EFFECTIVNESS OF TAX INCENTIVE IN PROMOTING INVESTMENT

IN ETHIOPIA

BY

MISTIRIE DAMTEW

A THESIS SUBMITTED TO ST.MARY'S UNIVERSITY COLLEGE, SCHOOL OF GRADUATE STUDIES IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION

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APPROVED BY BOARD OF EXAMINERS

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List of Acronyms

EIA	Ethiopian investment Agency
ERCA	Ethiopian Revenues & Customs Authority
FDI	Foreign Direct Investment
FTZ	Free Trade Zone
GDP	Gross Domestic product
GTP	Growth & transformation plan
HQ	Head Quarter
IMF	International Monterey Fund
MoFA	Ministry of Foreign Affairs
MNC	Multi National cooperation's
NBE	National Bank of Ethiopia.

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Abstract

Investment plays a significant role in the development process of developing countries. Given this many developing countries particularly, Ethiopia is striving to become middle income level country. In order to realize this goal promoting investment activity has a major significance. Fiscal incentive was one among the attempts made to create investment friendly environment. This paper objective was to see the relation between fiscal incentives and investment and analyzes the effectiveness of tax incentive in promoting investment to Ethiopia. The study gathers the information from Ethiopian revenues & customs authority and Ethiopian investment agency officers through questionnaire. The study concludes that the tax system and fiscal incentive administration in the country is not in satisfactory level due to lack of clear regulation that can serve all scenarios. Regarding the investment volume, it's increasing from time to time and non tax factors are considered as influential in the investment decisions. In addition cheap labor cost and market opportunities have their own contribution in the investment growth. Infrastructural facilities were considered as an obstacle in the investment promotion activity.

CHAPTER ONE

INTRODUCTION

1.1.Background of the Study

Instrument of investment incentives have been around for over 100 years. In the 19th century they were used in the United States of America, in the 20th century governments around the world began to offer direct grants, tax breaks, training funds, free infrastructure and other inducements to attract investments (James, 2009). Moreover the well-known multinational companies make use of them. Investment incentives represent very large sums of government spending and foregone revenue.

The United Nations Conference on Trade and Development (UNCTAD, 1996, p. 11) define investment incentives in general as “measurable advantages provided by government to particular companies or group of companies with a goal to force them to behave some way”. Thomas (2007, p. 11) describes investment incentives as “a subsidy given to affect the location of investment. From the above definition it’s clear that incentives are a way to influence the investment decisions of investors in favor of the government and also should be measurable.

“Tax incentives improve economic performance only if government officials are better able to decide the best types and means of production than are private investors.” (Bird, 2008)

When Incentives are provided it is essential that:

• They be based on rules and not be open-ended (with strict time limits).

• Benefiting investors file tax returns and face audits.

• Governments produce tax expenditure statements so that the cost of incentives is transparent.

• Incentives be reviewed occasionally for their efficacy

Investment incentives have a mixed record. They have been associated with growth in some countries but limited impact in other.

Hassett and Hubbard (2002) find that tax policy affects investment, with a 1.0 percent increase in the user cost of capital lowering investment by 0.5–1.0 percent (for an elasticity of –0.5 to –1.0). This analysis is based on microeconomic data from firms. Macroeconomic data, by contrast, provide little evidence that tax policy affects investment. But this conclusion is likely due to measurement errors in macroeconomic data, inter-asset reallocation of capital, and simultaneity, which make it difficult to draw causal links or make correct attributions using macroeconomic data.

Taxes increase the user cost of capital, so any uniform reduction in that cost should encourage capital investment. But targeted incentives are unlikely to broadly reduce the cost of capital. Low inflation which is the result of factors other than a policy decision to award incentives serves as a good investment subsidy.

Economic growth is higher in countries that invest more in equipment, mainly because workers learn better skills by operating different kinds of equipment. Thus equipment subsidies are good for growth because they generate positive externalities. Investment incentives do not work for many firms that face finance constraints and cannot grow to take advantage of tax incentives (FIAS, 1999).

Almost every argument used to support or criticize the implementation of tax incentives, in developing countries is debatable and hard to measure. Because there is no model, developing countries do not have the guidance to implement an established system to achieve the economic goals these kinds of policies are intended to achieve, so usually the tax policies implemented in developing countries are based on trial and error.

The Government of Ethiopia is seeking to transform the economy based on major investments in economic infrastructure, economic management reforms, and strategic public sector engagement in the economy. The government tries to encourage investment and promote the inflow of foreign capital and technology into Ethiopia. One of the steps taken by the government to enhance Investment in Ethiopia is the provision of investment incentives the following incentives are granted to investors engaged in areas eligible for investment incentives:

- Customs Import Duty.
- Income Tax Holiday.
- Duty Draw-Back Scheme.
- Voucher Scheme.

• Bonded Manufacturing Warehouse Scheme. (MFA, 2011)

In this study the focus will be on how the investment & investment incentives are executed. In the study the theoretical assumption & principles of incentives were analyzed in relation to Ethiopia's current situation.

1.2. Statement of the Problem

Incentives are intended to influence investment decisions that can benefit the economy as a whole. To determine this it is necessary to analyze the nature of the problem the incentive is intended to tackle, the likely effects of any incentive, and to analyze whether it's the appropriate technique or not.

Many governments offer tax incentives to attract investment, yet policies often fail to fully assess their likely costs and potential benefits. Incentive policy should balance the higher revenues and social benefits jobs, positive externalities, signaling effects from possibly increased investment with the indirect costs of incentives such as administrative cost and the revenue losses from incentives given to investments that would have been made even without them. sabastian (2010)

According to Bird (2008) "If one cannot simply eliminate tax incentives, I have elsewhere suggested three simple rules to reduce the damage that may be caused by poorly-designed and implemented incentives: keep them simple, keep records, and evaluate the result."

- Governments should assess in advance tax incentives targeted to boost investment;
- if introduced, the tax incentives should be evaluated (using cost-benefit tests) on a periodic base to gauge whether their effectiveness; to enable proper evaluation and assessment, the specific goals of a given tax incentive need to be explicit at the outset;(clark, cebriero & Bohmer, 2007)

Any incentive policy requires constant monitoring to prevent leakage, imposing an additional burden on tax authorities. Excessive use of tax incentives complicates administration, facilitates evasion, and encourages corruption. Khan (2006)

The investment climate is especially crucial for determining the effectiveness of incentives in attracting investment. Every steps that the investor take to start his/her business helps to asses the investment climate. The time taken in getting licenses and legal documents, the access to land, corruption, social and political stabilities of the country allow to understand its investment climate. These important factors affect the choice of investor to invest in particular region or sector.

The investment climate influences the effectiveness of fiscal incentives in attracting investment through the role that public goods play in improving investment returns. Here the public goods are the components of the investment climate, such as infrastructure, rule of law, enforcement of contracts, and so on. The public goods are funded through a tax on capital, which in turn reduces the return on capital. But if the public goods make capital more productive, then an increase in taxation spent on them would have the opposite effect. On balance, the effect is ambiguous. However, when public goods and investment are highly complementary—as with the investment climate—then in countries with large endowments of such goods, a drop in taxes is much more effective at encouraging investment than in countries with smaller endowments. (Sebastian and Parys, 2009)

The most important question is whether the investment will generate the promised positive externalities. Around the world, several large investments have had limited direct impacts on local economies.

The problem concerns the effectiveness of incentives is the benefits that a government assumes is not necessarily comparable with the cost that is possible to take place. So considering Ethiopians level of growth to provide effective incentive on investment seems debatable because of the amount of efficient man power & clear procedures needed. So the aim of this study is to analyze tax incentive and the general investment environment so that it can be used as a literature in addition to the existing ones.

1.3.Research Questions

The central question of the study is; did the tax incentives benefit exceed the cost of having them.

To understand the above points the study seeks to answer the following Sub question;

- What kind of the tax incentives implemented in Ethiopia?
- What are the trends of investment activities in Ethiopia?
- Do the investment incentives have direct impact on investment?

1.4.Objectives of the Study

1.4.1. General Objective

The main objective of the study is to get insights on tax incentives and their effect in supporting investment activities in Ethiopia.

1.4.2. Specific objectives

- To asses tax incentives implemented in Ethiopia.
- To explore investment environment & progress in Ethiopia.
- To examine tax incentives and their relation with investment.

1.5.Significance of the Study

At the end of the study, it intends to provide valuable information to the government bodies' i.e. customs authority & investment agency & the society regarding their employee's perception about the tax system, tax incentive and its administration. Also From the forwarded recommendation they will take the constructive comments to improve the system.

It will also serve as a stepping stone for other researches which will be conducted in similar topic area in the future. & finally it has increased the knowledge & ability of the researcher in conducting in similar studies.

1.6.Delimitation/Scope of the Study

This study investigated the effect of tax incentives in promoting investment in Ethiopia Thus, the study is expected to show the tax incentives effects and also to asses its effectiveness in promoting investment.

The scope of the study is bound to tax incentives packages & their effectiveness in promoting investment. This study will try to asses & identifies vital points related to incentives &it's implication to the society and the economy as a whole. The study intended to address selected writings (publications) also individuals, officials to gain the general picture of tax incentive practice & the policy in the city administration with in 6month time period. The researcher faces difficulties in collecting data because of shortage of time to collect and analyze the data; unwilling individuals to provide necessary information, Lack of experience in doing research also hinder the researcher in preparing the study.

1.7. Organization of the paper

This study is organized in to five chapters. The first chapter provides an introduction to the study. It contains background of the study, statement of problem, objectives, research questions, significance and limitation of the study.

The second chapter is the literature review of the study. In this part literatures related to the topic will be reviewed. It includes review of different books for identifying the main theoretical perspectives. In addition prior studies will be reviewed.

The third chapter explains methods of the study. In this chapter the type and design of the study, the subjects and sampling of the study, sources and tools of data collection, procedures of data collection and the data analysis techniques will be discussed.

The fourth chapter is about the results and discussion of the results of the study. In this part of the study the analyses of the collected data are summarized, and then findings are discussed and interpreted. The fifth chapter includes the summary, conclusions and recommendations of the study based on the findings,

CHAPTER TWO

2. LITERATURE REVIEW

2.1.Introduction

This literature review is aimed at providing more inclusive theoretical concepts on investment incentives & investment growth. The literature review consists of three subsections. The first sub section discusses about investment incentives special about tax incentive concepts generally and also in Ethiopia case. The second subsection deals with Investment and the last subsection deals with the theoretical frame work between tax incentives & investment.

2.2. Definition of Investment Incentives

Investment incentives has many definition depending on given scenario but in its broad concept, it's Government schemes aimed at stimulating private sector interest in specified types of capital expenditure, or investment in areas of high unemployment or backwardness. These incentives may take the form of direct subsidies (investment grants) or tax incentives that compensates the investors for their capital costs.

According to (smelt, 1998) ,selective interventions that are deliberately and selectively targeted at investment or production decisions in specific industries, localities or activities. So it can be seen a government tool in promoting economical development focusing on areas that need due attention or encouragement.

Most Governments have been actively promoting their countries as investment locations to attract scarce private capital and associated technology and managerial skills in order to help achieve their development goals. They have increasingly adopted measures to facilitate the entry of foreign direct investment (FDI).Countries offer a number of benefits, including tax and non-tax incentives for establishing new investment undertaking. Incentives may be provided directly by the government through some form of fiscal incentive, involving lower effective tax rates (either by reducing tax rates or by narrowing the tax base, perhaps by offering investment tax credits or immediate expensing) or direct grants; or may instead comprise indirect subsidies.

It’s obvious that every plan or police to be effective it has to go under many steps to prove & ensure its intended benefits/output. Also for incentives there are four broad steps involved in incentives policies they are:-designing incentives; granting incentives; implementation; and follow-up of compliance by firms that have benefited from the incentive measures. In this respect, incentives imply financial as well as administrative costs.

A. Incentive design

The very first step required in designing incentives are we should have to clearly list and analyze the market imperfections and the extent of the imperfections that the incentives are designed to reduce or eliminate. The costs of granting incentives can then be compared to the benefits of removing or reducing the imperfections. Otherwise the cost of administering the incentives can be hard to manage (James , 2010).

B. . **Incentives should be granted automatically**

Eligibility for incentives provided by law should be based on clear criteria, not granted through special permission or certification by investment promotion agencies, ministries of trade, or other government agencies. This approach ensures prompt decision making and quick turnaround times for investors essential to attracting and retaining investment. This step also can slightly show the investment environment i.e. the corruption level or office bureaucracy.

C. **Implementation**

The tax administration should ensure that investors receiving tax incentives satisfy the requirements for them. To enable them to do so, it should be compulsory for tax returns, declarations, and relevant forms to be filed regularly for investors to receive tax benefits. Tax incentives should not be used as an excuse to avoid tax administration, information, audits, and any other compliance requirements.

D. **Follow up**

Periodic review of the incentives by Governments offers a potential double benefit. On the one hand, it can help Governments prevent revenue leakage by eliminating excessive incentives or unnecessary tax breaks to investors. On the other hand, it can help them update incentives packages to provide real value to investors that will attract more investment.

2.2.1. Objectives of Investment incentives

In generally speaking the objective of incentive can be to enhance one's country revenue by making favorable investment condition. But According to UNCTAD study it's classified by four major categories;

Regional Investment

Countries often employ a mix of incentives to channel investment for development of a particular area or region. Regional development objectives include support for rural development, building industrial zone away from major cities and reducing environmental hazards, over-urbanization and concentration of population. In this case the government focus is only to specific region that needed attention/affirmative action.

Sectoral Investment

Countries employ tax incentives in order to promote sectors of industry or activities considered crucial for development.

The majority of tax incentives granted by developing countries relate to investment in manufacture, exploration and extraction of mineral reserves, promotion of export and, increasingly, the tourism and leisure sectors. The above mentioned sectors are selected because of their behavior like great start up capital need of educated human force and the like.

Performance enhancement

Incentives can be targeted at many types of activities, such as export promotion, employment/skills training etc. Free trade zones (FTZs) typically cover incentives for export-oriented manufacturing. To be competitive in the world market it's a must to be able to provide quality goods & services so the need to improve the way of production is essential. In the mean time it will force to improve performance.

Transfer of technology

An important objective of using incentives to attract investment to developing countries is the transfer of technology. Due to Foreign Direct investment new technologies will enter in the country. The skills of the host country employees will be improved and new technology will be familiar in the country.

2.2.2. Classification of investment incentives

2.2.2.1. Non Fiscal Incentive

Nontax incentives can be defined as all nontax aspects that encouraging investment, such as effective regulation, good access to land, and a healthy business environment. In general the processes that are encouraging investors to invest can also include in this categories.

2.2.2.2. Fiscal incentives

A good tax system ensures predictable revenue for government, presents a reasonable tax burden to investors, is stable, and minimizes distortions in investment decisions. In the past tax issues were not determining factors for businesses to decide whether to invest in one country over another. Some studies showed that ‘‘the statistical determinants of the location of investment are market size, labor cost, infrastructure quality, growth of industrialization, level of foreign investment, growing domestic markets, and stable international relations(). However, according to more recent studies, tax issues are becoming a more important factor in the decision-making process; ‘‘globalization has dramatically reduced the importance of these factors, and elevated the role of tax incentives’’ (Margalioth, 2003).

Tax incentives can be defined as any incentives that reduce the tax burden of enterprises in order to induce them to invest in particular projects or sectors. They are exceptions to the general tax regime. According to (clark, cebriero & Bohmer, 2007) tax incentives are chosen by governments to attract investment in developing countries are mainly because they are

- Much easier to provide than to correct deficiencies in, for example, infrastructure or skilled labor, implementing economic reforms.

- do not require an actual expenditure of funds or cash subsidies to investors; and,
- Politically easier to provide than funds.

2.2.2.3. Costs of Managing and Administering Incentives

Governments may see incentives as a necessary measure to compete with other countries, and to signal government commitment to an open investment environment (Moran, 1998). Support for incentives could also arise from agency problems and the comparative ease with which incentives can be enacted (Aliber, 2001; Wells & Allen, 2001). In most instances however, the efficacy of these measures are overestimated while the costs remain hidden.

The legal instruments granting tax incentives has to be drafted carefully so that they achieve policy objectives with a minimum leakage of tax revenue. They are expressed as precisely as possible so as to avoid the need for frequent corrections or changes. It is believed that frequent changes could contribute to the perception that the tax system is complex and difficult to comply with. Apart from the tax incentives regime, stability and predictability of the tax system are major factors influencing firms when they commit to long term investment.

According to (Klemm, 2009**)**"The cost of tax incentives are wide ranging and go beyond any immediate revenue loss". Apart from revenue losses, they include distortions to the economy as a result of preferential treatment of investment qualifying for incentives, administrative costs from running and preventing fraudulent use of incentives schemes, and social costs of rent-seeking behavior, including possibly an increase in corruption.
Excessive use of tax incentives complicates administration, facilitates evasion, and encourages corruption. It also costs businesses time and money to comply with audit requirements

Effective incentive policy requires reducing the nonrevenue costs of incentives. Ways to do so include reducing misuse of incentives, administering incentives effectively, and easing the compliance burden on investors who want to take advantage of incentives. Among other things, nonrevenue costs can involve:
• Distortions created by encouraging new investments that are detrimental to existing ones.

• Time and money spent by businesses lobbying the government for tax incentives.

• Time and money spent by businesses qualifying for and obtaining tax incentives.

• Revenue lost to illegal activity, such as from businesses that do not qualify for tax exemptions but falsify information to do so, or indirect revenue lost to businesses that do not qualify for tax incentives but illegally use tax-exempt entities to source goods.

• Additional costs for authorities responsible for administering tax incentives. (James, 2009)

Providing incentives can create risks that might have implications for the investment Climate and overall fiscal compliance. It also encourages lobbying and rent seeking.

Increasing transparency on the costs and benefits of tax incentives would, in the long run, help frame future policy. Providing a level playing field to all businesses through a broadly based, low, uniform tax rate has been the best investment incentive in many countries.

When Incentives are provided it is essential that:

• They be based on rules and not be open-ended (with strict time limits).

• Benefiting investors file tax returns and face audits.

• Governments produce tax expenditure statements so that the cost of incentives is transparent.

• Incentives should be reviewed occasionally for their efficacy.

A related issue involved in the design and administration of an incentives system is the discretionary power of officials granting the incentives. Administrative discretion can be reduced if the enabling legislation clearly defines the incentives package and the criteria under which incentives may be granted.

Assessing the relative advantages and disadvantages of tax incentives is a complicated and controversial issue. The main difficulty in assessing their benefits is in determining if incremental

Investment is indeed the result of incentives. Because it's recognized that incentives are not the prime determinant of investment decisions.

A popular metric for measuring the cost-effectiveness of investment incentive policies is to calculate the dollar cost of the jobs they create, based on total tax spending/tax expenditure. Though this approach is not very precise, it provides a ballpark figure that helps policymakers decide if the incentive was worthwhile. (James, 2009)

Here in the figure below are the advantage & disadvantage of common tax incentive packages are discussed.

Incentive	**description**	**Advantage**	**Dis advantage**
Reduced corporate tax rate	lower corporate tax rates	▪ Distortions minimized ▪ longer benefit period ▪ flat tax rates reduce confusion	▪ has to be below 35% to be effective ▪ rewards old capital
Sectoral incentives	Reduced corporate tax rates for certain sectors/ activities.	▪ signaling effect of government commitment ▪ easier to implement	▪ may distort market
Tax holidays	Period of tax exemption/ reduced tax.	▪ flexible, can be used to targets certain industries ▪ immediate benefit To income-earning firms.	discretionary approach → distortions, potential for mismanagement □ favors existing firms over start-ups ▪ can lead to tax leakage and avoidance through transfer pricing ▪ rewards short term investment in 'footloose' industries
Investment tax	Allowances/credits tax credit/ allowance for Investment expenditure.	▪ Supports expansion in existing firms. ▪ Encourages long term investment. ▪ less revenue leakage	
Accelerated depreciation	Deductions are calculated over a shorter time period	▪ Supports expansion in existing firms ▪ encourages long term investment ▪ Less revenue leakage.	▪ Eroded by high inflation.
Input sales tax credit tax	credit against input sales tax, especially on capital Goods.		
Loss carry forward	Write-off of losses against gross profits of following years.		
Export/ import Incentives	Exemption on customs duties, zero-VAT rating on exports, export marketing assistance.	▪ Can be used to target sectors.	▪ restricted by trade treaties ▪ dependent on capacity of customs administration
Subsidies/ grants	outright grants, upfront subsidies and subsidized Loans.	▪ Flexible, can be used to target sectors.	▪ high upfront costs ▪ dependent on capacity of tax administration

			▪ open to abuse
Regional incentives	grants/ tax allowances/ subsidized loans/ infrastructure provision when investing in certain Regions.	▪ flexible, can be used to target regions	▪ dependent on capacity of regional administration ▪ open to abuse

(Sources: UNCTAD Policy Review Series; Biggs, 2007; Morisset and Pirnia, 2000

2.3. Investment

According Business dictionary () to Investment is the amount of money, knowledge or resource you put into business in order to make profit. The driving force behind private investment can be conceptualized in terms of risk and return. High return is expected for risky investments and the reverse is also true. Investment projects are viable when the expected rate of return on capital exceeds the entry cost rate.

In discussing investment the key area to focus is its operating environment.In countries with weak investment climates with extensive bureaucracy on accessing land, starting a business, or exporting and importing lowering the effective tax rate has limited impact on foreign direct investment (FDI). The average response is far more pronounced in countries with good investment climates. For example, “lowering the effective tax rate from 40 percent to 20 percent raises average FDI by 1 percent of GDP for countries ranked in the bottom half in terms of investment climate—while the same change raises FDI by 8 percent of GDP for countries in the top half”(james,2010).

2.4. Investment in Ethiopia

Overview of Ethiopian economy

Ethiopia is in the midst of a sustained growth trend that is becoming increasingly broad-based, building on major improvements in educational attainment, improved health outcomes, and infrastructure capacity in terms of access to power, transportation and telecommunications. The Government’s Growth and Transformation Plan sets ambitious targets for further improvements in these areas, together with significant reforms aiming to meet the socioeconomic Millennium Development Goals by 2015, and to achieve middle-income status for Ethiopia by 2020−23.

Ethiopia's economy is based on agriculture, which accounts, in 2009/10, for about 42 percent of the gross domestic product (GDP), 90 percent of foreign currency earnings, and 85% of employment. Generally, the overall economic growth of the country has been highly associated with the performance of the agriculture sector.

Ethiopia investment environment

From the bureau of economic development affairs report in 2013 Ethiopia has undergone major socio-economic and political transformations ranging from a feudal system to socialist and more recently an open market-based economy. The economy is still young with a vast resources and a range of investment opportunities. The country has comparative advantages in textile and garments, agriculture, agro-processing, and leather and leather products.

Ethiopia has made a considerable progress in economic and social development since 1992 as a result of the implementation of favorable policies and strategies that are instrumental in improving the national economy. The Rural Development Policy and Strategy, the Industrial Development Strategy, and other sectoral policies and strategies have initiated a new push towards creating frameworks conducive to economic and social development.

The Government of Ethiopia in recognition of the role of the private sector in the economy has revised over three times the Investment Code over the last eighteen years to make it more transparent, attractive and competitive. Major positive changes regarding foreign investments have been introduced through Investment Proclamation no 280/2002 and regulation no 84/2003.
Ethiopia is mounting a highly ambitious economic infrastructure development program, which has already resulted in significant expansion of installed electricity capacity and distribution, road length, water and sanitation supply, and telecommunication services throughout the country. Ethiopia is starting to develop its infrastructure connections to neighboring countries, including transportation and power links.

The World Bank's Doing Business report for 2013 ranked Ethiopia at 127 out of 185 countries, losing ground from the 2012 ranking of 125. Contributing to the drop were declines in scores for investor protections, tax payments, contract enforcement, and resolution of insolvency.

Ethiopia’s macro Economic Scan

In the bureau of economic & business affair 2013 investment climate report Ethiopia economic situation ha discussed as follows. The economy of Ethiopia has experienced strong and broad based growth over the past decade, averaging 10.6% per year in 2004/05 - 2011/12 compared to the regional average of 5.4%. Expansion of the services and agricultural sectors account for most of this growth, while manufacturing sector performance was relatively modest. Private consumption and public investment explain demand side growth with the latter assuming an increasingly important role in recent years.

Economic growth brought with it positive trends in reducing poverty, in both urban and rural areas. While 38.7% of Ethiopians lived in extreme poverty in 2004-2005, five years later this was 29.6%, which is a decrease of 9.1 percentage points as measured by the national poverty line, of less than $0.6 per day. Using the Growth and Transformation Plan (GTP), the target is to reduce this further to 22.2% by 2014-2015.

GDP

Real GDP grew by an average of 10.4 percent in year 2009/10, which places Ethiopia among the top performing economies in Sub-Saharan Africa despite world economic meltdown and global financial crisis. All sectors contributed to this relatively high economic growth. Accordingly, agriculture, industry and services grew by an annual average of 7.6, 10.6 and 13 percents, respectively, during the indicated period.

Inflation

Inflation has surged to worrisome levels. Some of the contributing factors have been external to Ethiopia, including volatility in international food prices. Domestic drought conditions have also contributed to the volatility. However, non-food price inflation has been relatively high and on an upward trend, which suggests an excessively accommodating monetary policy. The latter conclusion is strongly corroborated by cautionary advice from the IMF (2012a, p. 4) concerning the need to restore interest rates to positive levels in real terms. Inflation has decelerated sharply into single digit levels in the first months of 2013; 14 however, African Development Bank economists conclude that Ethiopia lacks a credible monetary policy anchor (Durevall and Sjö, 2012). Monetary policy continued to focus on containing inflationary pressure and building international reserves of the country. Efforts were made to make the growth of broad money supply in line with nominal GDP growth (2010/11 annual report page97)

Real Exchange rate

Ethiopia's real exchange rate temporarily returned to more competitive levels in 2009 and 2010, but this trend reversed over the period 2011-2012, with a renewed rise, driven in large measure by high domestic rates of inflation; renewed policy attention seems required.

Trade Balance

Ethiopia's international trade has grown rapidly over the past decade. Until 2008, import growth was especially strong, reflecting both Ethiopia's rapid industrialization and the real exchange rate appreciation. Export growth picked up strongly in 2010 and 2011 following the real exchange rate adjustment.

Important macro challenges do remain, notably inflation volatility, renewed upward pressure on the real exchange rate, and negative real interest rates. This situation generates a broad range of macroeconomic management challenges and constrains the growth of the savings needed to fuel Ethiopia's investment requirements, as well as putting pressure on Ethiopia's external balance.

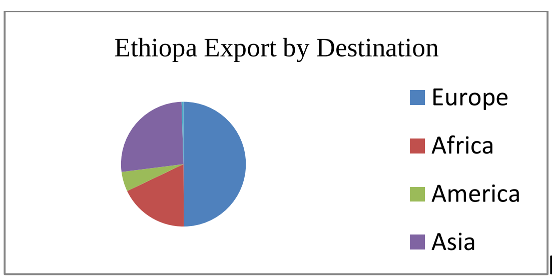

FIG.1 Source NBE

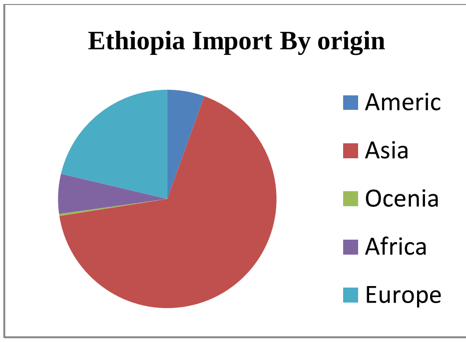

Fig.2 Source NBE

2.5.The effect of effective incentives on investment

Governments make extensive use of investment incentives in an effort to attract investments. Their effectiveness has been the subject of intense debate, and little consensus has emerged. Some experts have argued that there is little evidence such incentives are effective a view that has guided considerable technical assistance recommending that governments reduce their use. Others have argued that investment Incentives have contributed to the rapid economic growth of countries.

Investment incentives can have positive & negative effects. According to Black and Hoyt (1989)" competing for investment can be effective when it moves governments to provide public services at marginal cost, rather than average cost". Incentives are invested where the social benefit of the investment exceeds the private benefit of the investment. Also incentives by providing many investment opportunities unemployment rates can also be reduced, Bartik (1991) considered that in the market for investment, the jurisdictions with the greatest need as high unemployment will offer the largest location subsidies. Also they have effect on attracting foreign direct investment (FDI) that can be a potential to transfer knowledge and technology, create jobs, boost overall productivity, enhance competitiveness and entrepreneurship, and ultimately eradicate poverty through economic growth and development.

Different publications suggests on three points as pre requisite for effectiveness of tax incentive. These are:

- Investment is highly dependent on tax rates, with lower taxes resulting in significant additional investment.
- Investment generates many social benefits.
- The incentive policy has low indirect costs.

Kokko and Zejan (2000) are against incentives for three reasons; firstly because without investment incentives multinational corporations might not enter the host economy; secondly, it is very difficult to make calculations about expected future benefits; and thirdly, foreign investors do not differ from the local investors. The other point considered as negative aspect is Harmful tax competition may be caused by the implementation of tax policies by developing countries to offer tax incentives and other tax benefits for foreign investors.

The most acute disadvantage of discretionary tax incentives, especially in developing countries, is that they are susceptible to corruption. In many countries, discretionary application of tax incentives is one of the most important contributors to corruption. (Avi-Yonah and Margalioth 2007).

Tax incentives are far less effective in weaker investment climates than in stronger ones. Moreover, tax incentives should not be used in an effort to compensate for a weak investment climate.

2.6. Conceptual frame work

This study investigates the effectiveness of incentives in promoting investment. In the study the dependent variable of the study is investment .The independent variables of the study are the availability (prevalence) tax (fiscal) incentive. The availability of fiscal incentives include two variables i.e. investment climate & political consideration. According to (James, 2009) tax incentive can be considered as beneficial when they satisfy the conditions mentioned below:

Investment responds strongly to incentives and revenue rises as a result	+	Social benefit from increased investment	>	Lost revenue from investments that would have been made any way	+	Indirect cost of incentive

Figure2.3**:Conceptual frame work**

CHAPTER THREE

3. RESEARCH DESIGN AND METHODOLOGY

3.1. Introduction

This chapter deals with the research design and the methodology that was used in gathering data for the study. It contains the research design, the sampling method and the sample size, source of data, variables of the study, data collection procedure and data analysis techniques and finally reliability, and validity section.

3.2. Research Design

Based on its purpose the study is explanatory type. It emphasis on studying a situation or a problem in order to explain the relationships between variables in this study it is used to explain the relation between effectiveness of tax incentives in promoting investment . According to Saunders et al (2009) "explanatory studies establish causal relationships between variables ".

The data collected by employing a survey strategy can be used to suggest possible reasons for particular relationships between variables and to produce models of these relationships. In addition survey strategy as it use samples it will enable to generate a representative finding of the whole population at a lower cost (Saunders et al, 2009).

3.3. Population and sampling Technique

3.3.1. Sampling techniques

For this study the source populations were the current government officials/employees in investment promotion department & duty free scheme department of Ethiopian Investment agency and Employees of Ethiopian revenues & Customs Authority incentive administration & investment promotion support team. Due to the difficulty in addressing all concerned government bodies throughout the country the researcher uses a convenience/deliberate sampling technique. It's a non probability sampling technique that involves purposive or deliberate selection of particular units of the universe for constituting a sample which represent the universe.

The preliminary survey undertaken by the researcher before questionnaire distribution indicated that there are two government offices & two departments that is considered to be most relevant for the study. The sample population of this study comprises employees from two different government bureaus. I.e. from Ethiopian investment agency the investment promotion & duty free scheme department and from Ethiopian revenues & customs Authority HQ support team for tax incentive & from kality Branch incentive administration department. A total number taken as a sample is 44out of that 36 found in ERCA head office investment support team and Kality incentive administration and the rest are taken from Ethiopia investment agency.

3.4. Data collection Instruments

There are different techniques on how to collect data. The chosen alternative depends on which method best answers the question of the investigation/study.

This study used both primary and secondary sources of data. The primary data was collected through questionnaire. The questionnaire questions are direct, simple and grant the respondents the opportunity to reflect on them and answer at their own time but within the time period.

The questionnaire had four sections. The first section was on the background of the respondents, which request information on the age, sex, work experience, educational qualification. The second section is about the availability of tax incentive. The third section is about investment specially FDI trend. The fourth section is focused on the linkage/relationship linking investment & investment incentives.

Secondary data are already available they refer the data which have already been collected and analyzed by someone. The secondary data was collected from different publication, documents in EIA & ERCA also proclamations were used.

3.5. Procedures of Data collection

The construction of a research instrument or tool for data collection is the most important aspect of a research project because anything you say by way of findings or conclusions is based upon the type of information you collect, and the data you collect is entirely dependent upon the questions that you ask of your respondents.

The form of questionnaire used in the study is a combination of close ended & open ended. The questionnaire has been distributed for promotion & investment incentive administrative officials who have been selected through convenience sampling. In the closed form of questionnaire the respondents choose one of the alternatives as possible answers. The questionnaires were directly given to the respondents. Thus, the respondents answered the questions and the filled questionnaires were collected from each respondent according to the time line provided for data collection.

3.6. Methods of data Analysis

Analysis of data means studying the tabulated material in order to determine inherent facts or meanings. It involves breaking down existing complex factors into simpler parts and putting the parts together in new arrangements for the purpose of interpretation.

The collected data was analyzed by using both descriptive and inferential statistics. Descriptive statistical analysis is concerned with numerical description of a particular group observed. From descriptive statistics percent, frequencies are used to analyze the variables of the study.

3.6.1. Objectivity

Objectivity is the absence of the researchers influence on the results of the study, It is about limiting the influence of the researchers own value, interest and intention. The researcher has tried to keep a high level of objectivity in all works of the study by trying to search for information from varies sources and triangulating the findings in the analysis. And since this study is not written at the request of any company or organization there is no pressure on the researcher to reach at a specific conclusion, which has made keeping an objective perspective easier.

CHAPTER FOUR

4. DATA PRESENTATION AND ANALYSIS OF FINDINGS

4.1. Introduction

This chapter presents a discussion of the results and the process through which the results were obtained. First the background information of respondents is presented and discussed. The chapter also deals with the presentation and an analysis of data collected and discusses it in relation to tax incentive & investment promotion. The statistical methods used for analyzing the data collected include frequency results, descriptive statistics analysis, a correlation analysis, and simple linear regression analysis by using SPSS version 20.

4.2. Data Analysis

4.2.1. Background information of Respondents

A total of 42 questionnaires were sent among concerned government organization. In Kality ERCA 27 questionnaires were sent and 19 questionnaires were returned which is 70.37% response rate. For ERCA HQ a total of 9 questionnaires were sent and 7were returned which is 77.8% response rate. In the case of EIA 6 questionnaires were sent of which 5 were returned which is 83.3% response rate. From total questionnaires which were distributed in the three offices, 31 questionnaires were returned which is total of73.81% response rate.

4.1 Respondents profile

From the 31 respondents 21 are male and the remaining 10 are female. The age composition of the respondent's shows that 77.42% of the respondents are between the age 20 and 30, 77.42% of the 22.58 of respondents are between the age 31 and 40. The majority of the respondents are found between the age 20 and 30.

Work experience and education qualification of the respondents show all has received higher level education but they are less experienced in the area.

4.2 Investment trend

The Ethiopian Investment Agency and Regional Investment Offices licensed 62,068 investment projects with an aggregate capital of Birr 1.2 trillion in the period between 1992/93 – 2011/12. Of these projects, 52,462 (84.5 percent) were domestic, 9,498 (15.3 percent) foreign and 108 (0.percent) public.

TABLE4.2 DETERMENAT OF INVESTMENT IN ETHIOPIA

	Frequency	Percent
TAX FACTOR	6	22.6
NON TAX FACTOR	24	77.4
Total	31	100.0

The responses gathered regarding determinate factor of investment in Ethiopia, 77.4% of the respondents has chosen non tax factor over tax factor. In developing countries the non tax factors that attract investors mostly are underdeveloped markets, low product competition, cheap labor, and currency exchange. It indicates that the above listed factors are also more powerful in influencing investors in Ethiopia.

TABLE4.3 MAJOR OBSTACLE FOR INVESTMENT

	Frequency	Percent
INVESTMENT CLIMATE	10	32.3
TAX FACTOR/ISSUE	5	16.1
INFRASTRUCTURE	16	51.6
Total	31	100.0

According to 51.6 % of the respondents the reason that hinder investment is infrastructure, next to it investment climate also regarded as an obstacle. According to the NBE 2010/2011 report the infrastructure development in the country is showing progress. By the five year growth and transformation plan in 2014/2015 the government intended to increase the water supply to 98.5%,increasing the number of fixed line subscribers from 1 million in 2010/11 to 3.05 million by the end of 2014/15. The number of mobile-telephone subscribers and Internet users is also expected to pick up to a respective 40million and 3.69 million by the end of the plan period from 6.52 million and187, 000 in 2010/11.for power supply, electricity generating capacity is expected to reach 8000 MW by the end of fiscal year 2014/15 from the current level of 2000 MW. And also the city light train and other intensive road projects has been undertaken. In 2008/09, the total road network, excluding community roads, had reached 29,257 miles, out of which 46 percent are track roads and the remaining 54 percent are rural roads with annual growth rate of 5 percent. Based on the classification of the road network, more than 12,694 miles are in the Federal network, out of which asphalt road constituted 30 percent and gravel road 70 percent. All-weather rural road, constituting 15,613 miles of the total road net work in 2008/09 grew by an average of 7% per annum in the last several years.

TABLE4.4 INVESTMENT DRIVING CONDITION WITHOUT INCENTIVES

	Frequency	Percent
MARKET SIZE	5	16.1
COST OF LABOUR	13	45.1
MARKET GROWTH	7	22.6
COMPETITION	5	16.1
Total	31	100.0

Investment can be boosted in one country through different favorable condition. In this study market size, cost of labor, market growth and competition are the alternatives given. From the alternatives presented most of the respondent's i.e.45.1% has chosen cost of labor as the major force that attracts investment in Ethiopia. 22% select market growths and 16.1&19.4% accounted for competition & market size respectively. In the UNCTAD report regarding innovation & investment it listed out the determinant factors in Ethiopia some of the are unique geographical location, comparatively safe & less corrupted business environment , having a capital city that hosts head quarter of many national & international organizations and a bring a country that's rich in culture and history can attract investors.

4.3 Tax Incentive

TABLE4.5 SIMPLE & TRANSPARENT TAX SYSTEM IN ETHIOPIA

	Frequency	Percent
YES	7	22.6
NO	24	77.4
Total	31	100.0

Before assessing tax incentives it's a must to have an overview about the country tax system and also due to the fact that tax system design is also closely linked to domestic and international investment decisions the researcher has raised question on the tax system in Ethiopia.

More than half of the respondents i.e. 77.4% have indicated their doubt in the country's tax system their main reason is lack of clear & simple tax rule & regulation that can be applied in to different scenarios. Different authors have shown that developing countries lack simple or suitable tax systems, According to (William B. Barker, 2007)" emerging economies do not have a model to rely on that demonstrates the efficient use of their tax systems to provide the critical ingredients for development, including increasing and retaining investment and at the same time increasing tax revenue.

TABLE4.6 EFFECTIVE INCENTIVE ADMINISTRATION

	Frequency	Percent
YES	6	19.4
NO	25	79.6
Total	31	100.0

Respondents were questioned in the effectiveness of investment incentive administration.25 out of 31 respondents response indicate that the incentive administration like the tax system is not simple & transparent. The reasons that are mentioned as a cause are lack of clarity on the law & directives, absence of integrated information system.. According to data collected by customs and revenue authority from 2005-2009 revenue forgone from duties and tax exemptions are on average 51% of total revenue and 5% of GDP per annum. The duties and taxes exempted had shown an annual average growth rate of 49.22% which is an evidence for the increase in incentives. Furthermore since incentive scheme involves imposing multiple tax rates on different sectors and firms it requires many resources to manage and administer it. It may also discourage investment by creating distortion between sectors granted incentives and those not offered incentives. In addition the lack of clear regulation creates an opportunity for rent seeking activities.

TABLE4.7 % OF INVESTORS THAT USE THEIR RIGHT TO INCENTIVE

	Frequency	Percent
0-25%	4	12.9
25-50%	7	22.6
50-75%	14	45.16
75-100%	6	19.4
Total	31	100.0

It's known that any investors that fulfilled the prerequisite for receiving incentive have equal opportunity to use them. But due to different factors mainly because of lack of awareness investors fail to exercise their right. The respondent's response shows that there are some weak links that hinder investors not to exercise these rights. General tax incentives may reduce the risk of corruption in developing countries since the policy is applied to all investors without exemptions or special conditions. In developing countries, corruption is a major problem for the administration and distribution of the country's revenue. Multinational enterprises are able to negotiate more favorable conditions for themselves with the local authorities. This situation may lead corrupt local authorities to take advantage of the multinational enterprises so briefing investors about their rights regarding incentives and incentive mattes are important in smoothing the incentive system and also encouraging investment.

TABLE4.8 INCENTIVE HAS BEEN WELL COMMUNICATED FOR CONCERNED PARTS

	Frequency	Percent
YES	20	64.52
NO	11	35.48
Total	31	100.0

When investment incentives are granted it's obvious that it will help and attract investors to come and invest. In order to get the expected outcome the concerned body has to work on investors regarding the rules, regulation & procedures.64.52% of the respondents indicated investment incentives has been well communicated to concerned parties.

TABLE4.9 AREAS RESERVED FOR INCENTIVES

	Frequency	Percent
MANUFACTURING	4	12.9
AGRI BUSINESS	12	38.7
MINING	2	6.5
INFRASTRUCTURE	5	16.1
SERVICE ORIENTED	8	25.8
Total	31	100.0

The above table show that the 38.7% of the investment incentive has focused on the agriculture sector 25.8% on service oriented,16.1 on infrastructure development ,12.9% in manufacturing industry and 6.5% goes to the mining activity.

The GTP indicates that the government of Ethiopia has given much emphasis on increasing the productivity of agriculture and manufacturing industry. Ethiopia is an agricultural based economy. Half of The country's GDP is generates from this sector also it covers over 80% of export earnings. But the Production is predominantly in the hands of small farmers working individual smallholdings mainly for household consumption. so encouraging investment in the agriculture system will have a significant impact in the development of the country as a whole.

TABLE4.10 OBJECTIVE OF INCENTIVE IN ETHIOPIA

	Frequency	Percent
SECTORAL INVESTMENT	14	48.4
REGIONAL INVESTMENT	3	9.7
TECHNOLOGICAL TRANSFER	5	16.1
EMPLOYMENT/JOB OPPORTUNITY	8	25.8
Total	31	100.0

In the literature part it's discussed that incentive objectives can be categorized in four broad parts. The figure in this study indicates that Ethiopia focuses on sectoral development. Also in the revised investment code of 1996 the government gradually removed most of the sectoral restrictions on investment; Ethiopia's investment code prohibits foreign investment in banking, insurance, and financial services. The remaining state-controlled sectors include telecommunications, power transmission and distribution, and postal services with the exception of courier services. Manufacturing of weapons and ammunition can only be undertaken as joint ventures with the government. Allowing foreign investors to participate in this areas believed to enhance the technological transform and at the same time to generate employment opportunities to the local community. Most of the respondents has supposed Ethiopia's focus is in encouraging sectoral investment.

TABLE4.11 Country of Origin

	Frequency	Percent
SIGNIFICANT	16	51.61
HAVE SOME RELATION	10	32.26
LITTLE IMPACT	3	9.7
NO IMPACT AT ALL	2	6.5

Total	31	100.0

The country's of the investors has significant relation with the amount of investment/FDI. According to EIA data the major sources of FDI inflows to Ethiopia are India, Turkey, China, Saudi Arabia and USA. These countries accounted for more than half of the FDI flows to the country. Germany, Sudan, and Britain are the second major sources of FDI flows to Ethiopia. Most of the FDI sources are developing countries like china, India and Saudi Arabia. This may indicate that most of the FDI flows to Ethiopia are resource and market seeking. Despite Ethiopian government offered many incentives FDI flows from developed country is very low. This condition is also supported by the world bank report for the existence of unfavorable conditions like investor protections, tax payments, contract enforcement, and resolution of insolvency This raises a question of attractiveness of Ethiopian investment environment to efficiency seeking industries which has believed to have a significant role in promoting growth through its spillover effect.

4.4 Tax Incentive & investment

TABLE4.12 WEAK INVESTMENT CLIMATE CAN BESUPPORTED BY INVESTMENT INCENTUVE

-	Frequency	Percent
YES	13	41.9
NO	16	58.1
Total	31	100.0

In the question forwarded to assess the relation between weak investment climate and incentive 58.1% of the respondents indicate weak investment climate cannot be supported by incentive. According to different studies countries with weak investment climate incentive are not effective. The investment climate is a pre requisite for most investors whether they are domestic /foreign to invest in specific location

James(2009) states " In countries with weak investment climates—say, with extensive red tape on accessing land, starting a business, or exporting and importing—lowering the effective tax rate has limited impact on foreign direct investment (FDI). Morisset and Pirnia (2001) support this conclusion, stating that "incentives will generally neither make up for serious deficiencies in the investment environment nor generate the desired externalities

TABLE4.13 INCENTIVE HAS VISIBLE IMPACT ON INVESTMENT

	Frequency	Percent
YES	22	74.2
NO	8	25.8
Total	31	100.0

According to 74.2% of the respondents they that incentive has visible impact on investment the rest 25.8% don't agree with its visible impact. From this we can realize the incentives that are provided have playing their role in attracting investors to invest in Ethiopia.

TABLE4.14 SIGNIFICANT INVESTMENT DECISION FACTORS

	Frequency	Percent
POLTICAL STABLITY	12	38.7
SOCIAL CONDITION	7	22.6
ECONOMIC FACTORS	12	38.7
Total	31	100.0

Based on 22.6 percent of the respondents social condition has less impact on investment decision compared to political stability & economic factors. Political stability & economic factor have equal contribution on investment decision.

TABLE4.15 BETTER FACTOR IN PROMOTING INVESTMENT

	Frequency	Percent
INVESTMENT INCENTIVES	11	35.5
INFRASTRUCTURE DEVELOPMENT	20	64.5
Total	31	100.0

From the given option i.e. investment incentives & infrastructure development that can promote investment better than one another .20 of the respondents believe a better infrastructure in the country can promote & attract investors to invest whereas 11 respondents choose investment incentives has stronger power in power in promoting investment.

According to the respondents, the factors that are considered as tax incentive management are regulations that don’t fit to the real scenario and ambiguous situations, lack of clear control system. Also the respondents point out some points as disadvantage of fiscal incentives.

CHAPTER FIVE

5. SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1.Summary

The government of Ethiopia has been taking changes & reforms in the last 20 years to achieving sustainable economic growth, employment and a rising standard of living in a country, while maintaining financial stability and environmental sustainability, and thus contributing to sustainable economic development. To realize this goal promoting investment has gain due attention. In doing so incentives are ways to attractive investors & to promote investment. A system of investment incentives was created and has been adapted to meet changing conditions. Both fiscal and non fiscal incentives are provided, custom duty exemption, Income tax exemptions are major fiscal incentives.

In this study the major focus were on assessing the investment trend and fiscal incentives. The objectives of the study were:-

- To asses tax incentives implemented in Ethiopia.
- To explore investment in Ethiopia.
- To Examine tax incentives & their relation with investment

The study has gathered data from questionnaires and by analyzing secondary data sources. The studies focus were employees of ERCA & EIA. In the analysis part important points regarding investment & fiscal incentives has been discussed. Secondary data has also been collected from different website and related reading materials.

The major findings of the study reflect these points in General:

- The investment volume in Ethiopia has been increasing since 1992.
- Granting tax incentives have benefits like increasing inflows of FDI, creating employment opportunities and creating technological transfer effect to domestic firms. But the fact shows that non tax determinants factors have more influence on promoting investments than tax factors including tax incentives.

- In Ethiopia both non tax & Fiscal/tax incentives are designed and serving us investment attraction tools. But the administration of fiscal incentives lack clarity and this problem accelerate corruption; increase the forgone revenue due to high administrative expenses.

5.2 Conclusion

In previous chapters of this paper, the bird's eye view of conceptualization and theoretical aspects of investment and incentive was taken place. The paper also used questionnaires and secondary data to asses fiscal incentive effectiveness. In the data analysis, part the researcher found data's that illustrate the condition that based on these the researcher draw conclusion.

- From the data gathered the general tax system of the country is not simple and transparent. The reasons mentioned were complicated rule and regulation that has different meaning depending on situations .As a result the implementing body faces difficulty in serving the society.

- From the data's from EIA Investment has shown remarkable growth status within the last 20 years. The volume and capital of in domestic, foreign and public investments are indicating encouraging numbers, this growth in investment plays vital role in creating employment opportunities, technological transfer and to adjust the counties trade balance.

- Data's show the investment determinant factors mostly depend on the non tax factor than tax factors. We can realize that investors invest in Ethiopia for one of the three reasons the first one is in search of available market for their products market through investment rather than export second, efficiency seeking that's to benefit from the low labor cost or in search of natural resources available in the country but not being attracted to the fiscal incentives
- The major obstacle of investment mentioned is infrastructure. The availability of water, electricity, and road and telecommunication service is basic necessity in operating a business. The government of Ethiopia has realized this problem & is trying to make improvements. For investors the following factors are important: economic and political

stability, production and work costs, qualified labor force, infrastructure, industry tradition, low costs, and development of the country.

- Investment incentive has been well communicated to the investors and most of them are exercising their right.

- The flow of FDI has shown progress in number and also in capital. Most of the foreign investors originated from developing countries like India and Sudan this indicates they prefer to invest because of cheap labor and to find market.

- The other point considered was weak investment climate cannot be backed up by providing incentives.

5.3 Recommendation

- If the government assures low taxes and maintains stability in the country, it will be favorable for investors without any investment incentives. Even if the research showed that investment incentives are effective, there is still no stable control over them. Governments should try protecting their economies and try becoming attractive by ensuring good economic conditions and avoiding grey economic areas such as tax evasion.
- When incentives are provided it is essential that they be based on rules and those benefiting from incentives file tax returns and face audits that governments produce tax expenditure statements so that the cost of incentives is transparent, and those incentives are occasionally reviewed for their efficacy.
- The government has to work on designing simple and transparent tax system that can generate revenue in the mean time it will help to improve the infrastructure service and social welfare.
- The government also has to evaluate & follow up the investment activities if they really are creating positive externalities or performed by the cost of our natural resources and man power.
- To increase investment flow incentive investment promotion activities has to take place. Other than the countries geographical location, natural resources Building good image in customer service, work ethics & culture will also benefit the country.

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APPENDIX

QUESTIONNAIRE

ST MARY'S UNIVERSITY SCHOOL OF GRADUATES

BUSINESS ADMINSTRATION MASTERS PROGRAM QUESTIONNAIRE TO BE FILLED BY

Dear Sir/Madam, this is a research work on The Effectiveness of tax incentive in promoting investment in Ethiopia. Your participation is very important part of this research. Thus, I politely request you to spare some time to fill up this questionnaire genuinely. I would like to thank you in advance for your cooperation.

Purpose

The primary purpose of this study is for the fulfilment Masters Degree in Business Administration. Thereby the research intends to identify the effectiveness of incentive in promoting investment.

Confidentiality

The information you will provide for the study will be confidential. The findings of the study will be general for the study community and will not reflect anything particular of individual person. The questionnaire will be coded to exclude showing name no reference will be made in and will refer reports that link participants of the study.

Thank you!

Section I – Background information

Please indicate your choice by putting a thick mark (√) among the given alternatives

1. Please mention your age

Below 20 ☐ 20-30 ☐ 31-40 ☐ 41-50 ☐ above 51 ☐

2. Sex:

Male ☐ Female ☐

3. How many years of experience do you have in your current organization?

Less than 2 years ☐ 2 - 5 years ☐ more than 15 Years ☐

6- 10 years ☐ 11-15 years ☐

4. What is your educational qualification?

Below Level IV Diploma ☐ Level IV Diploma ☐ Masters Degree ☐

Bachelor Degree ☐ Above masters Degree ☐

Section II The Prevalence (availability) of investment incentives

Please indicate your choice by putting a thick mark (√) among the given alternatives

5. What type of investment incentive is mostly used in Ethiopia?

   Tax incentives ☐ Non tax incentives ☐

6. What are the key areas reserved for investment incentive in Ethiopia?
   A. Agri business
   B. Mining
   C. Infrastructure
   D. Service oriented
7. What is the major objective of tax incentive in Ethiopia?
   A. Sectoral investment
   B. Regional investment
   C. Technology transfer
   D. Employment /work opportunity

8. Do you believe the investment incentive administration is simple & transparent

   Yes ☐ No☐

9. What are the reasons that hinder the tax incentive administration to be simple & transparent?

   ____
   ____
   ____

10. What percentage of the investors you believe that uses their right for tax incentives?
    A. 0-25
    B. 25-50
    C. 50-75
    D. 75-100
11. Do you believe the tax incentive have been communicated/promoted well enough to attract investors?

    Yes ☐ No ☐

12. Which one of the following way granting tax incentive that boosts investment?

    Temporary ☐ permanent ☐

13. Do you believe Ethiopia has a simple & transparent tax system?

    Yes ☐ No ☐

14. Can you mention advantage or disadvantage of tax incentives implemented in Ethiopia?

    ____
    ____

____.

Section II Investment Trend

15. Which one of the following did you see as a major obstacle for investment?

    A. Investment climate(Political stability, economical ,legal)
    B. Tax issue
    C. Infrastructure

16. Which one of the following factors are major determinant of investment in Ethiopia?

    A. Tax factors
    B. Non tax factors

17. Which of the following factor considered as significant in investment descsion?

    A. Political stability
    B. Social condition
    C. Economic factors

18. Do you think weak investment climate can be supported by investment incentives?

    A. Yes ☐ B. No ☐

19. Which factors do you think that will drive investors to invest even without incentives?

    A. Market size
    B. Cost of labor
    C. Market growth
    D. competition

20. Did the area of origin (countries that investors originated) have impact/relation with investment volume?

    A. Significant impact
    B. Does have impact/relation ship
    C. Little relation shipe

21. Do you think investment incentives have visible impact on investment promotion?

A. Yes ☐ B. No ☐

22. Have you experienced a major tax envisions related to carrying out of tax incentives?

A. Yes ☐ B. No ☐

23. Which one of the following factors contribute lot in promoting investment?

A. Investment incentive
B. Infrastructure development

24. Do you think there are alternatives to tax incentive that can encourage investment?

A. Yes ☐ B. NO ☐

25. Mention other alternatives that encourage investment other than tax incentives?

____
____
____
____.

26. Is there any other major activities performed to enhance investment in your office?

____
____
____
_____________________________________.

27. What are the major obstacles you face in executing incentives to action?

____
____
____
_______________________.

DECLARATION

I, the undersigned, declare that this thesis is my original work, prepared under the guidance of Ashenafi . All sources of materials used for the thesis have been duly acknowledged. I further confirm that the thesis has not been submitted either in part or in full to any other higher learning institution for the purpose of earning any degree.

Mistirie Damtew June2014_

Name Signature& Date

ENDORSEMENT

This thesis has been submitted to St. Mary’s University College, School of Graduate Studies for examination with my approval as a university advisor.

___________________________ ________________________

Advisor Signature& Date