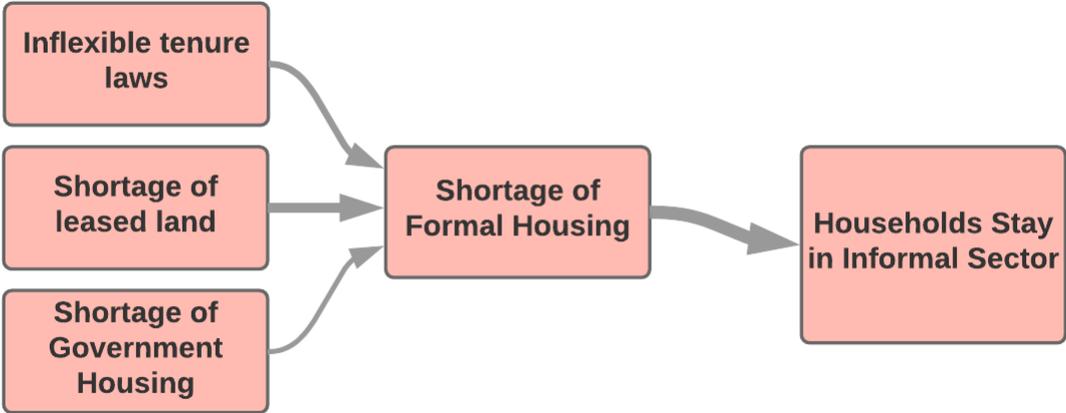
The middle-class and low-income alternative to the land leasing system is the government cooperative housing scheme. Under this scheme, the government builds housing that targets different income brackets within the society and makes it available with subsidized mortgages. The amount of down payment varies depending on the type of housing, ranging from 10% to 40%. Availability is a problem because government funds are limited, with years-long waitlists. The style of housing also limits certain activities, particularly home businesses that are common

³⁷ Gondo, T. (2011). Housing Informality in Expanding Ethiopian Cities: Moving beyond the ‘New Normal’ Syndrome. Proceedings: Real Corp 2011. Web: <https://pdfs.semanticscholar.org/f1e4/368284a25c5110ba6aa746bb37913746226d.pdf>

³⁸ Kaganova, O. (2014). Land Management as a Factor of Urbanization in Ethiopia. World Bank. Washington, D.C.; Lamson-Hall, P., Angel, S., Degroot, D., Martin, M., Tafesse, T. (2018). A New Plan for African Cities: The Ethiopia Urban Expansion Initiative. Urban Studies. <https://doi.org/10.1177/0042098018757601>; Hailu, Z. (2016). Land Government Assessment Framework Implementation in Ethiopia Final Country Report. World Bank. Washington, D.C.

to poor families. The diagram below illustrates the impact these causes have upon the shortage of available formal-sector housing and informality, with arrows weighted based on strength of impact.

Causes and Effect of Shortage of Formal-Sector Housing³⁹



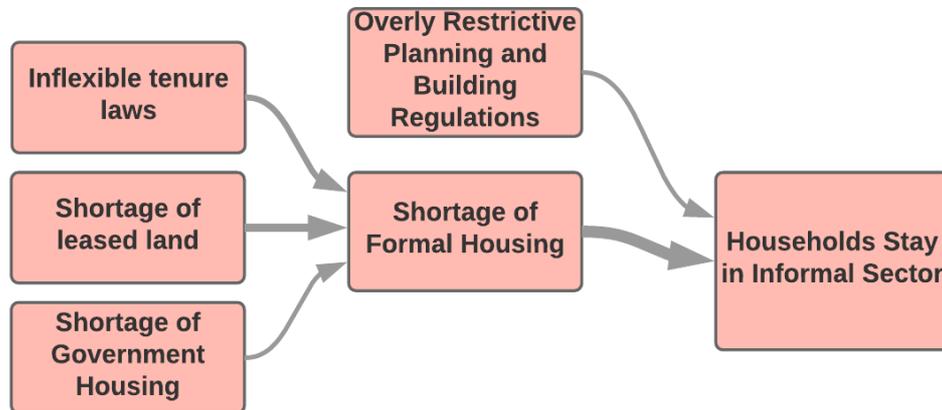
5.2.2: The Impact of Regulation

If these constraints were to be relieved by an increase in supply, the Ethiopian regulatory framework would still force many households into the informal sector by prescribing norms that do not correspond to typical levels of income. People cannot afford to buy homes that meet the regulated standards and have to find other housing. Problematic norms include inappropriate minimum plot size norms, minimum unit size norms, standards for services, setback regulations, and community planning standards. Phasing is also a problem -- Ethiopian regulations assume that housing will be occupied when construction is finished and will never be modified thereafter. But incremental construction is common in developing countries, with homes gradually improving as their owners' incomes allow. Because of the lack of land for formal-sector housing, most households never actually encounter these regulations. However, if the land constraint were to be relieved these regulations ensure that the informal sector would continue to dominate.

In the informal sector, plot sizes, locations, prices, designs and levels of services vary to accommodate almost every household. The informal land and housing supply is elastic and there are no effective controls on new construction, meaning the informal sector is better able to satisfy demand. Finally, most households in the informal sector are eventually formalized, meaning most people buy or rent with the understanding that they will eventually receive a title and security of tenure. These factors combine to make the informal sector attractive to almost all Ethiopian households. The following diagram illustrates the causes and effects of the shortage of affordable housing, with the thickness of the arrows illustrating the strength of impact.

³⁹ Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.

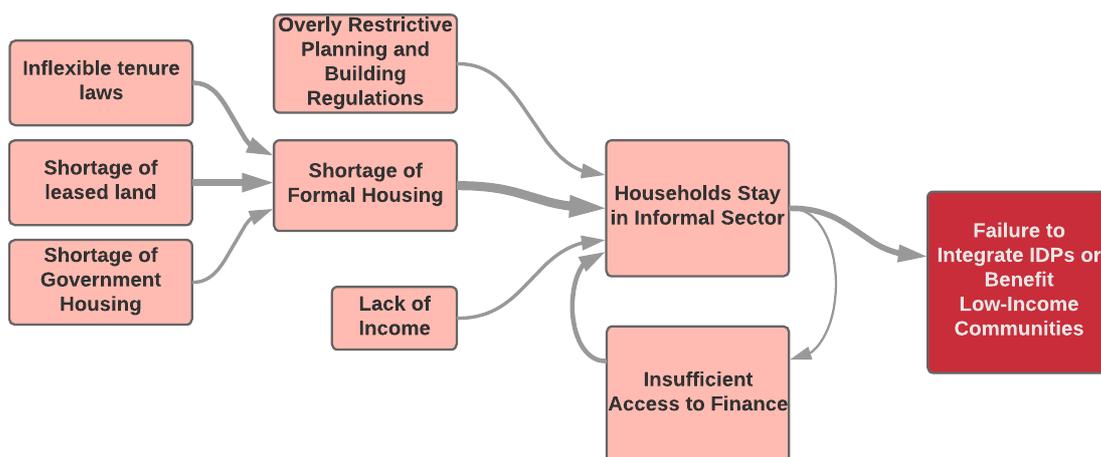
Impact of Urban Planning and Building Regulations with Shortage of Affordable Housing Causes and Effects⁴⁰



5.2.3: Financial Constraints

The supply constraints on affordable formal-sector housing lead to very high housing costs, because the supply of housing is unable to meet the demand for housing. These costs are unaffordable for the average person. Typical incomes are not sufficient to pay for formal housing. Compounding this problem is the lack of home financing. As discussed in the previous section on access to finance, home mortgages are generally unavailable except for those relatively few people who are able to obtain government housing. Most home buyers are members of the diaspora or people who are wealthy – a small part of the population. Thus, insufficient access to finance and low incomes also creates demand for informal housing, as illustrated below.

Causes of Informal Housing in Ethiopia⁴¹



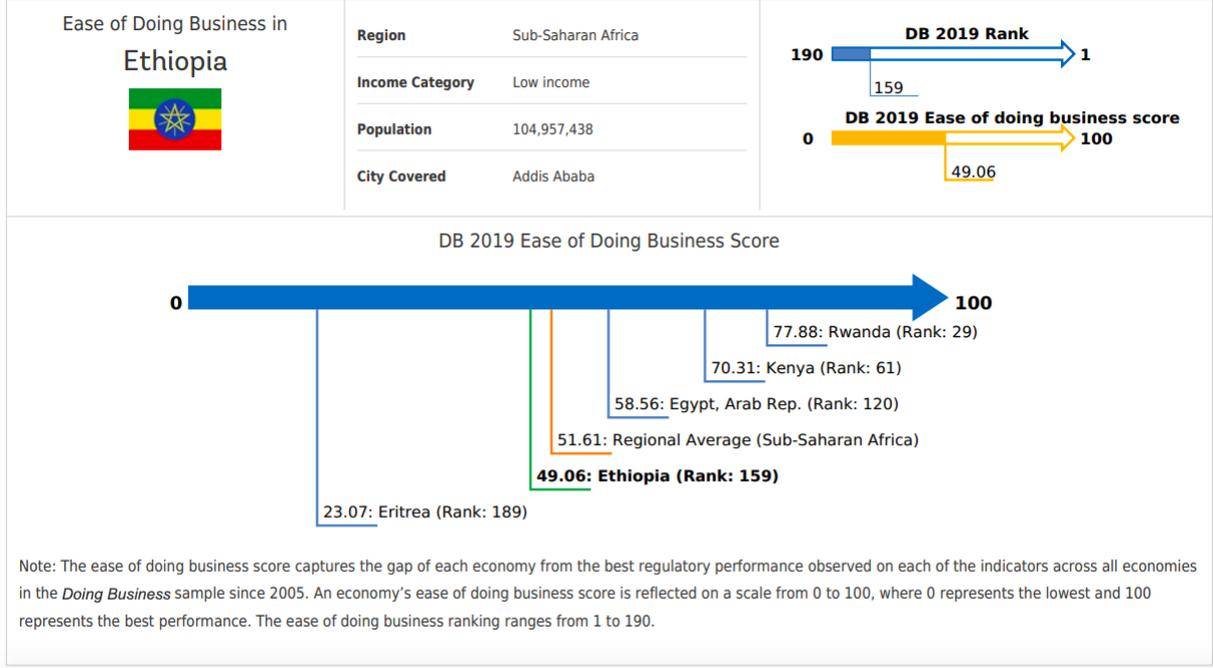
⁴⁰ Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.

⁴¹ Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.

Section 5.3: Barriers to Starting and Operating a Formal-Sector Business

Despite positive steps in recent years, businesses in Ethiopia face serious challenges starting up and operating in the formal sector. Ethiopia ranks 159th out of 182 countries in its overall ease of doing business, according to the World Bank Doing Business Report.⁴² Several of the country’s institutions, especially the Ethiopia Investment Commission, have taken laudable steps to improving the business environment, but problems with lack of coordination among different government agencies have hindered progress.⁴³ Furthermore, government corruption hinders private-sector growth in Ethiopia. Ethiopia ranks 107th on Transparency International’s Corruption Perception Index,⁴⁴ and 27% of firms have reported experiencing at least one bribe request.⁴⁵

Ease of Doing Business in Ethiopia

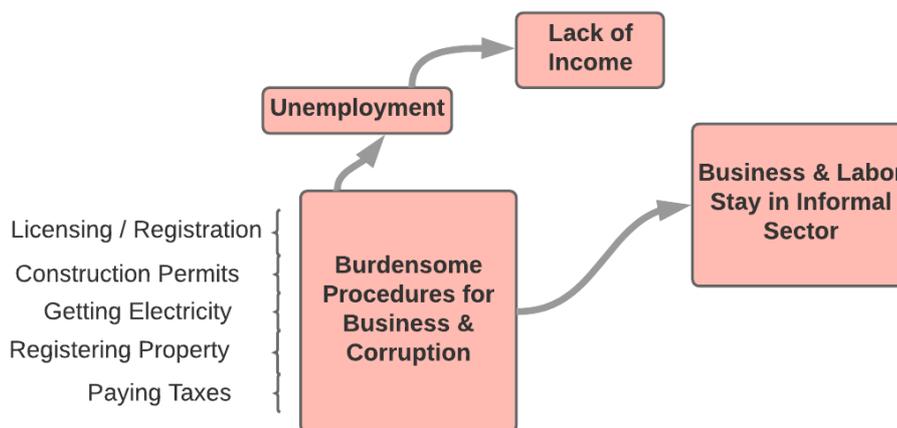


Source: World Bank, Doing Business 2019 Economy Profile: Ethiopia

As a result, many businesses, particularly those operated by low-income or displaced persons remain informal, operating with few legal protections or resources. Moreover, barriers to doing business weaken the overall business dynamism of the country, contributing to a lack of decent, well-paying work for displaced people.

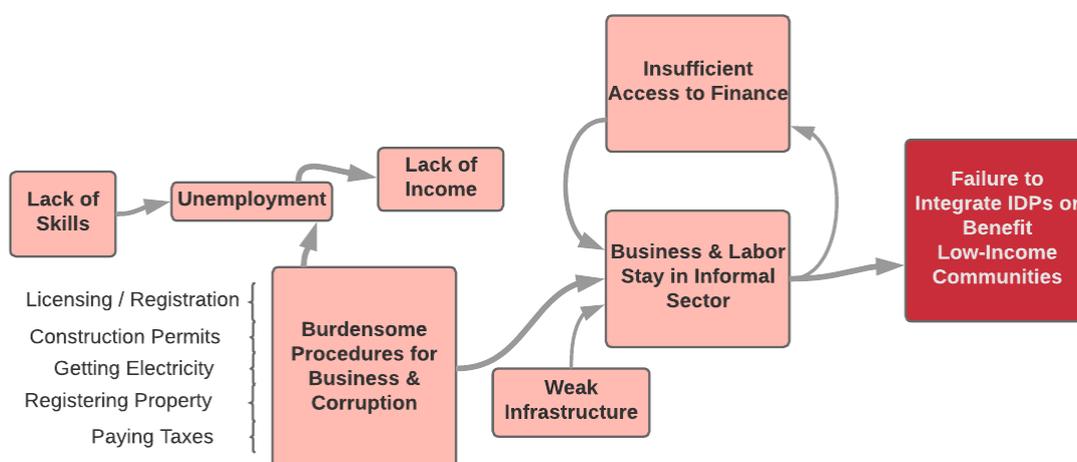
⁴² See World Bank, Doing Business 2019 Economy Profile: Ethiopia
⁴³ See U.S. State Department, Bureau of Economic and Business Affairs, *2018 Investment Climate Statements: Ethiopia*, available at: <https://www.state.gov/e/eb/rls/othr/ics/2018/af/281416.htm>
⁴⁴ See Transparency International, *Corruption Perceptions Index 2017*, available at https://www.transparency.org/news/feature/corruption_perceptions_index_2017#table
⁴⁵ See *2015 World Bank Enterprise Surveys: Ethiopia 2015 Country Profile*.

Impact of Burdensome Business Regulatory Procedures and Corruption⁴⁶



Burdensome business procedures is not the only cause of unemployment and the growth of the informal sector. Low-quality infrastructure also depresses the investment climate, which reduces the supply of formal-sector jobs and businesses. Moreover, lack of skills in the workforce also contributes to unemployment. Also, lack of finance keeps businesses in the informal sector in a vicious cycle as discussed previously. All of this contributes to the inability to integrate displaced people.

Causes of Informal Business and Labor and Lack of Income in Ethiopia⁴⁷



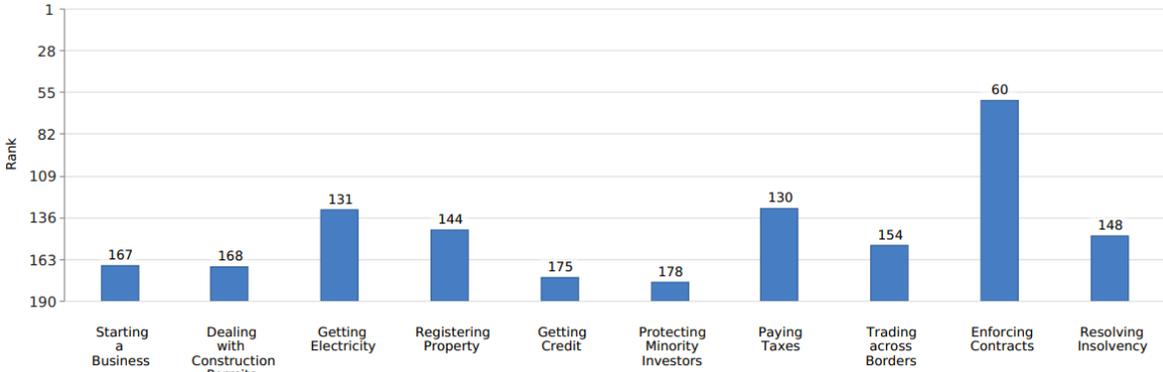
An SDZ would substantially reduce many of the most severe challenges for businesses to operate in the formal sector. As explained in greater detail in Annex A, some of the most severe barriers to businesses include the difficulties with starting a business (167th), dealing with construction permits (168th), registering property (144th), getting credit (175th), and paying taxes (130th), among others. Under the model presented in the next Chapter, an SDZ would make it significantly easier for businesses of all sizes (including those that would employ or be run by IDPs) to satisfy these requirements, smoothing their pathway to the formal sector.

⁴⁶ Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.

⁴⁷ Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.

Moreover, through new administrative systems, the SDZ could reduce corruption and offer new techniques that can be replicated by all other government entities.

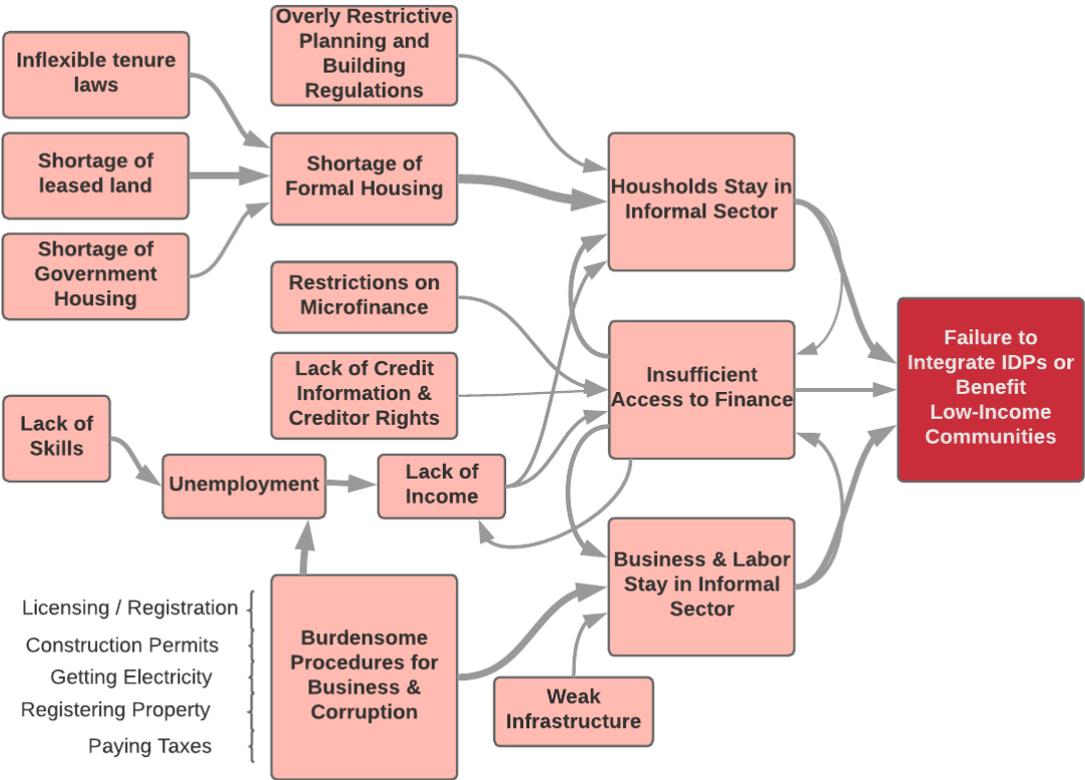
Ease of Doing Business in Ethiopia - Specific Topics (out of 182 economies)



Source: World Bank, Doing Business 2019 Economy Profile: Ethiopia

The causes of informality in Ethiopia, and therefore the challenges with providing durable solutions to displacement, are complex and interdependent. Below is a causality diagram that incorporates the causes of informal housing, insufficient access to finance, and informal business and labor into one. The size of the arrows represents the degree to which they impact other causes and effects, all of which lead to the inability to achieve a durable integration of displaced people. To be effective, the SDZ must address these root causes comprehensively.

Factors Impacting Informality and Integration in Ethiopia⁴⁸



⁴⁸ Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.

CHAPTER 6: PROJECT PROPOSAL: “SME CITY: BRIDGING THE INFORMAL WITH THE FORMAL IN ETHIOPIA FOR IDPs AND LOCAL COMMUNITIES”

Section 6.1: General Approach

SDZs are a durable solution to the IDP crisis by providing a path to integration into host communities. SDZs would integrate IDPs into an inclusive local community of high-, middle-, and low-income residents and businesses, all of whom mutually benefit from each other’s presence.

SDZ would be designated new cities designed to reduce the barriers to entering the formal economy. SDZs would accomplish this by creating new laws and administrative frameworks that make it easier to legally work and operate businesses, access finance, and develop housing. In this way SDZs would confer all the benefits of the formal sector (security, legal rights, upward mobility, etc.) while retaining the positive aspects of the informal sector (its ability to flexibly provide housing, income, and goods and services adapted to the needs of low-income people). SDZs can also serve as a testing ground for reforms and new administrative and service approaches that can be adopted more broadly throughout the country in the future.

To do this, the SDZs would need special legal status at the national and regional levels that allows them to establish new rules and systems regarding urban planning, construction, finance, business licensing and registration, property registration and transfer, identification documents, and tax administration. To acquire this special status, the SDZs would depend upon both existing and new national and regional legislation.

An SDZ can operate as a social enterprise that uses blended finance to lease land, develop basic infrastructure, and provide services to low-, middle-, and high-income residents and local and international businesses. It would generate revenue from the land and a portion of the tax revenue collected from the SDZ, while also generating increased revenue for government stakeholders. Residents of the SDZ would be shareholders in the project, so they directly benefit and have a voice in its decisions.

Section 6.2: Development and Operational Model of the SDZ

In the pilot SDZ, which would be called “SME City”, a social-enterprise SDZ Developer would have a long-term lease over a 200-500 ha area of land. The pilot SDZ should have room to expand, ideally up to 2,000-3,000 ha or more, to allow for the formation of more comprehensive urban frameworks. Subsequent SDZs should be similarly large. SDZ Developers would perform a wide range of development and administrative functions in the zone. A majority of the initial shares of the Developer would be owned by the project promoters, and other shares would be owned by local, regional, and national government entities, residents of the SDZ, and other stakeholders.

The land should be vacant or lightly occupied and in a rapidly urbanizing area. The SDZ Developer would establish a masterplan for the land that provides a plot layout and areas for roads, common areas, and other basic infrastructure. It would also establish a cadaster that defines the rights for all of the plots of land. Defining and respecting land rights will require a careful process, given the complexity of interests that typically exist for many plots of land.

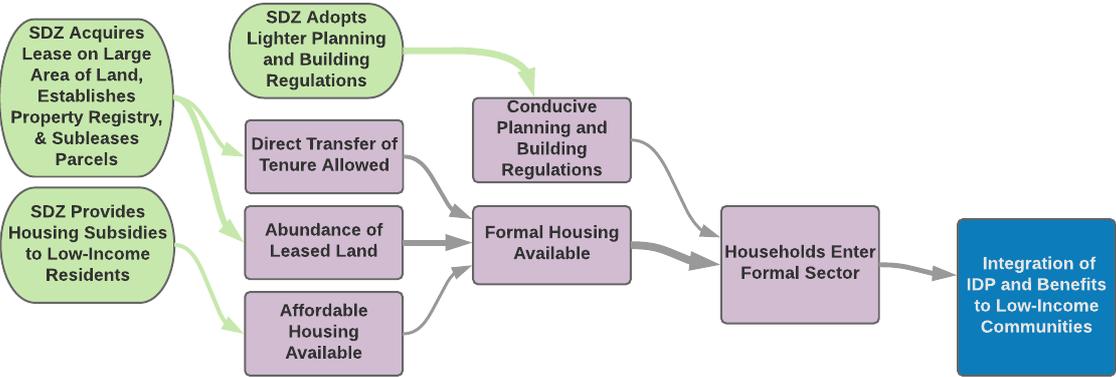
Existing occupants may include some informal settlers, farmers, and potentially some formal houses and businesses, but the land should be mostly undeveloped. Existing informal settlers would not be displaced, but rather be formalized through subleases on their plots of land from the SDZ Developer. The Developer would further ensure that farmers are adequately

compensated for the loss of their farmland through equity shares in the Developer, in addition to the compensation they receive from the government. Existing occupants with formal tenure (i.e., people with a valid lease to the land), could also be brought into the SDZ without losing their property rights. For these occupants, their land lease would not transfer to the Developer, but they would be simply brought under SDZ Administration.

The SDZ Developer would incrementally develop roads and basic utilities for the SDZ (power, water, sewage, etc.) in accordance with its masterplan. It would also sublease unoccupied parcels of land to new businesses and residents in accordance with powers under the Industrial Parks Proclamation, as described in further detail in the proposed legislative framework section below. Many of the public works efforts would rely upon local workers, to generate jobs and local economic activity, similar to the existing cobblestone roads and land rehabilitation programs.

While the SDZ Developer may build some basic housing and business facilities itself and sell or lease them to residents, residents would be empowered to develop their own housing. The Developer would facilitate this by attracting local building-materials companies and construction companies to the area if they are not already present. Residents can purchase the materials and construction services to develop homes themselves, with financial support facilitated by NGOs, donors, and microfinance institutions. The Developer would assist the residents to comply with a new building code, which would avoid threats to public health and safety, and would also allow incremental development -- in line with existing local practices. We believe this model would lead to structures that are much more affordable and tailored to the individual needs of their occupants than traditional “top-down” development models, and place a greater degree of autonomy and power in the hands of residents. Moreover, residents would be allowed to transfer property and subleases to others through direct transactions that would be registered with the SDZ Administration.

SDZ Effect on Housing Informality⁴⁹



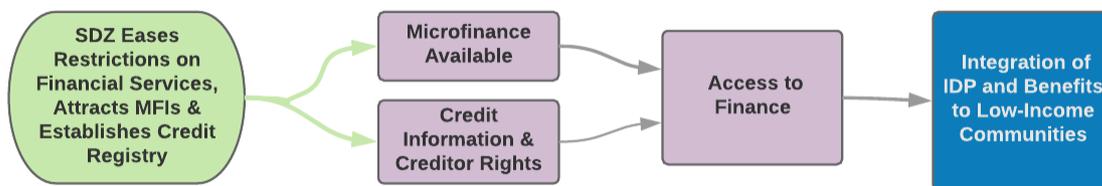
The Developer would establish an SDZ Administration that would perform a range of public service and regulatory tasks on behalf of government entities at the local, regional, and federal levels. These tasks would include:

- Property registration and maintenance of an SDZ cadaster;
- Planning and building regulations that are conducive to development by people of all income levels;
- Establishment of an on-site one-stop-shop services center for residents and businesses;

⁴⁹ Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.

- Creation of independent business startup and operation procedures, including simplified registration, licensing, approvals, and permits;
- Construction regulation and electricity connections;
- Tax administration, including collection of filings, payments, and enforcement on behalf of governments;
- Establishment of a collateral or credit registry and other tools for improving access to finance;
- Adoption of new, appropriate financial services regulations; and
- Facilitating and streamlining all other functions of government carried out by other government entities.

SDZ Effect on Access to Finance⁵⁰

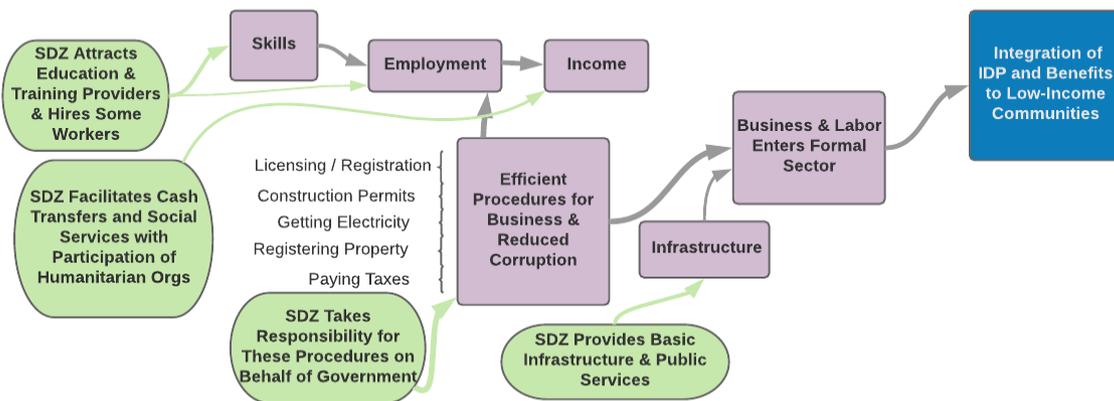


Within the SDZ one-stop-shop services center, residents could find a range of services, such as:

- Social services, including:
 - healthcare,
 - education,
 - psychological counseling,
 - vocational training,
 - job placement,
 - humanitarian NGOs,
 - cash assistance, and more;
- Legal assistance, advocacy, and mediation, helping low-income residents and small businesses receive justice in criminal and civil matters;
- Financial services and business mentorship;
- Tax preparation and accounting;
- Getting set up with power, water, and telecommunications;
- Handling all business regulation needs, including registration and all licenses and approvals; and
- Access to dispute resolution services, including arbitration.

⁵⁰ Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.

SDZ Effect on Business and Labor Informality and Income⁵¹



Over time, the SDZ would generate a return on investment through rental income from the subleases. The subleases would be subject to an annual reassessment and adjustment of the rental price to reflect the approximate market value of the property in the SDZ. This approach has several benefits for both the SDZ and the wider region and nation. Among other things it:

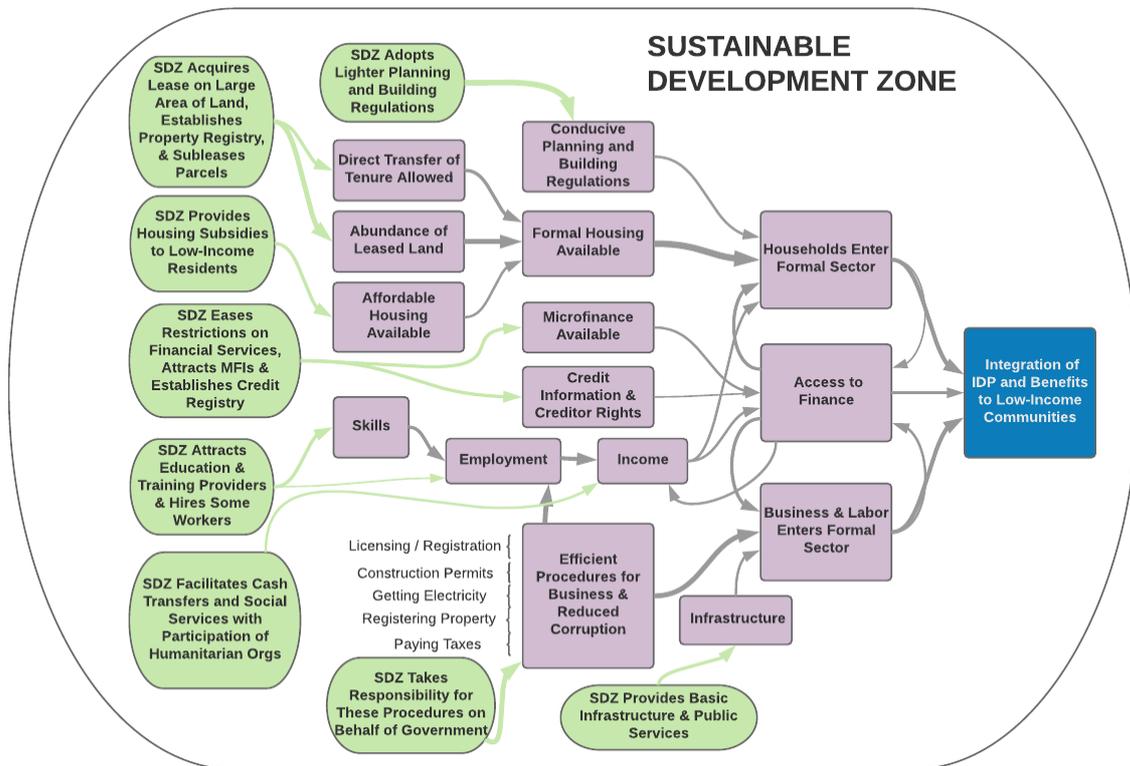
- Aligns the financial incentives of the SDZ Developer with providing high-quality services and administration, because good services and administration will tend to improve land value and increase revenue;
- Provides the government a model for deriving revenue from the value of land rather than income tax, which is more difficult to administer;
- Creates a cultural expectation around paying a property tax, establishing an important new norm.
- Encourages intensive use of land, including vertical development, leading to more efficient land use; and
- Mobilizes private finance and equity investment by generating ROI.

Low income residents (including IDPs) could receive housing vouchers or cash assistance to help pay for their rent and other services if they lack the ability to pay.

The SDZs specific rights and obligations would be set out in a legally binding agreement formed with a special administrative areas committee, as described in greater detail below. The agreement would provide an end date under which the SDZ would transfer to the regional and/or local government similar to a build-operate-transfer concession agreement.

The diagram below illustrates the effect of an SDZ on the barriers to entering the formal sector described in Chapter 5. An SDZ would create a special area with interventions targeting the root causes of informality from housing, finance, and business and labor dimensions. As with the previous diagrams, thicker arrows represent stronger effects.

⁵¹ Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.



Section 6.3: Proposed Legislative Framework for the SDZ

To create an SDZ, it is recommended that two legislative frameworks be layered over the same geographic area. First, the SDZ should be given industrial-park status, entitling it to all of the benefits of the Industrial Parks Proclamation. Second, the SDZ would need new legislation that does not yet exist, a Special Administrative Areas Proclamation, which would enable the SDZ to accomplish its unique aim of integrating people into the formal economy. The sections below discuss the role each of these laws would play in the SDZ.

6.3.1: Role of the Industrial Parks Proclamation for the SDZ

The SDZ should obtain status as a private industrial park. Under the Industrial Parks Proclamation, private parties can apply to the Ethiopia Investment Commission (EIC) to designate a specific area of land as an industrial park and to become the developer of the industrial park.⁵³

If the EIC approves the application, it issues the Developer a permit and a long-term lease to the land, which the EIC will have acquired from the local authorities responsible for the area. The Developer is then free to develop a master plan and infrastructure for the area and sublease property to industrial park enterprises. Industrial Park enterprises must be registered with the EIC and receive an industrial park enterprise permit. The Proclamation also allows residents to live on-site and lease property, provided they obtain an industrial parks residence certificate.

⁵² Source: Politas Consulting (2019). As with all other causality diagrams, the arrows are weighted based on the estimated degree of impact, with the thicker arrows having a stronger impact.

⁵³ See for this and the following: Industrial Parks Proclamation, No. 886/2015.

There is no explicit requirement in the Proclamation that a resident be an employee of an industrial park enterprise.

Within an industrial park, enterprises enjoy exemption from customs duties on their imports in proportion to their level of exports. They also enjoy more secure protections for their investments and property, higher quality infrastructure, and more streamlined regulatory approval and access to services via a one-stop shop.

Currently, the industrial parks are used almost exclusively by larger, foreign, export-oriented manufacturing investors, however, the EIC has expressed a strong desire to use the industrial-parks program to benefit local SMEs and to integrate residential housing into the industrial parks.

An SDZ would utilize the industrial-parks legal framework by enabling the Developer to integrate SMEs and residents in a urban setting. It would do this by securing industrial-park-enterprise status to all businesses within the SDZ and industrial-park-resident status to all individuals within the SDZ. It would then leverage this status to provide formal tenure to these businesses and individuals and lower the barriers that prevent low-income people from entering the formal sector.

Industrial Park status would add several necessary elements to the SDZ, in particular it:

- Allows the SDZ Developer to sublease industrial park land. (Industrial Parks Proclamation, Art. 5) This would enable the SDZ Developer to grant formal tenure to current occupants and future occupants by issuing them subleases. It would also provide it with a revenue source derived from the value of the land.
- Provides greater flexibility over the terms, tenure, and use of land in the SDZ. (Industrial Parks Proclamation, Art. 22/4). This should grant the Developer more flexibility to acquire a long-term lease on the land, to modify the master plan for the property, and to permit transfers of subleases among enterprises and residents.
- Enables businesses in the SDZ to take out a mortgage on property (Art. 22/6). This would facilitate access to finance for SMEs and residents to lease or build new property.⁵⁴
- Consolidates some of the procedures for starting a business, reducing bureaucracy. (Art. 12). Currently, the EIC carries out some functions in the industrial parks typically done by other government entities and channels other functions through its one-stop shop, such as registering and licensing businesses, issuing construction permits, and customs clearance. Ideally, the EIC can delegate responsibility for performing many of these functions to the Developer.
- Enables export-oriented businesses to acquire duty-free imports. (Art. 9/2)⁵⁵ This can help the SDZ attract large foreign investors as anchor tenants and support smaller local businesses that serve these anchor tenants.

⁵⁴ The Industrial Parks Proclamation only explicitly grants the right to mortgage property to the Industrial Parks developer, operator, or enterprises. It does not state that individual residents can mortgage property. However, the EIC might help residents acquire home mortgages by allowing them to form holding companies that technically own their homes and to grant these holding companies status as industrial parks enterprises.

⁵⁵ Under the Industrial Parks Proclamation, industries receive exemptions from import duties in proportion to the level at which they export final products. Currently all, or nearly all, industrial park enterprises export 100% of their products, however it is possible under the law for a business to, say, export 50% of their products and sell 50% domestically - in which case, 50% of its imports would be exempt from duties.

6.3.2: Role of New Legislation - Special Administrative Areas Proclamation

SDZs would require new, additional legislation at both the national and regional level to serve their objectives. This legislation would delegate many of the functions of government that are most critical to the development of the formal sector to a special SDZ Administration. It would complement the legal exemptions conferred under the Industrial Parks Proclamation by giving SDZs special responsibilities to adopt and enforce rules. This legislation which we have provisionally called the Special Administrative Areas Proclamations (SAAP), would need to be adopted by the national parliament and regional parliament.

Under the proposed SAAP, a Special Administrative Areas Committee (SAAC) would be formed for each region desiring to participate in the program. The SAAC would consist of representatives of the regional government and national government, civil society, the international community, employers, unions, and parliamentary committee chairs. A party could submit a proposal to the SAAC to create a Special Administrative Area (SAA) -- a new administrative authority over an area of land that is currently mostly undeveloped and either unoccupied or lightly occupied. The proposal would be evaluated against criteria defined in the SAAP for at the national and regional levels. Approval of the proposal would mean that the party submitting the proposal could establish a new administrative authority that has the power to carry out several government functions on behalf of relevant national, regional, and municipal governments.

An SAA would have an obligation to share a certain proportion of the revenue earned from the area with stakeholders, including regional and national government entities. The SAA would have an obligation to ensure these government entities derive significantly more revenue from the area than they would have otherwise.

The powers of the SAA should include, for instance:

- Independent authority to register businesses and issue business licenses. The SAA would have the power to create a business register and licensing requirements that are more flexible and efficient than existing practices, enabling more businesses to enter the formal sector.
- Authority to issue construction permits and adopt new construction approval requirements. The SAA should be empowered to reduce the burden of obtaining permits and allow more developments to be considered formal.
- Authority to create a cadaster, masterplan, and planning and building regulations for the area. This would include the power to formalize land tenure and adjust land use restrictions.
- Power to collect taxes on behalf of the local, regional, and national government. The SAA could establish a tax administration that makes paying taxes more predictable, efficient, and fair for residents and businesses in the area. By introducing best-practice administrative techniques, the SAA should increase collection rates. Funds received would be split between the levels of government to which they are owed and the SAA itself, provided the funds received by government are substantially more than they would have otherwise received had they collected the tax themselves.
- Ability to provide public services, including utilities, transportation, sanitation, social/humanitarian services, and all municipal functions. This should enable higher-quality, more reliable and more cost-efficient services in the area than typically enjoyed in the country.
- Ability to develop low-cost legal assistance, dispute resolution systems, and courts with defined competencies. These would open access to justice to low-income residents and businesses in the area.

The SAAC would oversee the actions of each SAA to ensure compliance with legal requirements contained within legally binding concession agreements. Part of these requirements would include:

- Information sharing. The SAA should exchange information about its activities and levels of government and other relevant stakeholders.
- Annual audits of activities and finances. Each SAA Administration would be subject to audits of not just its finances, but also its administrative practices. Audit findings would be publicized, and violations punished.
- Revenue sharing. The SAA would have obligations to divide defined percentages of taxes collected and other revenue with relevant government entities at the local, regional, and national levels.

6.3.3: Combined Industrial Parks and Special Administrative Area Status

The SDZ would form by combining industrial parks status with the new special administrative area status. These two statuses would interact as follows:

- Industrial Parks Status - Allows the SDZ Developer to sublease land, allow transfers, and confer other benefits to businesses
- Special Administrative Area Status - Delegates certain governmental functions to the SDZ Administration.

By combining these two statuses, the SDZ would have greater ability to formalize land tenure and businesses. It would do this by lowering the barriers to obtaining formal-sector housing and operating a formal-sector business.

As for formal-sector housing, industrial park status, by itself, would allow the the SDZ to have its own master plan and parcels of property for sub-lease, enabling it to rationalize urban planning and land rights. Special administrative area status would enable it to go further - to perform urban planning, building regulation, and property registration on behalf of the government. This would allow the SDZ to optimize these functions to achieve both greater flexibility and greater protection of public concerns. Residents would thus be able to legally acquire or build property much more affordably and have much more secure rights to that property than they would have without the SDZ.

As for formal-sector business, industrial park status, by itself, would consolidate some of the procedures for obtaining licenses, permits, and other approvals for enterprises. Special administrative area status would enable the SDZ to go much further - to enable the SDZ to perform business regulatory functions on behalf of the government. Under special administrative status, the EIC, the Ministry of Construction, the Revenues and Customs Authority, regional government entities, and the municipalities, would delegate responsibilities to the SDZ. This would allow the SDZ to make it easier for businesses to obtain licenses, permits and other approvals of all kinds; pay taxes; register and develop property; get access to electricity; and more. In exchange, the SDZ would transfer a portion of the revenue it collects from residents to the relevant government entities, ensuring they receive a significantly larger amount than they would have otherwise received without SDZ status.

As a result, residents would thus gain more secure rights to their property and their businesses. This would secondarily greatly improve access to credit, security, livelihood, income, and upward economic and social mobility.

Potential Innovative Partnerships: Creating an “SME Smart City” as an Incubator for New Technologies and Social Change

One potential use of an SDZ or SME City is as an incubator for technological innovation. Such an “SME Smart City” could attract local and international partners that aim to develop and introduce skills and new technologies to Ethiopia through the safe and conducive business environment provided by SDZ status.

An SME Smart City could serve to introduce renewable energy knowhow, digital and communication technologies, and help to further food processing and manufacturing methods. Each SME Smart City would host at least one startup incubator and facilitate co-working spaces for young entrepreneurs. Campuses for accelerated learning and skill development allowing for the introduction of professions of the future can provide the necessary boost for the Ethiopian economy to shift and transform to supplement labor-intensive manufacturing with more advanced industries.

The SME Smart Cities could serve as a lab for possible national social and digital innovation and providers and developers of blockchain, crypto and digital applications could be attracted to introduce innovative governance and financial transaction systems. SME Smart Cities would be limited in space and would have a population of around 50,000 people, making them well suited for research and development (R&D) to form smart governance and service provision. As there is a clear focus on allowing SMEs to access the formal sector while attracting modern technologies, the environment is conducive for new systems to be tested.

Available facilities and relevant administrative services, such as business and partnership accelerators, would catalyze synergies and effective collaboration between investors, businesses, social-service providers, and, primarily, civil society and citizens. One-stop social service and counselling centers built on a smart network help promote effective access to social rights, information, and referral to service providers.

The financial feasibility of an SME Smart City should be assessed as the SDZ program is advanced.

Section 6.4: Overarching Roadmap for Creation of an SDZ

Formation of an SDZ will require a consensus from many stakeholders, particularly at the regional and national government level. The broad steps required to form an SDZ are:

1. Development of a pre-feasibility study. The pre-feasibility study should present a detailed description of the institutional, legal, and political features of the SDZ and an indication of its economic and financial potential.
2. Obtaining “in-principle agreement” from the relevant national and regional authorities. This agreement should include the Ethiopia Investment Board, relevant cabinet ministries, and at least one regional government. There should be broad support for the basic features of the SDZ detailed in the pre-feasibility study, including agreement in principle to delegate functions to the SDZ Administration.
3. Drafting and adoption of the proposed Special Administrative Area laws. These laws would include a proclamation by the national parliament to establish the SAACs and transfer specified functions from national government agencies to the SAAs upon approval by the SAAC. It would also include a regional-level law that assigns regional officials to the SAAC and transfers specified functions from the regional and municipal government to the SAAs upon approval by the SAAC.

4. Formation of an SDZ Developer. The Developer would be formed by a variety of international institutions and private-sector organizations, and would be jointly owned with national and regional governments and SDZ residents.
5. Formation of the SAAC and approval of the SDZ Developer’s proposal for special administrative area status.
6. Approval by the Ethiopia Investment Commission to give the SDZ industrial park status. Under the SAA Proclamation, the EIC would delegate many functions to the SDZ, along with other government entities.
7. Formation of a long-term lease and concession agreement for the approved SDZ site.
8. Formation of an SDZ Administration. The Administration would assume the functions of government delegated to the SDZ.
9. Initial development and service provision. The SDZ would establish a masterplan, sublease parcels, and provide basic infrastructure and public services.

Section 6.5: Advantages of an SDZ for Key Stakeholders

6.5.1: For National, Regional, and Local Governments

For national, regional, and local governments, an SDZ would:

- Generate significant increases in tax revenue, resulting from:
 - Inclusion of informal businesses into the formal economy
 - Economic growth from the special legal and administrative institutions in the SDZ
 - Higher collection rates through delegation of tax administration to the SDZ;
- Generate share of profits of the SDZ Developer, derived from rental income on land;
- Integrate IDPs and informal settlements in a sustainable way;
- Shift burden of providing administration, infrastructure, and services to the SDZ;
- Attract foreign-direct investment and foreign exchange;
- Stimulate growth of local businesses and SMEs;
- Lead to sustainable and inclusive economic development;
- Provide a test case and “incubator” for new urban management and reforms while avoiding the political challenges of pursuing region-wide or nation-wide changes from the start;
- Support broader urban planning and development needs by providing new serviced urban space; and
- Eventually transfer to governments as part of their regional and local frameworks after the build-operate-transfer concession ends.

6.5.2: For Local Communities

For local communities, including both formal and informal residents and businesses, an SDZ would:

- Provide informal businesses with an easier pathway to enter the formal sector, resulting in legal protections, stability, finance, and avenues for growth;
- Open opportunities for local community members to find dignified employment and develop new skills;
- Provide businesses and residents in the formal-sector a streamlined and predictable administrative and regulatory environment and high-quality infrastructure and public services;
- Provide informal residents with an easier pathway to formalize their homes and obtain legal rights to them;
- Allow SDZ residents to participate in development decisions and profit from development as shareholders; and

- Create an economic hub that benefits the surrounding economy through supplier, purchaser, and technology-transfer linkages.

6.5.3: For IDPs

For IDPs, an SDZ would:

- Create meaningful economic opportunities through an environment that supports job creation and entrepreneurship;
- Empower them with education, employment, funding, and social services, thereby enabling them to become self-sufficient; and
- Pave the way for full integration in the host community through formal participation in civic and social affairs, education, business, work, and other aspects to society.

6.5.4: For International Development and Humanitarian Organizations

For international development and humanitarian organizations, an SDZ would:

- Maximize the impact of international assistance through a focus on institution building;⁵⁶
- Offers a highly resource-efficient intervention through the generation of a return on investment that attracts private-sector capital; and
- Provides a platform upon which to coordinate and deliver humanitarian and social services in an area.

Section 6.6: Potential Locations

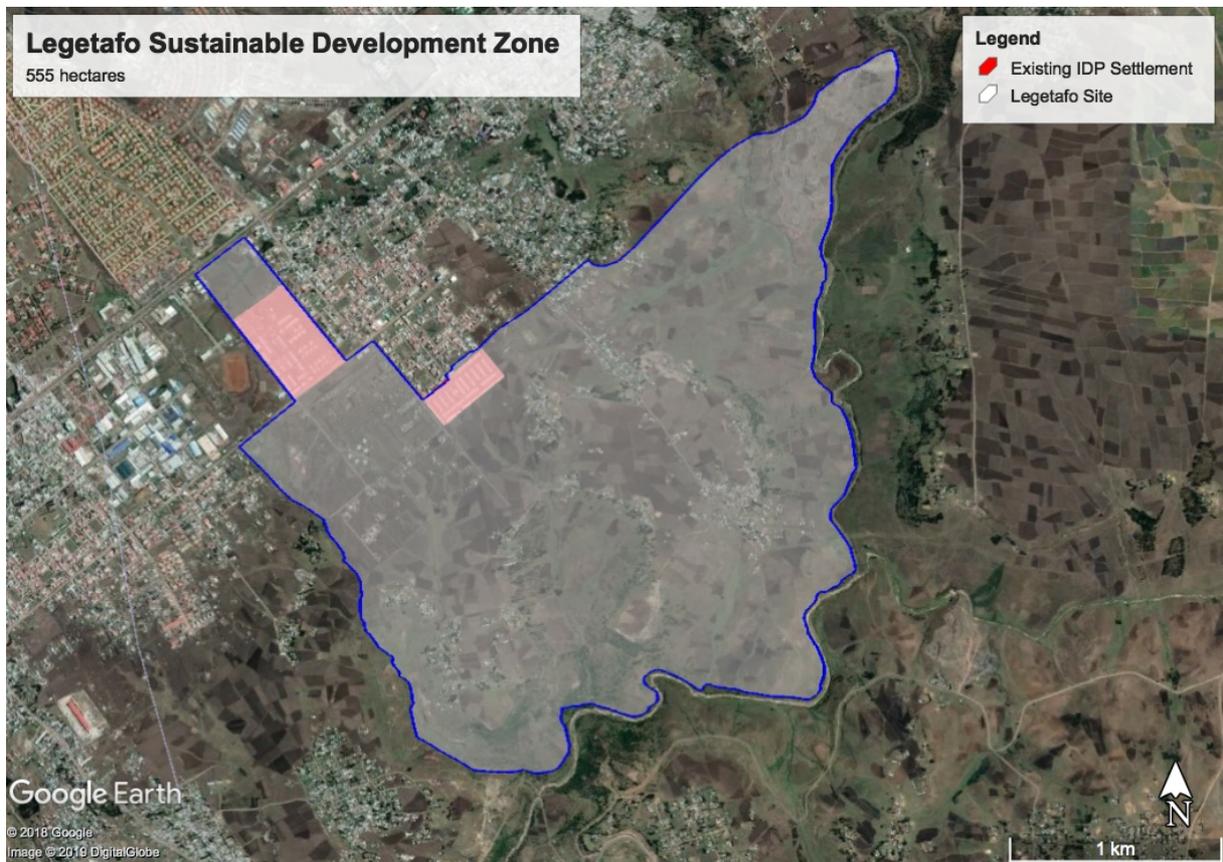
Given that the primary criteria for SDZ locations is availability of land, proximity to infrastructure and labor, and political and cultural support, there are numerous potentially suitable sites for SDZs. Provided below are maps of three sites in Oromia in the greater Addis Ababa area. The identification of these sites is for illustration purposes only. An in-depth investigation into the legal, cultural, political, and other factors of these sites has not yet been undertaken. Subsequent work is needed to study these and other potentially suitable sites for an SDZ.

Each map illustrates how the pilot phase of the SDZ might be demarcated. Each is relatively close to Addis Ababa, well connected to infrastructure, and near an existing population base (including IDP settlements).

⁵⁶ There is strong evidence to suggest that the quality of institutions is the largest factor in economic development. *See, e.g.,* Daron Acemoglu and James A. Robinson, *Why Nations Fail* (Crown Publishers, NY 2012)



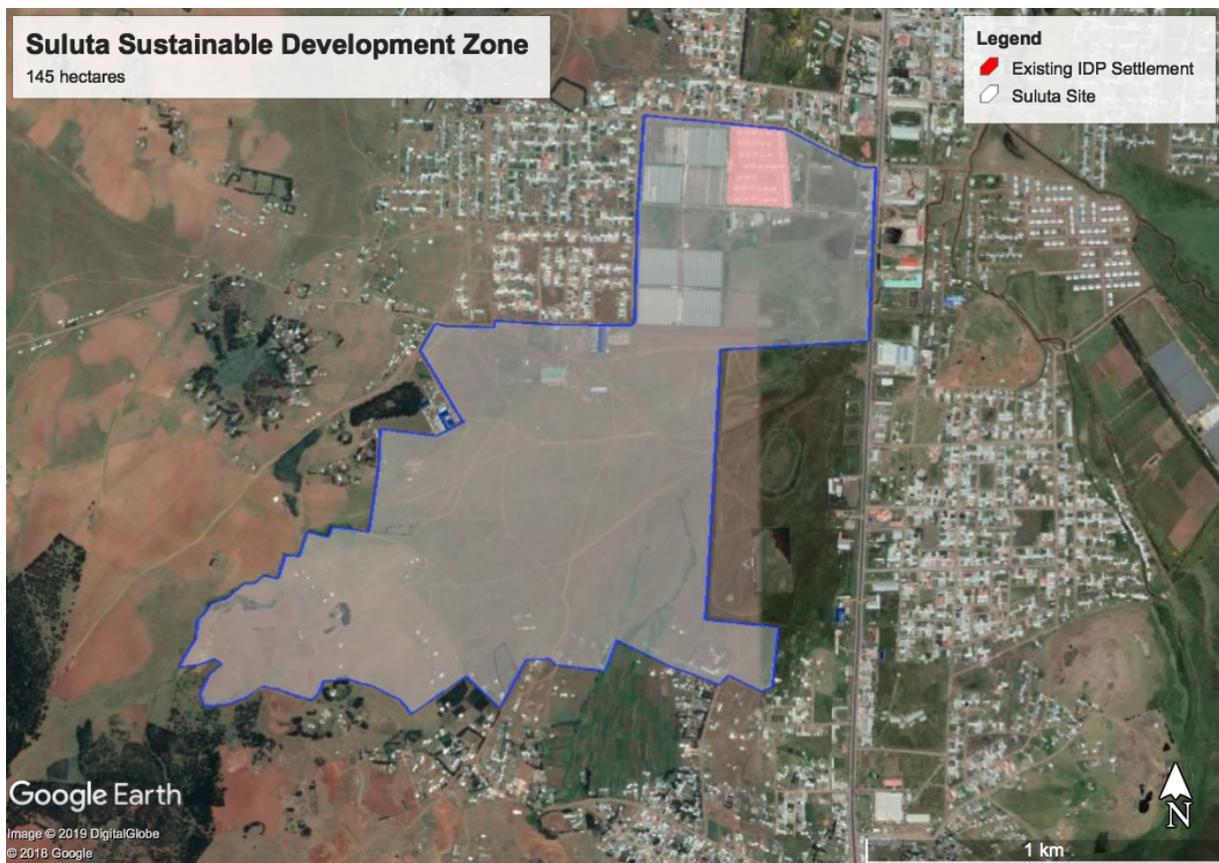
6.6.1: Legetafo



Relevant Characteristics:

- Good connectivity to metropolitan area of Addis through A2 road
- Low population density considering proximity to urban area (estimated population count 250 - 300), but with large nearby workforce.
- Village centers will be retained as core urban areas of residential and commercial zones, eliminating need for displacement.
- Currently occupied by a mix of middle-class, IDPs, informal settlers, and farmers. Luxury housing development is across the main road.
 - Lots of construction underway, as well as already occupied units
- Informal homes are being developed in an orderly way, with straight areas for roads.
- Mix of classes sets the framework for a diverse urban area, with a strong tax base and mixed uses

6.6.2: Suluta



Relevant Characteristics:

- Currently development is limited to fringes of the site due to lack of road access, however it is in a high-demand area.
- Existing IDP settlement and thriving export-oriented agro-business can form core of site.
- Large potential workforce in immediate area.
- Strong opportunities for new tenants to expand on agro-business processing and value added agricultural products.
- Site occupies mainly agricultural land, well-suited to residential development or agro-business.
- Site adjoins highway and has good connectivity to existing urban area
- Level terrain with room for future expansion to the south and west

- Existing population of approximately 100 living in dispersed rural homes can be upgraded or kept in place.

6.6.3: Bishoftu



Relevant Characteristics:

- Existing IDP settlement is near Hora Lake in zone with touristic potential and with limited land availability.
- New site (in blue) should be developed to the northwest, near the existing industrial park.
- Leveraging the transportation infrastructure and linkages from the park will promote industry clustering.
- Current site population is low, with one settlement that can provide urban core for residential and commercial development, eliminating the need for displacement.
- Site is flat and has ample land for expansion to the north, east, and west.

CHAPTER 7: RECOMMENDED NEXT STEPS AND BUDGET

In line with the above mentioned Overarching Roadmap for the Creation of an SDZ, it is recommended to establish a project implementation unit (PIU). The PIU would be tasked with technical experts who can advise and spearhead the project along all of the steps outlined in the above roadmap. The PIU should be established within the next 4 months. Prior to establishment a “pre-PIU” consultancy should be established.

Section 7.1: Pre-PIU Team

As an immediate next step, it is recommended that the current individual consultancies be continued for the next 3-4 months until the PIU is established. If the PIU is not established within that time, the consultancies should be extended to another 2-3 months.

Beyond the current consultants, two additional consultants should be added to supplement the work of the current three consultants by providing technical, administrative, human resources, and operations assistance. During this time, the consultants will serve as a “pre-PIU” and:

1. Develop the pre-feasibility study
2. Engage government and secure in-principle agreements from relevant government entities
3. Engage other stakeholders
4. Design and prepare details of PIU
5. Further refine project documentation
6. Mobilize finance with donors and private sector

Section 7.2: PIU Team

There are 3 options for the status of the PIU which must operate independently:

Option 1 (recommended): Formation of a “Social-Enterprise Special Purpose Vehicle” (SPV) with part of the operating costs provided by:

- UNHABITAT with donor money/seconded staff;
- Directly co-financed by private sector; and
- Government of Ethiopia, if possible.

Option 2: Full UNHABITAT administered project unit but with a separate reporting line to the Head Office Nairobi

Option 3: Start with a UNHABITAT Unit as per Option 2 but transitioning to Option 1 at a later stage

Details of the PIU should be prepared by the “pre-PIU” consultants, however preliminary rough planning elements are as follows:

- Addis Unit would consist of a Team leader, Operations Manager, Project Manager for the pilot SDZ (plus 2 additional Project Managers for 2 further pilots), Technical Sector Specialists for Governance, Urban Planning, Legal, Economist, Fundraising, Investment/Finance, Stakeholder Manager, Information manager, and support staff
- International support and backstopping team on a drawdown consultancy budget
- Office space, ground transportation, communication, travel
- Timeline: Establishment of PIU: May 2019; Implementation of project: May 2020
- Operations of the PIU should continue through the life of the SDZ program. Once the SDZ program has begun and SDZs are up and running (estimated at 2 years after formation), the PIU’s ongoing responsibilities will include:
 - technical support to institutions relevant to the SDZ program;
 - monitoring and evaluation of the SDZs for compliance with legal and social responsibility obligations and overall performance;
 - compliance assistance, and
 - liaison support among stakeholders.

The Terms of Reference for the PIU will feature the tasks necessary to guide the SDZ project through the roadmap recommended above all the way to SDZ establishment and operation. This includes:

1. Providing assistance to the National and Regional Parliaments with drafting Special Administrative Areas Legislation
2. Developing location specific operational implementation technical and finance plans
3. Mobilizing resources
4. Preparing full feasibility studies on specific sites to identify the actions needed to establish an SDZ and assess its economic, social and financial impact given the unique legal, political, social, environmental, and economic characteristics of the area
5. Gathering the necessary private-sector, donor, and government actors to establish the SDZ Developer
6. Providing technical assistance to the envisioned special administrative areas council, the EIC, and other relevant government actors involved with the special administrative areas and industrial parks program
7. Facilitating the negotiation of the lease agreement between the regional government and the SDZ Developer
8. Overseeing and assisting the SDZ Administration as it commences operations
9. General stakeholder engagement on international, national and local level
10. Oversee and backstop project implementation

Section 7.3: Budget

1. Consultancy (pre-PIU) (4 months)	
• 3 Senior Consultants (JR, MCM, KK) - 100 days/US\$600	US\$ 60,000
• Operations Consultants - 80 days/US\$400	US\$ 64,000
• Travel/Per diem - Lump Sum	US\$ 40,000
Total:	US\$164,000
2. PIU (first 12 months)	
a) 1 Coordinator-Senior Advisor P5	US\$ 200,000
b) 3 Project Managers P4/NO (US\$ 180,000)	US\$ 540,000
c) 8 Experts P3/NO (US\$ 150,000)	US\$ 1,200,000
d) 10 Support Staff/Assistants	US\$ 200,000
e) Office Operations	US\$ 100,000
f) Travel/Per Diem	US\$ 100,000
g) Transportation/Vehicles (2 Cars/rental)	US\$ 150,000
h) Backstopping Consultancy Lump Sum	US\$ 200,000
i) Miscellaneous contingencies	US\$ 50,000
Total:	US\$ 2,740,000

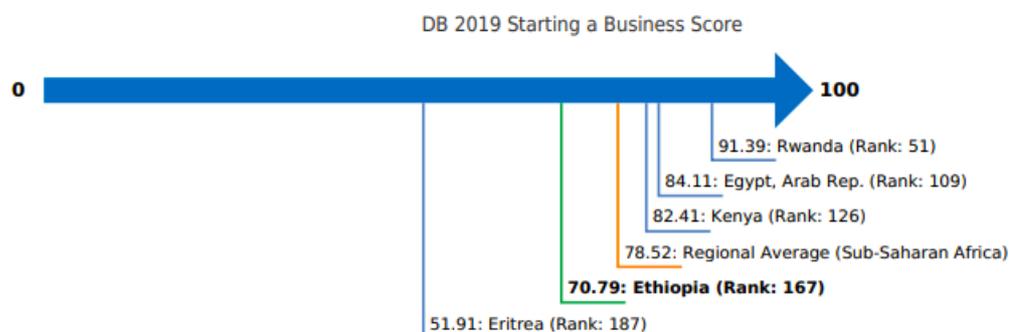
ANNEX A: MAJOR BUSINESS ENVIRONMENT CHALLENGES AND HOW SDZS WOULD ADDRESS THEM

SDZs would directly improve the ease of doing business in Ethiopia in several specific areas. Provided below are key barriers to starting and operating a business in the formal sector in Ethiopia and descriptions of how an SDZ would reduce them.

Starting a Business

Ethiopia made some positive reforms in 2016 to remove burdensome and duplicative requirements, however further improvements would lead to a strong increase in formal employment and business creation. Ethiopia is 167th in ease of starting a business. It takes a typical business 11 procedures, 32 days, and 52.7% of income per capita to start a new business. Procedures for a typical business include reserving a unique company name, authenticating company documents and a lease agreement at DARO, obtaining a tax identification number, registering the company and obtaining a commercial registration certificate, making a company seal, registering the company and employees with the Private Organization Employees' Pension fund, registering with the Ethiopian Revenue and Customs Authority for VAT, Publishing the name in a nationwide newspaper (15 days), reserving a unique trade name, obtaining a business license, and installing a cash registration machine. The Ethiopia Investment Commission one-stop shop intends to streamline the process so businesses can start up in as little as one-day, but is so far rarely able to achieve this goal.

Ease of Starting a Business in Ethiopia and Comparator Economies - Ranking and Score



Source: World Bank, Doing Business 2019 Economy Profile: Ethiopia

An SDZ Developer could improve the ease of starting a business by introducing its own system for business registration, included within an advanced online and on-site one-stop shop. This system could be modeled after systems in other countries and serve as a test case for the future nationwide business registration process. As a start, the Developer could pilot a digital system instead of the current paper-based registration process, as the EIC envisions adopting in the future.

Dealing with Construction Permits

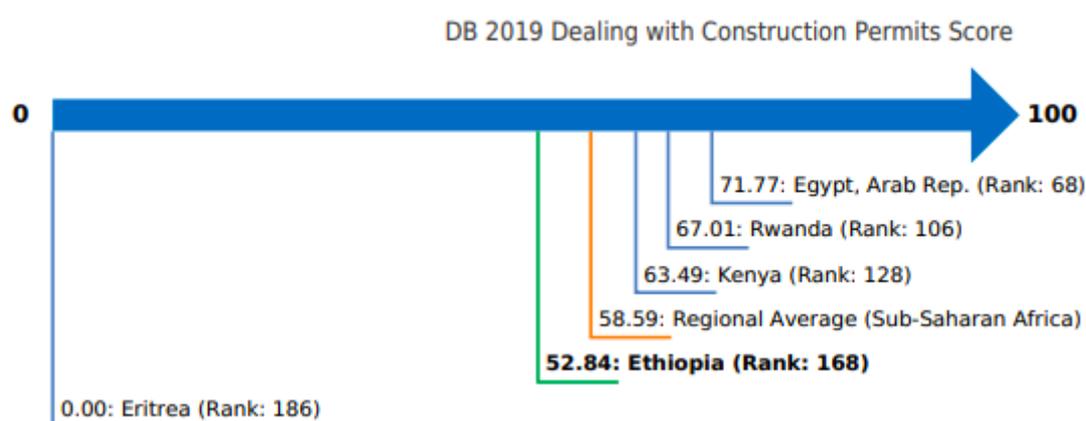
Obtaining construction permits are also a problem for businesses. Ethiopia is 168th in ease of obtaining construction permits.⁵⁷ A construction permit for a typical business takes 13

⁵⁷ See World Bank, Doing Business 2019 Economy Profile: Ethiopia.

procedures, 134 days and 14.4% of the total warehouse value. This system unfortunately only results in a building quality control score of 7 out of 15. Moreover, 51% of firms reported being requested or expected to give a gift or informal payment to receive their construction permit, compared with 31% on average for Sub-Saharan Africa.⁵⁸

An SDZ Developer could improve upon businesses' ability to acquire construction permits and reduce the incidence of corruption if it is delegated the power to review, inspect, and issue permits for construction projects within the SDZ, by following best practices adopted elsewhere and set a model for new construction permitting procedures nationwide.

Ease of Dealing with Construction Permits in Ethiopia and Comparator Economies - Ranking and Score



Source: World Bank, Doing Business 2019 Economy Profile: Ethiopia

Getting Electricity

The problems with obtaining electricity in Ethiopia are not as acute as other business constraints, however, an SDZ could still improve businesses ability to obtain electricity. Ethiopia ranks 131st in ease of getting electricity,⁵⁹ and 10% of businesses described it as their biggest constraint.⁶⁰ It takes 4 procedures, 95 days, and 891.8% of income per capita for a typical business to get powered. The system scores 0 out of 8 for reliability of supply and transparency of tariffs, due to a insufficient systems for monitoring outages, restoring services, publicizing tariffs, and more.

Almost all of the cost for businesses is for receiving and paying the estimate of power requirements and receiving internal wiring inspections. An SDZ Developer could, in theory, cover these upfront costs for all enterprises in the SDZ and perhaps provide its own independent power generation and reliability monitoring, depending on a cost-benefit assessment.

Registering Property

Difficulties with registering property affect not only the ability to start and operate a business, but also the ability to develop formal housing, as described earlier. Currently, Ethiopia ranks 144th in ease of registering property. It takes a typical business 7 procedures, 52 days, and 6% of property value to register property and the quality of land administration is only a 6 out of 30. By receiving the authority to maintain a cadaster for the SDZ and registering property in it,

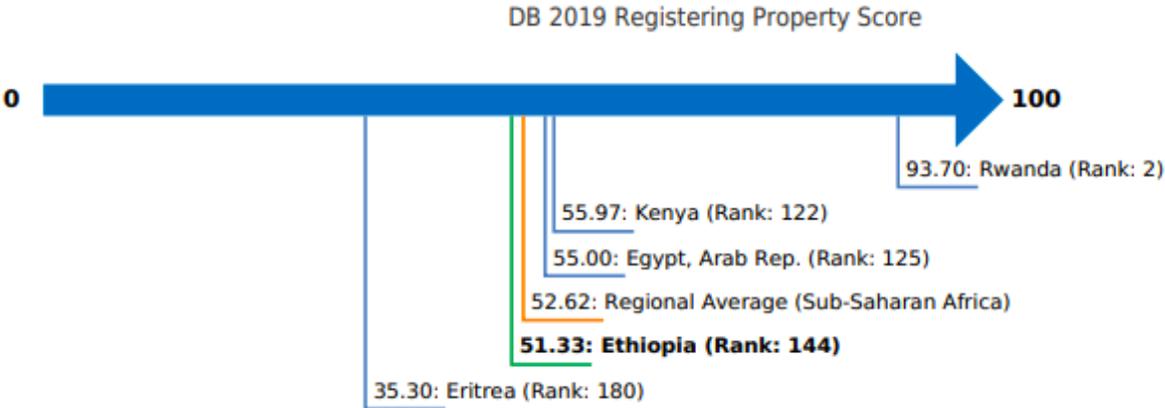
⁵⁸ See 2015 World Bank Enterprise Surveys: Ethiopia 2015 Country Profile.

⁵⁹ See World Bank, Doing Business 2019 Economy Profile: Ethiopia.

⁶⁰ See 2015 World Bank Enterprise Surveys: Ethiopia 2015 Country Profile

the Developer could greatly improve the ease of registering property and provide a model for future property registration procedures in Ethiopia.

Ease of Registering Property in Ethiopia and Comparator Economies - Ranking and Score



Paying Taxes

While reforms to the tax law in 2016 improved the burden of paying taxes, an SDZ could improve tax administration for people and businesses in the SDZ. Ethiopia ranks 130th in ease of paying taxes. The typical business spends 300 hours, 29 payments, and 37.7% of its profit on taxes. Senior management spend on average 11.9% of their time on tax-related regulations, and 17% reported being requested or expected to give gifts or informal payments in meetings with tax officials. 8% of firms reported tax rates as the top business environment constraint and another 7% reported tax administration as their top constraint. Spending 37.7% of profit on taxes is relatively competitive with other Sub-Saharan African countries, which average 46.8%. The 37.7% figure primarily includes corporate income tax (30%) and labor tax and contributions of 12.4%.

The Developer could improve the business environment by maintaining an independent tax collection and enforcement system for SDZ individuals and enterprises. The SDZ could collect taxes owed to the national, regional, and city governments and distribute it to them, cutting out inefficiency, bureaucracy, and corruption.

Infrastructure

Businesses and individuals in Ethiopia also struggle with infrastructure weaknesses. Ethiopia ranks 120th out of 140 countries for infrastructure in the World Economic Forum’s Global Competitiveness Report. Particular weaknesses are road connectivity, quality of roads, electrification rate, and water supply. The SDZ Developer could improve the quality transportation and power infrastructure within the SDZ and partner with the regional and national government to improve connections to the major cities, seaports, and airports.

Other Potential Reforms in the SDZs

The Ethiopian government could use the SDZs to set the stage for other future anticipated reforms, such as allowing competition against state-owned monopolies. For instance, it could pilot competition in the telecommunications field, by allowing enterprises in the SDZ to compete with Ethiotel. Jamaica similarly used its free zones to initiate privatization and

competition of its telecommunications infrastructure. Ethiopia currently ranks 138th out of 140 countries in information communication technology (ICT) adoption.⁶¹

Moreover, Ethiopia could improve its companies law by launching reforms in the SDZ.⁶² Ethiopia ranks 178th out of 182 countries at protecting minority investors in the World Bank’s Doing Business Report. The World Economic Forum’s Global Competitiveness Index lists Ethiopia as having one of the worst corporate governance regulations.⁶³ Faced with similarly weak corporate and financial services laws, the Dubai and Abu Dhabi have both created special zones with new corporate laws in the Dubai International Financial Centre and the Abu Dhabi Global Markets. Both zones are modeled after the companies laws of England and Wales.

ANNEX B: SERVICES PERFORMED BY CONSULTANTS AND BIOGRAPHIES

To develop this proposal UN Habitat contracted three consultants, Joachim Rücker, Kilian Kleinschmidt, and Michael Castle-Miller. These consultants all performed a combination of off-site desk work and 10-11 days of field visits and stakeholder meetings in Addis Ababa from 10 - 20 December 2018. Provided below is a schedule of their meetings in Addis Ababa and each of their biographies.

Date	Meeting
10 Dec	11.00 - IPDC 3:00pm - UNIDO
11 Dec	8:30 am - MoUDH- Genete 10 am - IOM Afternoon - Camp visit (Legetafo) 18.00 - Reception
12 Dec	Camp visit (Legetafo and surrounding informal settlement)
13 Dec	10.00 am: Meeting with German Ambassador (JR) 13.30 - UNHCR Representative 19.00 - 21.00 Dinner with German Federal Government representative at Hilton (KK, JR)
14 Dec	9 am - UNDP 1:00 pm - UNOCHA 4:00 pm - NRC
15 Dec	Desk Work
16 Dec	Off
17 Dec	Field Visit (Bishoftu and surrounding community) Joint working dinner

⁶¹ See World Economic Forum, Global Competitiveness Index (2018).

⁶² See Hussein Ahmed Tura, *Overview of Corporate Governance in Ethiopia: The Role, Composition and Remuneration of Boards of Directors In Share Companies*, 6 Mizan Law Review 1 (June 2012).

⁶³ See World Economic Forum, Global Competitiveness Index (2018).

18 Dec	9:00am - Investment Commission Oromia Commissioner appointment Afternoon - Field Visit (Sululta IDP settlement and agricultural business) 17.00-19.00 meeting with Operations Manager of Tycoon Real Estate 19.30 Dinner with Mengesha Kebede
19 Dec	9:30 am - EU 13:00 -- US Embassy 14.30 Lunch with local real estate developer and bank 4:00pm - Internal wrap-up discussion in UN-Habitat office 7:00 pm - Farewell
20 Dec	10:00 am: Meeting of Solutions and Resilience Working Group for IDPs in Ethiopia, chaired by Ethiopian Government / NDRMC 5:00 pm - MoFEC -- PPP state minister, Dr. Teshome

Joachim Rücker

Dr. Joachim Ruecker is an economist, independent consultant and former Ambassador of Germany. Until 2017, he was also the Special Representative of the Federal Government of Germany for the Middle East Stability Partnership. In this capacity, Joachim Ruecker was personally involved in implementing the “Jordan Compact”, a project combining Special Economic Zones in Jordan with new job opportunities for Jordanian citizens and Syrian Refugees. Previous positions include Permanent Representative to the UN in Geneva, President of the UN Human Rights Council, Special Representative of the UN Secretary-General in Kosovo and Inspector-General of the German Foreign Office. In a first phase of his service in Kosovo, Joachim Ruecker was responsible for economic reconstruction. He conducted a comprehensive program for privatization and for restructuring of public enterprises and helped laying the foundations for a functioning market economy including the creation of industrial parks / special economic zones. For almost a decade, Joachim Ruecker served as Mayor of the industrial city of Sindelfingen in Germany (home of Mercedes production). He has broad experience in decentralization, local governance, public infrastructure & housing and the structuring and steering of utilities.

Kilian Kleinschmidt

Kilian Kleinschmidt is an international networker, humanitarian and refugee expert with 30 years of experience in a wide range of countries, emergencies and refugee camps as United Nations official, Aid worker and Diplomat. He is the founder and Chairman of the startup Innovation and Planning Agency (IPA) which aims at connecting the millions of poor and disadvantaged with relevant and under-utilized resources and modern technologies of the 21st century through its project SWITXBOARD <http://www.switxboard.net>. He is part of a number of initiatives and Projects which aim at global connectivity through better use of globalization. He is currently developing a number of ventures which aim at sustainable investment and social impact in very fragile environments.

He most recently became known as the “Mayor of Za'atari” when he managed the refugee camp of Za'atari in Northern Jordan from 2013-2014 on behalf of UNHCR. Za'atari has become a symbol for new and innovative approaches in refugee and humanitarian management under his leadership. He is now challenging the Humanitarian Aid Sector through a range of new and unorthodox partnerships, technologies and ways of financing building on networking and swarm intelligence rather than hierarchies and ineffective bureaucracies. His work on emerging

cities, Special Development Zones and urbanization of refugee camps is widely recognized as the way forward dealing with mass migration, population shifts and transformation of society.

Previous senior roles included Deputy Humanitarian Coordinator for Somalia, Deputy Special Envoy for Assistance to Pakistan, Director for Communities and Minorities in the UN administration in Kosovo, Executive Secretary for the Migration and Refugee Initiative (MARRI) in the Stability Pact for South Eastern Europe and many field based functions with UNHCR, UNDP and WFP. He worked extensively in Africa, South Eastern Europe, Pakistan and Sri Lanka and during the European refugee crisis advised the Austrian Minister of Interior on Refugee reception centres. Most recently he was a Special Advisor to the German Minister of Development on Refugee issues and innovative partnerships (2016). In 2017 he and a global IPA team developed a strategy on stabilisation of migration flows and development in Africa for the Chancellor of Austria. Currently his team and network are working on new approaches to the stabilisation of Libya through partnership acceleration for businesses and municipalities and the establishment of Special Development Zones.

He has published three books - “Weil es um die Menschen geht” (ECON 2015) , “Beyond Survival” (Dumont-Mair 2016) and “Tod dem Helfer” (Dumont-Mair 2017) and authored a number of articles on refugee and migration issues. He is a renowned public speaker in conferences, TEDx and other events.

Michael Castle-Miller

Michael is a legal and policy consultant who has helped develop special economic zone (SEZ) programs in over 20 countries in the Middle East, Southeast Asia, Latin America, and Africa. Over the course of his career, governments and private companies have relied on him to draft regulations, establish administrative agencies, introduce investment climate reforms, structure public-private partnerships, and promote socially and environmentally responsible development projects. In addition to serving as CEO of Politas, he is also the Founder and Executive Director of Refugee Cities, an NGO applying SEZ frameworks to expand opportunities for migrants.

Michael's professional experience ranges from legal and policy consulting to real estate negotiation, and from organizational management to community engagement. Michael has served as the Managing Director of Locus Economica, a boutique SEZ consulting firm advising on numerous World Bank, UNIDO, and direct-government projects. He has also been a consultant with the World Bank, Legal Vice Presidency, specializing in urban law and development issues. Before that, he worked for the Public International Law and Policy Group, where he provided legal assistance to the governments of South Sudan, Georgia, and Yemen on a variety of matters.

Michael earned a J.D., *summa cum laude*, from American University, Washington College of Law and an M.A. in International Politics from American University, School of International Service. His publications in legal journals cover the political economy of international trade and investment, comparative local government, “Charter Cities,” U.S. immigration law, and expropriation jurisprudence. He regularly gives talks and participates in panel discussions on SEZs and refugee cities at conferences internationally.

Michael is a member of the Pacific Council on International Policy and a Senior Program Officer of WEPZA, a trade association of SEZ practitioners. He is also an active member of the New York State Bar Association and licensed to practice law in New York.