

WOLKITE UNIVERSITY

**COLLEGE OF SOCIAL SCIENCE AND HUMANITIES
DEPARTMENT OF GOVERNANCE AND DEVELOPMENT STUDIES**



TTHEISIS TITLE: FACTOR AFFECTING THE ROLE OF PRIVATE INVESTMENT IN AGRICULTURAL SECTOR IN SOUTH WEST SHOA

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A SENIOR ESSAY SUBMITTED TO THE DEPARTMENT OF GOVERNANCE AND DEVELOPMENT STUDIES AS A PARTIAL FULFILLMENT OF THE REQUIREMENT FOR THE AWARD OF BACHELOR OF ARTS (BA) DEGREE IN GOVERNANCE AND DEVELOPMENT STUDIES.

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Wolkite University

January 2021

Declaration

The study was conducted on factor affecting private investment in agricultural sector in South West Shoa. This study submitted in partial fulfillment for Bachelor of Arts degree in Governance and Development Studies in Wolkite University is entirely our own work and has not been submitted anywhere else for the award of degree, diploma, and fellowship to any other academic institution. To the best our knowledge and belief, all sources of materials used for this study are dully acknowledged.

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Acknowledgement

First of all we would like to thank our God for helping us to accomplish this thesis successfully. Secondly, thanks to our respected and honored advisor Tamiru Berafe (Asst. Prof) for giving his unrestricted comments suggestion and offering useful advices until the finalization of this research. Thirdly, we would like to thank Wolkite University specially the College of Social Science and Humanities and Department of Governance and Development Studies for everything they did to us. Fourthly and finally, we would like to genuinely thank everybody for their respective contributions.

Abstract

Ethiopia is one of the leading agrarian economies due to the fact that it has huge resource potential to attract domestic and foreign direct investment. The objective of this study was to identify and analyze factors affecting private investment in the agricultural sector in South West Shoa. The results of the micro level study showed that access to credit, access to infrastructure facilities, access to market, market factors, investment incentives and agro climate factors are significant determinants of agricultural investment in the study areas. The results of this study also revealed that most of the problems encountered by agricultural investors were lack of commitment to invest, lack of adequate finance and institutional constraints. The intervention program might be viewed as strengthening institutional set-up and improving the micro economic stability in one hand and encouraging investors to invest on the other hand. This could be done by establishing true, independent and efficient institutions and eliminating unnecessary regulations so as to create access to credit, provide infrastructure facilities to agricultural investment. The Oromia regional governments should work with investors to make a conducive investment climate and open up its doors to investors by applying appropriate policies and investment incentives to achieve the long term development of the regional economy.

Abbreviation

FAO	Food and Agricultural Organization
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
ICT	Information and communications technology
WFP	World Food Programme
OECD	Organization for Economic Cooperation and Development

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CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND OF THE STUDY

Investment is a key variable necessary for economic growth and development of countries (Levine & Renelt, 1992). Ouattara (2004) defines investment as a broad and open ended, with a list of specific types which are indicative rather than conclusive. Mertonson (cited in Bayai & Nyangara, 2013) states that the term ‘investment’ is essentially ambiguous. Moreover, studies done by Antonakis (2008), Seruvatu and Jayaraman (2001), Ndikumana and Verick (2007), Bakare (2011) and Dehn (2000) defined investment in different ways. Among them, some define investment as an activity that involves the acquisition of goods which are intended not to be consumed and others define as the act of obtaining income generating assets either as additions to existing assets or to replace assets that have depreciated. These studies classified the term investment as private investments (investment spent by residential/ nonresidential investors and their objective is mostly for profit and risk diversification and public investment (investment spent by the public or government). Regarding public investment, Keynes (1936), believes that there is a need for government intervention to activate and regulate the economy. However, private investment is regulated by private investor.

According to Bakare (2011) and Dehn (2000), since private investment is more efficient and less closely associated with corruption, it has a stronger and more positive effect on economic growth than public investment. Similarly, Batistar (2015) supports the idea of private investment playing a greater role than public investment in determining economic growth. The role of the private sector is important in terms of its ability to allocate and employ resources efficiently and its contribution to the quantity of domestic investment. According to the study conducted by Frimpong and Marbuah (2010), United Nations (2002), and World Bank (2004) report, private investment have an important role in job creation, growth expansion and poverty reduction. Meaning that the mobilization of private investment is essential for the development of a country

and this can contribute directly to economic growth. On the contrary, where the growth of private investment is low, the productive capacity of the economy fails to increase and it results in lower rates of growth and job creation, and fewer opportunities for the poor to improve their livelihoods.

Furthermore, according to Access Capital Investment Assessment Report (2011/2012), the ratio of private investment to GDP in Ethiopia has been averaged between 5.8 and 10%. This ratio is below the levels being practiced in successful nations' economies, which is required to support economic growth needed for employment creation and poverty reduction.

Due to the fact that private investment is below expectation, the government of the Federal Democratic Republic of Ethiopia has recognized and paid due attention to the promotion and development of private investment which includes working a lot to attract private investors for investment in different sectors of the economy.

According to government policy, the Ministry of Agriculture and Rural Development has given the responsibility of providing technical support for private sector in agriculture development to the Agricultural Extension Department through the Private Support Team. The support ranges from providing information, technical support, and facilitation of other public services as long as they are related to the success of the investment project. Depending on the extent of private sector engagement, the support team will also be established at regional and Woreda level. Similarly, the support service will ensure proper utilization of the natural resources and other responsibilities the investment has committed to. Those investment incentive packages are implemented in all cities and towns of the country. However, the present state of private investment in agricultural development in Ethiopia is at a low level despite the availability of infrastructure, social impacts and political factors. But, it should be noted that there are still abundant opportunities for investors to consider the investment. Though, many projects took investment license from the town; there are some projects which transferred from planning to implementation and operation (Negarit Gazeta, 2008).

Generally, role of private investments in Ethiopia are not performing as expected. Some go to the operation and performing their task while other is not. Many problems have been influencing factor for the growth of private sector in the economy and subsequent investment patterns. In

addition to these, the role of private investment has been influenced by other different factors such as lack of infrastructure, size of market, level of education and political instability that must be handled with proper policy frame. That is why this paper is focused to identifying the factor affecting role of private investment specifically in the agricultural sector. Therefore, this research will to fulfill the gap tire to investigate factor affecting role the role of private investment in agricultural sector.

1.2 Statement of the Problem

The private investment sector plays a vital role in the growth process of developing countries and it determines the rate at which physical capital is accumulated (Jongwanich & Kohpaiboon, 2006). Private investment has been a major economic powerhouse for developing countries (Ouattara, 2005).

Empirical evidence (Ghura, 1997) indicates that private investment has a stronger, more favorable effect on growth than government investment, probably because private investment is more efficient and less closely associated with corruption. Although the investment climate has improved greatly in recent years, there are still many aspect of investment promotion where improvement was urgently needed. Investment climate means refers to economic, financial and socio-political condition in the country that affects private investor. In other words, even if the situation or investment has improved from the Dergue period the participation of private sector is not satisfactory. Specially, private investment in agriculture sector preserves a multifaceted responsibility in achieving the targeted environmental sustainability, economic growth and development as well in reduction in poverty for the less and developing countries.

Mikhail (2014) addressed that private sector investment in agriculture sector is necessary to subordinate the pressure of the domestic demand occur with climate change, growth in the population, increase demand for daily use items containing food items, meat, milk, wheat, vegetables, energy products etc. However, to magnify and encourage the role of private investment in agriculture sector satisfactorily, the effort of Ethiopia is weak.

Lack of investment has been identified as a fundamental cause of the stagnant production and low productivity of Ethiopian agriculture. The United nations Food and Agricultural Organization (FAO) estimates that in order to double food production by 2050 (a target that must

be attained to feed growing populations and to ensure a basic right to food), developing countries need an additional USD 30 billion per year in investment. Public investment resources are limited by budgetary pressures, and official development assistance to agriculture has been declining over many years. The private sector in developing countries has tended to have little capacity to fund investment. International investments therefore, have a potentially important role to play (David Hallam, 2009).

At the same time, a number of countries are enthusiastically seeking to attract such investments to exploit surplus land that is unused or underutilized. However, selling, leasing, or providing concessional access to land raises questions about how the land concerned was previously being utilized, by whom, and on what tenure basis. “It is true that much of land in sub-Saharan Africa is currently not utilized to its full potential, ‘surplus’ land overall does not necessarily mean land is unused or unoccupied” (Ibid).

As the fact reveals Ethiopia is believed to have about 74.3 percent of arable land from its total land area. However, so far only about 18 percent of the farmland is being utilized by local farmers with traditional backward farming techniques. Surprisingly, as a whole, the farmland which is given to local and foreign agricultural investors within the past few years is not less than 5 percent (The Ethiopia Macroeconomic Handbook, 2010).

Ethiopian Investment Authority data show that approximately 1,100 foreign agricultural investors have registered since 2005, though only around 6 percent (64 in number) are reported to be operational so far (Ibid).

Even though the agriculture is currently being invested on by private investors’ who are believed to have better experience and advanced technological equipment’s that can increase the yield of agricultural production far better than that of local farmers, yet it is far from addressing the problem of food shortage and hunger that is prevalent in the country. The number of evidences shows that private investment in anywhere depends on a number of factors which significantly affects the growth of the sector.

Thus, in this study, identifying challenges of private involvement in agricultural sector is a key step to know the factors responsible for the poor performance of South West Showa’s government in making use of private agricultural investments so as to enhance the benefits of the

investment and minimize the threats that could come along with the investment. Therefore, this study will identify the factor affecting the role of private investment in agricultural sector. And this research will try to fulfill the gap in factors affecting role of the private investment in agricultural sector in South West Showa.

1.3 Research question

The study has attempted to answer for the following questions;

1. What are the major factors that affect role of private investment in agricultural sector?
2. What are the trends of private investment in Ethiopia?

1.4 OBJECTIVES OF THE STUDY

1.4.1 General objective

The general objective of this research is to assess the factor affecting role of private investment in agriculture sector.

1.4.2 Specific objective

1. To identify major factors that affect role of private investment in agricultural sector.
2. To examine the trends of private investment in Ethiopia.

1.5 Significance of the study

This study was initiated to identify the current factors that affect the role of private investment in agricultural sector. In doing so, the researchers presume that the study will add knowledge in area of private investment in agricultural sector.

In general the results of this study may benefit policy makers and development planner in re-designing appropriate policies and strategies.

1.6 Scope of the study

This study was focused on the identifying the factors affecting the role of private investment in agricultural sector only. Private investment in other sectors was not included in this study. Private investment in small scale farming in particular is the main focus of the study. Further the study analysis the trends and factor affecting private investment in agricultural sector of Ethiopia. In order to identify those factors, the survey was conducted in South West Whoa.

1.7 limitation of the study

The term investment is abroad topics. Within this broad topic, we face Corona virus pandemic. We cannot gate sufficient data. Because of the availability of data from investment office, the study was limited on document from investment office.

The limited time available to accomplish the study may restrict the researcher from consulting many books, empirical studies and relevant similar case studies that have been done in least developed countries. In addition lack of helping tools such as personal computers (laptop) and researcher's limited experience might have an impact on the conclusion of the study. Finally, the small amount of fund apportioned to undertake the research had its own drawback on the study.

1.8 METHODOLOGIES

1.8.1 SOURCE OF DATA

The study has used secondary sources of data. This secondary data were collected from different researches done in different part of Ethiopia and investment office. Secondary sources official documents that their recorded and other records related to the case under study were used.

1.8.2 METHOD OF DATA COLLECTION

In the data collection we were used secondary data only. Data was collected from different document and recorded researches. On the other hand secondary data will be collect from unpublished document of organization annual reports & internets.

CHAPTER THREE

LITRATURE REVIEW

2.1 Overview of Private investment in Ethiopia

As stated in many research, private sector investment started in Ethiopia during Emperor Menelek II with acquisition of land. This era was characterized by scramble of principalities more or less waging unsettled war against each other for control of the area and also to defend Ethiopia from foreign aggression. In this process acquisition of private property in the form of land, began and was seen as sign of prestige. However, development of the land by the owners for economic purposes was unknown because of rudimentary market linkages. Private sector started developing during Emperor Haile Selassie's time. Even during this period much of the private sector clustered around land and related activities. Land owners developed commercial farms and as a forward linkage agro-processing small scale industries were established by private owners. The constitution clearly supported the right of individuals to possess and develop private property.

Land, on which the livelihood of 90% of the Ethiopia populations is based, was privately owned and owners had confidence to develop it until confiscated by the Socialist Military Regime in 1974. In other sectors such as transport and services there were no big private investments. There were very few establishments that involved the private and public jointly owned companies. Private sector development cannot be discussed much during the socialist military government. The policy was very clear and was to systematically hinder the private sector. Since the beginning of the regime, the impact of the policy was total failure. The country experienced chronic food shortages. This resulted from confiscation of private property mainly land. Even after the collapse of the Regime, this situation continued at higher scale. The recent joint World Food Program (WFP) and Food and Agricultural Organization (FAO) report estimated that more than 40% of the agriculturally based population cannot feed itself. Structural food deficit, poor land management and other policy related problems exacerbated the indigent state of food production in the country. (Adugna, 2013).

Knowing of the fact the importance of private sector, the Socialist Government introduced a new period in Ethiopian political and economic history on March 5, 1990. In this economic history the change introduced was far reaching. The proclamation recognized the role of private sector development and stated that private sector could compete with public sector in all the economic sectors. The policy, however, did not last long. Between March 1990 and May 1991 very little implementation of the policy was seen. When Transitional Government took power, the economic policies were largely based on the preceding policy that focused on deregulation of banned territory and prices control. Privatization of public ownership was clearly pronounced. Sectoral policies were designed and proclamations were pumped and implementing line organizations such as Privatization Agency. (Investment Proclamation 769/2012).

2.2 Ethiopian investment policies and trends of private investment

Historically private Investment started to put its fingerprint in the Ethiopian economy during the imperial era, specifically during the 1950. Relatively an encouragement has extended to foreign investors during imperial regime (Michael, 2003).

The aftermath of the revolution that took place in 1974 however has brought a change of policy that ruled out the role of private sector. Accordingly the state took up the leading figure in economic development. Therefore, the strategy of government targeted at demolishing private investment both domestic and foreign in particular.

After the downfall of the socialist regime, a liberalized economic policy was adopted by present government. It was aimed at raising the role of private sector. To this effect the Ethiopian government issued a new investment code in 1992, which was a means to robust and build up the private sector participation in the mobilization of resources and formation of capital as part of liberalization process after the end of military years during which the private sector was denounced.

2.2.1 The Imperial Era

Ethiopia moved from a predominantly feudal system that simultaneously recognized kinship, tenancy and private forms of tenure. At that time where policies issued by the government to encourage private investors and public investment, particularly private sectors' investment. In 1966, the Investment Proclamation No. 242/1966 was enacted.

What is special to those Decrees was that they did not provide investment areas for the government. Thus, investors could invest in all areas of the economy with no restriction. They also provided investment incentives which included: import export income tax exemptions, income tax holidays. It was also possible for foreign investors to own land required for their investment.

2.2.2 Private investment in the Dergue period

The common economic policy and the Dergue regime which was centered on socialist economic system, gave a dominant role to the public sectors by limiting the role of foreign and domestic investment. The policy of the military of government had started to be implemented by the nationalizing different private property and instituted central planning as a means of allocating resources. This was possible by using proclamation notice and declaring 1975, Dergue's policy of nationality action was enacted as a proclamation no_26/1975. according this proclamation, the military government nationalized a number of industries, commercial farms, financial intuitions, houses, land etc. and restricted private portions to a few lines of activities and imposing capita selling on them.

2.2.3 Private Investment after Dergue period

Ethiopia currently has a federal structure that allows for considerable autonomy to the regional states and decentralized decision-making up to the lowest level in political, economic and social spheres including for administration of land. Since 1991, Ethiopian government issued a different agricultural policy, which basically aimed at encouraging the participation of private investors in the agricultural activities. According to the Rural Development Policy and Strategy

document, the basic ingredient and resource the country has for the agricultural development is the abundant land and labor. The policy and conditions of leasing land to both foreign and domestic investors for commercial farming is labeled as “open door” as it is highly favorable to investors (Oakland Institute, 2011; Rahmato, 2011). The policy opened the door to the extent that the government made purely commercial agreement with investor charging them only a dirt cheap rent. What they choose to do on the land for their own commercial intent is their own business.

Federal constitution explicitly gives private investors the right to lease land for different purposes (Article 40(6)). The Federal Rural Land Proclamation 456 (FDRE 2005) under Article 5(4) allows investors to acquire rural land for agricultural investment: ‘Private investors that engage in agricultural development activities shall have the right to use rural land in accordance with the investment policies and laws at federal and regional levels.’ The purpose of this legal provision is to attract investors who have the capital and technology to invest in small- and large-scale agriculture, mainly in the lowland areas of the country, where availability of infrastructure (roads, communications, etc.) is very limited. Initially, investors were not interested in these lowland areas because of the poor infrastructure and hostile environmental conditions. However, the federal and regional governments offered tax holidays and other incentives to attract domestic and foreign investors (Proclamation 280 (FDRE 2002), Regulation Number 84 (FDRE 2003), and Regulation Number 146 (FDRE 2008)).

New investment proclamation also provides a number of incentives to potential investors in different forms. Starting from minimizing the capital requirement for a single investment up to the highest tax exemption period-8 to 9 year-to investors engaged in forest development (Investment Proc. No. 769/2012; Regulation No. 270/2012). Foreign investors are also allowed to repatriate the profit and other incomes acquired from their investment in convertible foreign currency (Article, 26). Investment regulation No. 270/2012 provides more details of the privileges given to foreign investors. In the detailed income tax exemption section, the Regulation states that investors engaged in agricultural investment outside of Addis Ababa and Oromia Special Zone Surrounding Addis Ababa are entitled to 3-5 years of income tax holiday. The agricultural investment investors do in Addis Ababa and the regulation is trying to give tax privilege is quite not clear as big agricultural investment in the capital may not be expected.

Income tax exemption for an investor for almost for a decade would possibly made the country to lose the revenue supposed to be collected and thereby used for the wellbeing of the country. As provided in article 5 of the same proclamation, an income tax deduction of 30% for 3 years after the expiry of the former exemption period are given to encourage any potential investors to engage in the least developed and relatively low population density regions who establish a new investment venture. Investors are also allowed to import duty free capital goods and construction materials for new investment venture and for expansion (Article, 13). Moreover, investors who export or supply to an exporter at least 60% of their products or service input are entitled to have 2 more years of income tax exemption (Article, 7).

2.3 Empirical study in Determinants of Private investment

By focusing on different variables that determine private investment, many researchers have studied private investment from different perspectives. The researcher provides an overview of empirical studies on private investment and this is presented as the following.

The limited availability and poor quality of roads and bridges in most developing countries have been a major handicap to effective transportation of produce from the rural areas to various markets, resulting in high post-harvest losses and rendering agricultural investments less profitable. Similarly, access to other basic infrastructure such as electricity and telephone lines in rural areas is limited. Irrigation infrastructure is essential for investments in primary production, particularly in the horticultural sector, yet only 4 percent of the area under production in developing countries is irrigated, compared to 39 percent in South Asia and 29 percent in East Asia (World Bank, 2007). Transportation and information and communications technology (ICT) infrastructure are a precondition for the development of agro-industries; where absent or inadequate, value-addition is curtailed in the sector (Henson and Cranfield, 2008). Data from the World Development Indicators show low levels of ICT penetration for most developing countries (World Bank, 2009a). In addition to these basic infrastructural needs, the perishability of agricultural products requires special facilities such as cold storage and refrigerated transport. Moreover, agriculture-specific infrastructure such as laboratories for product testing and

certification purposes is a must if the sector is to be competitive, particularly in compliance with the sanitary and phytosanitary standards for world food trade.

From economic theory and empirical observation, land is one of the major factors of production. The results at a micro level showed that the probability of individuals to invest their capital is significantly and positively influenced by access to land (Baye et al., 2005). The variable treats as continuous variable, because it incorporated the amount of the land size of investors and it is hypothesized that the variable has a positive impact on investment decision. Legal and Judiciary system (Judsys): This variable refers to the respondent's perception of the efficiency of Bureaucratic red tape (Bureta): It is a composite index, based on six questions, which assessed the opinions of the sample respondents about the efficiency of the government bureaucracy which is provided by the time required to get investment license, land, construction permit, import machineries, bank loans and operation license. .

Lack of adequate infrastructure in the United Republic of Tanzania is blamed for high energy and transportation costs, which have caused the country's commodities to be less competitive (Msuya, 2007; World Economic Forum, 2009). On the other hand, South Africa's superior infrastructure has helped lower its production and distribution costs, hence made its products competitive in the global economy. Poor infrastructure is in fact found to be more constraining to agriculture prosperity than trade barriers (Msuya, 2007).

Haroon and Naser (2011) using consumer price index to refer to inflation rate, they examine the determinants of investment in Pakistan. They found that, private investment is a function of inflation rate, indirect taxes, subsidies given by the government, discount rate, gross domestic product, domestic savings, government development expenditures, amount of debt servicing, and past private investment (investment experience). Ang (2010) carried out a study on the availability of financial resources and a greater level of aggregate output has a strong positive impact on private investment, while macroeconomic uncertainty has a negative influence. Both foreign direct and public investments have a complementary effect on private investment. Matwanga (2007), found a positive influence of savings, GDP growth and public investment on the behavior of private investors in Kenya. Similarly, Kariuki (2003) found that public investment positively affects private investment while studying the determinants of gross fixed capital formation in Kenya. Abhijeet and Dinesh (2010) found that investment experience is

significantly determining both the investor behavior and investment decision. The study concludes that increase in the experience will be helpful to the investor. Frimpong and Marbuah (2010) conducted an empirical assessment of factors that have stimulated private sector investment in Ghana. Using the co-integration and error correction techniques within an ARDL framework, their results suggest that private investment is determined by public investment, inflation, real interest rate, openness, real exchange rate and a regime of constitutional rule. Raza et al. (2013) carried out a study on the relationship and impact of demographic variables on investment decisions in Pakistan. The findings of their study were men and youngsters are risk takers as compared to women and the older generation. Moreover, Kabra et al. (2010) examine the factors that influence investment risk tolerance and decision making process. This study concludes that the investors' age and gender mainly influence the risk taking capacity of the investors. Knight and Ding (2009) found that private investment has been increased due to an increase in rate of return on capital savings, lower inflation rate, interest rate, expansion in education leading to expansion in investment with high effectiveness, and a rapid rise in economic growth results in corresponding growth in investment. Ang (2010) conducted a study on the determinants of private investment in Malaysia in 2010 using OLS analysis and ECM methods found that both foreign direct investment and public investment have a positive effect on private investment. A greater level of aggregate output raises the level of private investment. Gilliam and Grable (2010) analyzed the impact of age and gender in the investment decision. The author observed gender based estimation bias which relates to household decisions that involves financial risk. The author concludes that older investors were more likely to underestimate their financial risk tolerance because of past experience. Wahid et al. (2008) using Panel data of five South Asia countries over the period 1973-2012, found the existence of low positive correlation between savings and investment in three selected Asian countries. Heena (2015) examined the relationship between demographic variables and personality traits on investors' attitude towards risk that may have an impact on the investment growth. The author found that there is a positive relationship between education and investment decisions. Herrmann (2007) using multiple specifications and leveraging multiple risk/return measures, provided the roles of gender in investment preferences. The study concludes the significant effect of gender in investment. Adugna (2013) conducted a study on the determinants of private investment in Ethiopia using the ECM model. His findings revealed that public investment, real GDP per

capita, inflation, international trade, corporate tax, and external debt have a positive relationship while interest rate and exchange rate have negative relationships with private investments. Moreover, Bader and Malawi (2010) study the impact of interest rate on investment using a co-integration analysis method, declare that the real interest rate has a negative impact on investment, while the income level has a positive impact on private investment. Ahangari and Saki (2012) studied the determinants of private investment in Iran. They found that private investment is a function of instability index, government investment, income from oil and gas exports, value added of industry, and banks' credits. Bakare (2011) studied the determinants of private domestic investment in Nigeria. He found that public investment is competitive (not complementary) for private investment. A depreciation of the exchange rate has a negative influence on private investment because it makes imports of capital goods and raw materials more costly for investors. An increase in corruption index and political instability prevent investment to grow. A rise in saving and an improvement in infrastructure, stimulate private investment. Abhijeet and Dinesh (2010) found that investment experience is significantly determining both the investor behavior and investment decision. The study concludes that increase in the experience will be helpful to the investor. Sajid and Sarfraz (2008) investigate the causal relationship between investment and exchange rate on saving and economic growth in Pakistan. The study used co-integration technique and vector error correction model to examine causality between investment and exchange rate. Their result showed that there is long-run as well as a short run equilibrium relationship between them. Jordan et al. (2010) studied the impact of interest rate on investment using a co-integration analysis method, declared that the real interest rate has a negative impact on investment, while the income level has a positive impact on private investment.

Level of education: It is undeniable that education is an important contributing factor to making wise investment decisions as it helps to minimize investment risk. The study by Egesa (2010) indicated that skilled managers increase firm survival. Moreover, a study on private investment determinants at the micro level by Baye et al. (2005) has also shown that the level of education significantly and positively influences the probability of an individual to invest their capital. In this study, the education level considered as level of schooling attended by the investors was recorded and hypothesized to positively influence on investment decision.

Size of the market: The size of the market, usually measured by the GDP of a host country or its population size has been found to be a major determinant of investment. A large market size implies better prospects for an investor since it equates to a greater demand for its goods and services, and offers the investor economies of scale. OECD (2008) found high correlations between the level of concentration of agro-food-related firms and a host country's GDP. In the study, South Africa and Nigeria, the largest countries in the region, had the highest number of large companies. However, the market-seeking hypothesis is true only for investment projects that target the domestic market and where the local people have the purchasing power.

Market related factors such as stock market development, market growth, product price, inflation and raw materials supply have brought major hindrances on the investment activities. Among these factors, inflation and raw materials supply are considered as the main obstacle by majority of private investors in the study area.

Socio-cultural factor: If there is strong competition for remaining land can invoke land conflicts, leading to civil and political instability. Reducing access of farmland and marginalization of small-size farmland owners has negative effects on any development geared towards the needs of the poor. Reduced access to land can lead to displacement of indigenous people or the exclusion of rural communities and increase rural poverty, especially for women. Access to use of common lands can be restricted (collecting fuel wood, wild fruits, medicinal plants, etc. or grazing livestock). As a consequence, socio-cultural cohabitation between different socio-professional groups (e.g. livestock and crop farmers, pastoralists, etc.) can be impeded. Emigration of local farmers can increase social tensions and urban poverty. If former landowners lose their livelihood this may induce a migration flow into cities and increase urban burden or poverty. Plus, a loss of inherent cultural habits may occur. Immigration of foreign employers can invoke social frictions. Income disparities in local communities may arise from the fact that often highly educated management personnel will be recruited from the investor's countries whereas low-level work will probably be done by local personnel. Especially if the imported employers benefit from better working standards or a firm's better healthcare system, social frictions can increase. Cultural and lingual divergences can also worsen social systems Baye et al. (2005).

2.3 Implication of the review

As stated in all above mentioned research the factor affecting private investment were summarized as follow.

❖ Policy related challenges

- ❖ No mechanism in place to ensure investment objectives (e.g. employment, technology, social and environmental issues). In other words, the proclamation is silent about investment benefits of the region (especially employment, revenue, and technology transfer. Etc.)
- ❖ No article that states duty to report and cooperate in the proclamation (as stated in the Federal Law)

❖ Institutional Capacity related Challenges

- Limited institutional capacity of pertinent institutions in providing direct and indirect services for investment activities of the region.
- Lack of guideline and directives on project monitoring and evaluation mechanisms
- Lack of laws that enforce technology transfer.
- Lack of enforcement mechanism to create employment opportunity for the local community affected by the investment.
- Cash compensation for unskilled farmers is not effective.
- Absence of minimum wage.
- Land allocation and handover process delays.
- Good governance problems.
- Controlling mechanism of environmental pollution and workers safety mechanisms.
- Inconsistency of the application of investment guidelines and directives, and the contending elements of the same.
- Uneven distribution of investment projects.
- Weak law enforcement mechanism to take corrective actions when deemed necessary
- Illegal settlement on land allotted for investment purpose

- Limited institutional capacity in terms of skilled manpower, finance and logistic.
- Compensation irregularities (ex, urban land vs rural land, and areas variation)
- Mission and mandates of the commission is to serve the investors not the public at large,
- Weak follow-up mechanism and technical support of investment
- Failure to identify necessary capacity development packages,
- Lack of investment project profile.

❖ Investors related challenges

- Not willing to cooperate with the concerned government bodies.
- Unable to create adequate employment opportunities for the local people, Marginalization of the local communities.
- Violating (or not respecting) the employees' rights –vs-national, regional and international labor laws).
- Unable to identify viable investment projects.
- No mechanism in place to control environmental pollution; OR the investors are unwilling to adopt mechanism that reduce pollution.
- Failure to develop the land as per the agreement, rather exploiting incentives and other privileges.

In addition to the above Challenge of Investors research in different researchers, Investors are late to start operation or construction, change of sector after obtaining of license, financial incapability, they do not use modern technology, lack of experience, they do not hire professionals, wage rate is very low, inefficient utilization of natural resources, and they expand their investment land illegally. The main bottlenecks of the investors that are involved in the agricultural sector; not to create employment opportunity as per their proposed plan are; seasonality of the demand to their production/service, financial problem, lack of foreign currency, and absence of skilled man power.

In other edge service deliverance for investor by Governmental body is not sufficient, for example some of the challenges that the investors faced during land acquisition process are; bureaucratic procedures, provision of land, access to loans, governance issues and availability of trained human resources. Problems in the application of technology are related with electric

power problem, shortage of water, lack of skilled labor to run the technology, and lack of maintenance and accessories.

The main factors for dissatisfaction of the investors that are included in the study with the service provisions of financial institutions are; very weak and time consuming banking service, insufficient credit provision and absence of long term credit, long process during loan provision particularly in the commercial and development banks, shortage of foreign currency, problem on the supply of credit and LC (letter of credit). Most of investors have got various incentives including duty free import, provision of land by initial lease price, tax incentive/holiday, credit provision and facilitation

CHAPTER THREE

RECOMMENDATION AND CONCLUSION

3.1. CONCLUSION

In this study, factors that affect the growth of private investment in agricultural sector were analysed. Different secondary data collected from published and unpublished documents and internet source was used in this study.

There were various factors that hinder growth of private investment at micro-level. Those factors were political instability, administrative and policy related factors like policy distortions and rent seeking, direct government involvement in some investment areas, corruption and dysfunction of the judiciary system, malpractices in granting licenses of investment activities, favoritism in tax revenue collection, arbitrary and inappropriate enforcement of business regulations, bureaucracy and policy implementation delay have brought major hindrances on the investment activities in Ethiopian agricultural sector at micro level. Among these factors, operational inefficiencies of those government institutions are considered as the main obstacle by majority of private investors in the study area. Infrastructure related factors such as electricity energy, water transportation and communication, health facilities, education facilities and unavailability of working age people are investigated-whether they are factors or opportunities of investment. Electricity energy, water, transportation and communication, health facilities, education facilities are considered as obstacle by majority of private investors in the study area, except unavailability of working age people in the investment area which is opportunity of investment in the area.

Macro-economic variables which have a nationwide effect, unavailability of foreign exchange reserves and exchange rate fluctuations are the main problems hamper their investment activities in the study area. Other variables which include access to credit in formal financial institutions, inadequate amount of loan, high interest rates of lending institutions to give loan are all affecting investment practices in Ethiopia. Market related factors such as stock market development, market growth product price, inflation and raw materials supply have brought major hindrances on the investment activities.

3.2. Recommendations

As have been observed in this paper, private investors are engaged in small investments. The ultimate goal of the government of Ethiopia is also gaining benefits from the workings of these private agricultural projects. However, as this study suggests there are many challenges that hindered the government of Ethiopia from driving all the desired benefits from private agro-investment projects.

To create strong private investment in agricultural sector, government should stabilize political system in the country. Reduction of corruption, implementing appropriate policy and creating accountable administration is also what government should do to encourage private investment in agricultural sector. Government should also increase access to credit in formal financial institutions, adequate amount of loan, and balanced interest rates of lending institutions.

Government should enable environment for making investments depends on essential public goods, such as rural infrastructure, including roads and electricity, which the private sector cannot be expected to provide. This requires government action and supportive policies and institutions. Market forces that shape investment decisions, which are largely determined by the private sector, can also be influenced by government policies.

Government and Policy-makers should prioritize the various needs for agriculture-related infrastructure development and Infrastructural related activities such as electricity energy, water transportation and communication, health facilities, education facilities, transportation and communication, health facilities, education facilities. Before deciding on investing in agriculture-related infrastructure, the government should undertake a cost-benefit analysis, factoring in risks and the potential project impact. Investors should have access to clear and efficient communication channels to indicate their infrastructure needs to policy-makers. Co-ordination mechanisms should also be established across the various government agencies responsible for infrastructure and agriculture throughout the policy design and implementation stages.

Agricultural investment also influenced by the level of taxation. Absolute and comparative assessments on competing tax jurisdictions influence location decisions of foreign investors. In

deciding the tax burden, governments should consider the objectives of agricultural investment and overall tax policy, including efficiency and equity, compliance costs and revenue requirements. Most smallholders do not pay income taxes as they fall under the threshold for raising such tax. Thus, a relatively high income tax rate may incentivize them to remain small to avoid paying such tax, thereby discouraging investment and growth.

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