

DFID ETHIOPIA COUNTRY ASSISTANCE PLAN 2006-10

CONSULTATION DRAFT

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PART I – POVERTY CONTEXT

THE CHALLENGE

Poverty and Vulnerability in Ethiopia

1. Ethiopia is desperately poor. It contains one of the largest concentrations of poor people on the planet. Ethiopia ranks 170 out of 177 countries on the human development indicator and on present trends will fail to meet any of the MDGs by 2015 and this has implications for the extent to which the whole of Africa will meet them.
2. GDP per capita has increased marginally from \$102 to \$113 between 2000 and 2004, but still remains at one of the lowest levels in the world. 31 million people live below the national poverty line (on less than half a dollar a day) and between 6 and 13 million people are at risk of starvation each year. Not only is Ethiopia poor but it is equally poor: 81% of the population of 77 million live below a poverty line of \$2 a day. There has been little improvement in either income or consumption poverty in the last decade.
3. Livelihoods are predominantly based on agriculture, which accounts for 85% of employment, 45% of national income and over 90% of export earnings. But Ethiopian agriculture remains low-input, low-value and subsistence-oriented, and subject to frequent climatic shocks. Labour productivity in agriculture is low and the country suffers increasingly from shocks from drought, which often lead to severe harvest failure and famine, and affect not only current but future levels of consumption. In the last major drought in 2002/03, over 13 million people in more than half the districts of the country were affected.
4. The most pressing concern of rural communities is the continued pressure on limited land resources. High population growth, slow rural-urban transition and limited employment opportunities outside farming have combined to make a significant reduction in landholdings from 0.5 hectares per person in the 1960s to 0.11 in 1999. Intensive use of smaller plots of land is contributing to environmental degradation in turn feeding back into even lower levels of agricultural productivity, and effectively locking many into a poverty trap.
5. Patterns of social exclusion affecting particular social groups or segments of the population contribute to increasing vulnerability in Ethiopia. Women are especially disempowered. There have been gradual gains in gender equality in Ethiopia but there is also a deep conservatism that pervades gender roles, severely proscribing what women can and cannot do, especially in rural areas. The extent to which gender inequity in Ethiopia is deep-rooted is epitomised by the widespread acceptance, by women themselves, of violence against women.

6. Women's poverty is characterised by their limited access to resources, services and employment, and inability to claim their rights: only 9% of women have access to agricultural extension services and 12% to agricultural credit; only 32% of permanent civil service posts are held by women, and only 10% of those are in professional cadres. The relatively high prevalence of harmful traditional practices, such as female genital mutilation, early marriage, and marriage by abduction significantly affects the vulnerability of women and girls, for example by increasing their risk of HIV infection, reducing their chances of finishing school, and violating their reproductive and sexual rights.
7. Pastoralists' traditional social, economic and political systems are being eroded. The delivery of services to Ethiopia's 11 million pastoralists is a major challenge for the Government, and a lack of mutual awareness and understanding has led to pastoralists' needs being excluded from policy development.
8. The overall health status of people in Ethiopia is extremely poor. Life expectancy is 54 years. Despite some improvements in recent years, the rates for maternal mortality, under-five mortality and infant mortality are high. High fertility is a major contributor to poverty.
9. The main health problems are communicable diseases, due to poor personal hygiene, proper garbage and waste disposal practices, and lack of an adequate and safe water supply. The major causes of death are infectious diseases (TB, respiratory illnesses, malaria, gastrointestinal infections, meningitis, AIDS and leishmaniasis).
10. Malaria is one of the country's worst health problems. 68% of the population is at risk of infection and malaria accounts for 10-30% of the disease burden in all age groups. Ethiopia is one of the world's 22 top countries for tuberculosis incidence.
11. In the past 40 years, the performance of the Ethiopian economy has been variable, with a very poor underlying trend of 0.2% annual growth in GDP per capita over the period 1961-2003. Due to the dependence of the economy on agriculture, growth has historically been affected by climatic variability, the terms of trade (eg the effects of volatility in international coffee prices), and conflict. Growth spurts have tended to be short-lived and associated with positive climatic shocks such as good rainfall. The main driver of growth in agriculture has been the expansion of land under cultivation rather than increased productivity, which is unsustainable in the medium to long term.
12. There is little in the way of export-led growth: Ethiopia is a landlocked country and trade (both internal and external) is constrained by the large distances and poor transport infrastructure. Growth rates increased in the 1990s, and since the war with Eritrea ended in 2000 the Ethiopian economy has performed relatively well, even despite the drought in 2002/03. Over the past five years the average growth rate has been 4-5% per annum, although this translates to only 2-2.5% growth in GDP per capita given rates of population increase, falling far short of what is needed to meet the \$1 a day MDG.

Improvements in Human Development and Progress towards the MDGs

13. Despite the lack of progress in reducing income poverty, the commitment of the Government of Ethiopia to poverty reduction is starting to yield positive results in measures of non-income poverty.
14. There has been an improvement in the level of access to education in recent years, and the gender gap in primary education has narrowed (although it has widened at secondary level). Literacy rates have improved, but remain very low with a significant gender gap. The poor quality of education remains a key concern. Access to health care remains low, but health indicators are improving. Immunisation against childhood diseases is increasing and infant and child mortality rates are falling. While national HIV prevalence is estimated at 4.4% amongst those aged 15-49 years (1.5 million people), analysis of the trend suggests that new infections may be slowing down. There have been increases in the proportion of the population with access to safe drinking water and sanitation facilities, although the levels remain low and rural-urban variations persist.
15. These results are all the more impressive against the backdrop of a rapidly growing population. The population is growing at a rate of about 2 million more people each year, which has implications for the distribution of resources, the performance of the economy and the ability of the state to deliver services. A significant expansion is required each year just to keep service coverage and per capita income levels the same: the Ethiopian economy is running to stand still!
16. Despite this commendable progress in human development, Ethiopia remains unlikely to meet any of the MDG targets by 2015. If it is to have any chance of doing so, there will have to be a major improvement in economic growth and massively scaled-up external assistance.

Government Plans for Poverty Reduction

17. In 2002 the Government produced its first PRSP, the Sustainable Development and Poverty Reduction Programme (SDPRP), setting poverty reduction as the core objective with economic growth as the principal means to achieve it. The SDPRP was built upon four pillars:
 - agricultural development-led industrialisation and food security;
 - the justice system and civil service reform;
 - governance decentralisation and empowerment;
 - capacity building.
18. In the 3 years since its launch the Government made good progress in maintaining macroeconomic stability and in boosting the poverty focus of its expenditures. Economic growth was hit by the drought of 2002/3 but has since rebounded strongly. The Government took important

initiatives in the launching the Coalition for Food Security and its comprehensive programme for capacity building. During the SDPRP period the Government's pro-budget allocation and progress in increasing domestic revenues have contributed to the upward trend in many social indicators. Progress in various areas was constrained, however, by the need for policy development to achieve the Government's objectives. These included

- overcoming the policy and institutional constraints to the development of the private sector;
- rethinking rural development strategies to foster employment generation, crop diversification and private sector involvement in rural areas;
- strengthening rural urban linkages and focusing on growing urban development issues;
- operationalising the national population policy;
- strengthening decentralised institutions to create the conditions for accountable and responsible local government and enhanced democratic participation;
- strengthening monitoring and evaluation systems, and taking forward partnership commitments.

19. Many of these points are addressed in the second PRSP, the Plan for Accelerated and Sustained Development to End Poverty (PASDEP), which the Government is in the process of finalising. Like its predecessor, the PASDEP has very strong Government ownership. For the first time it was debated and approved by Parliament. It has been designed to accelerate the effort to reach the MDGs. It builds on the first poverty reduction strategy, and is innovative in several important respects.

20. The PASDEP reflects a consensus that pro-poor growth is a fundamental priority. The programme centres around a growth strategy for the next five years consisting of eight elements:

- (i) commercialisation of agriculture and promoting much more rapid non-farm private sector growth;
- (ii) geographical differentiation, with a greater emphasis on urban development;
- (iii) population policy;
- (iv) addressing gender inequalities;
- (v) infrastructure development;
- (vi) risk management and vulnerability;
- (vii) scaling up service delivery to reach the MDGs; and
- (viii) generating employment.

21. The PASDEP advocates continuing to pursue the strategy of agricultural development-led industrialisation, but with a more balanced approach to urban development and with important enhancements to

capture the private initiative of farmers and encourage the shifts to diversification and commercialisation of agriculture. It advocates a private sector push, especially on exports, to create jobs and reduce foreign exchange constraints.

22. There is a reinforced emphasis on good governance, with plans to accelerate local empowerment, and exploit regional differentiations. Decentralisation, first to the regional, and then to the district (woreda) and sub-district (kebele) levels, remains a centrepiece of the Government's strategy both to improve responsiveness and flexibility in service delivery, increase local participation, and democratise decision-making. Policy reforms are expected to be enacted in a number of key domains during the PASDEP programme, including revisions to civil and commercial law, human rights, sexual/gender harassment, and children's and HIV/AIDS-affected persons' rights. A justice sector capacity building programme will aim to train and support the judiciary. The Human Rights Commission and Ombudsman's Office will both be strengthened as part of the PASDEP, with the establishment of systems and procedures, and capacity-building and increased gender sensitivity. The emphasis on civil service reform and capacity building will continue, with a focus on strengthening staffing and incentives, and setting service standards for responsiveness to the public. There is also an increased emphasis on training of Parliamentarians.

Assessment of PASDEP

23. The PASDEP is a Government-driven plan for poverty reduction, with clear targets and indicators to measure progress annually which provide the framework for results-oriented policies and strategies. The PASDEP is a medium term plan consistent with meeting longer term development objectives. However, some of the PASDEP targets may be over-ambitious and are unlikely to be affordable within the resources which currently appear to be available. In some areas, the linkages to the MDG targets could be more explicitly developed. There remains a need to make sure that the PASDEP and sector strategies are fully compatible and consistent which will help in ensuring that the targets are met through linkages with the budget and with the policy and results matrix on which monitoring and evaluation will be based. Further work is needed on developing the linkages between various sectors; including how cross-cutting issues such as gender, HIV/AIDS, population, vulnerability, the environment and governance could be more effectively mainstreamed across the sectors.
24. The Government of Ethiopia recognises that good economic and social sector policies, if they are to be implemented successfully, depend on effective state capacity. Capacity building is central to the Government's strategy for reducing poverty. The PASDEP identifies civil service reform and decentralisation as priorities, particularly strengthening the capability of local government to formulate and implement development plans, manage resources and deliver services

to citizens. It also demonstrates commitment towards making further progress on core aspects of public sector reform and democratic governance that promotes the rights of all its citizens, as enshrined in the constitution. However, the PASDEP does not adequately identify the critical contribution that civil society could make reinforce accountability to citizens, and in advancing empowerment and voice.

25. The PASDEP sets a target of 7% growth to achieve the MDGs: well above the historical medium term average of 5%. Expanding the infrastructure backbone is a top Government priority with focus on rural areas. Its progress will be critical to accelerating economic growth and increasing access to, and integration of, markets. It prioritises major economic infrastructure investment, including hydropower, irrigation, telecommunications and all-weather roads. Key challenges with respect to infrastructure investment include: the raising of adequate financing for capital investment; ensuring sustainability through the provision of a sufficient recurrent budget for operation and maintenance; and the limited domestic capacity for both management and construction activities, particularly at the regional and local level. Government policy provides little room for private sector investment in infrastructure. Most utility sectors (e.g. telecommunications, power, and transport) are state-owned enterprises and competition is constrained.
26. Although there is an increased emphasis in the PASDEP on the importance of growth, including the role of increasing agricultural productivity and an increased role for the private sector, key policy constraints need to be addressed to create a positive environment for private sector involvement in agriculture.
27. While World Bank surveys suggest that there have been some improvements in the business environment over the past three years, the climate for private sector development generally is weak. Bureaucratic hurdles impede business start-up processes, and make importing and exporting difficult. The legislative framework for regulation, contract enforcement and dispute resolution is weak, undermining investor confidence. Access to finance, particularly long term finance, is inadequate and there are severe restrictions on foreign direct investment. Lack of infrastructure also constrains the return on private sector investments more broadly. The PASDEP strategy intends to address these challenges through: the development of an institutional framework to enable private initiative, including legislative and financial sector reform and privatisation. Without further policy changes it is unlikely that the PASDEP targets for economic growth will be realised.
28. Ethiopia faces major challenges from current levels of environmental degradation and emerging threats from climate change. In a context of extreme dependence, especially of the poor, on an already fragile natural resource base, growth and development prospects are undermined. The Government has recognised, both in the PASDEP and in its international commitments to climate change-related

agreements, that Ethiopia is acutely vulnerable, one of the countries likely to be worst affected, and yet with the least capacity to respond. Despite this, implementation mechanisms are not well advanced, and are compounded by limited resources and capacity.

29. The Government recognises that development partners will have a key role to play in providing both financial and technical support for the implementation of the PASDEP. Unconstrained cost estimates using sector financing plans and the joint Government/World Bank MDG needs assessment suggest that poverty-oriented spending over the next five years would need to be in the region of \$39 billion; which is unlikely to be realistic. Sensibly the macroeconomic and fiscal framework in the PASDEP plans for expenditure of a little more than half this amount (\$27 billion), but even for this lower expenditure framework, external funding of \$1.6 billion will still be required. The PASDEP does not explore the implications of lower levels of expenditure for the implementation of sector strategies and the achievement of sector targets.

Governance

Accountability

30. The Ethiopian constitution provides the model for an ongoing state transformation process which began with the overthrow of the previous regime in 1991. The constitution provides for the equality and right of self-determination of nationalities and devolves power to ethnically-based regions and sets out exemplary institutions for state accountability.
31. The Government is committed to implementation of the constitution but there are serious challenges. Historically, Ethiopia's political institutions were very centralised and hierarchical. Power was held by minority ethnic groups from the highland areas and there has been a lack of downward accountability. There is a weak tradition of political compromise with polarised views, for example, on federalism, land privatisation and the appropriate role for the state in the economy. Key institutions for managing political conflict are underdeveloped: the centre still exercises strong control over regional executives, civil society and the media; national and regional parliaments are underdeveloped; the judiciary needs strengthening; and power is still seen to rest with the traditional elites.
32. The May 2005 elections were by far the most openly contested in Ethiopia's history. The access to electronic media given to all parties was exceptional. The ruling EPRDF party retained a majority in Parliament with a notable increase in the number of seats won by the Opposition. The results were not accepted by leading Opposition parties and election-related violence broke out in June and November 2005, resulting in a security clampdown and reported human rights abuses in many parts of the country. After an initial boycott, most

Opposition MPs have now taken their seats in the Federal Parliament. Efforts have been made to start reopening political space and reviving talks with the Parliamentary Opposition. New parliamentary rules of procedure have the potential to allow a greater role for the Opposition and initial steps have been taken to reform the National Election Board and media laws. The 2005 post-election crisis fits within a cycle which started in 1991 in which political space closes around election periods and then re-opens; the special feature of 2005 was the exceptional opening up of political space before the elections.

33. The hierarchy of the Ethiopian state, from the federal to the regional, to the woreda level, is designed to increase vertical accountability and participation by bringing Government closer to the people. There are institutions in place, such as the judiciary, Parliament, the Office of the Federal Auditor General, and the Anti-corruption Commission, but their effectiveness to hold the other branches of government to account is limited.
34. The Government has a stated commitment to reinforce capacity and move forward on democratic decentralisation and pluralism. While progress has been made in decentralisation, further action is required to make the state apparatus more responsive and accountable. A number of fiscal, technical and political constraints limit the downward accountability and meaningful responsiveness of state institutions to citizens. But the Government professes determination to improve the situation. Accountability is hampered by the lack of separation between the role of the party and the state. There is a recognition and pressing need to develop a permanent and impartial civil service if the process of democratisation and accountability is to be taken forward. The Government accepts the state should be more open but believes the civil service and judiciary currently lack the necessary ethics and results-based culture.
35. Opposition parties for their part are young and evolving, sometimes with weak policy agendas and inability to engage the Government constructively, plus an over-reliance on policy and finance from the external diaspora.
36. The trajectory of change since 1991 is positive in that citizens have become much more aware of their rights and are prepared to express views. But the lack of a democratic tradition and the tendency for the political space to be highly contested means that the transition of Ethiopia to a modern democratic state is likely to continue to be fraught with periods of progress and reversal.

Capability

37. The formal institutions of the state are well-defined and governed by clear rules. But problems arise in implementation due to weak human resources and poorly functioning systems. Weaknesses are particularly

acute at the district (or woreda) level, which has the front-line responsibility for the delivery of basic services.

38. The Government has a strong desire to build the capacity of the public administration and has embarked on a large scale programme of public sector reform which aims to improve public financial management, service delivery, citizens' empowerment and good governance. Generally fiduciary standards are high and corruption in public finance is not a major concern, although there are criticisms of some close links between the ruling party and business. The Government recognises the need to speed up the implementation of procurement reform and financial management information systems at all levels.
39. The management of conflict presents a major challenge to Ethiopia's development. Internal or local conflict is generally the result of disputes over resources, although renewed conflict over the domestic political situation remains possible. There are persistent disputes, often across national borders, leading to open conflict between pastoralists and sedentary farmers. A number of regionally based armed groups, seeking independence or political concessions for their ethnic populations, advocate the overthrow of the Government by force. State and regional capacity needs to be developed to analyse and manage internal and external conflict effectively. Ethnic federalism was introduced to diffuse ethnic tension by allowing self-governing geographical areas based on linguistic groups, but the process of identifying ethnic majorities at various levels of government has led to fierce and sometimes violent competition for political power.

Responsiveness

40. Ethiopia has adopted an ethnic-based federal system, with a parliamentary form of government, and a tripartite separation of power into legislative, executive and judicial branches at all tiers of government. The government structure has three levels: federal government, regional states, and woredas (equivalent to districts).
41. The constitution (1994) enshrines the fundamental human and democratic rights of all Ethiopian citizens. These include social, economic and political rights such as the right to "freedom of thought, opinion, expression, association, movement, assembly, access to justice and security" and the right to "vote and to be elected at periodic elections to any office at any level of government". Nevertheless, respect for human rights in Ethiopia is a concern and more needs to be done to ensure that individual rights are protected.
42. The decentralisation process introduced in the early 1990s is undoubtedly one of the most significant changes in the history of Ethiopia, by shifting away from a central unitary to a decentralised form of government that provides each region with sufficient autonomy. The accompanying fiscal decentralisation devolves decision-making powers to lower tiers of government. Financial resources are transferred from

the federal government to regions and woredas in the form of general purpose grants, untied or unconditional, and provide discretion on the use of the financial resources and spending.

43. There is little tradition of partnerships between the Government and civil society. Civil society organisations are widespread but small in scale and mostly restricted to basic service delivery. Membership-based organisations, such as youth and farmers associations, are given a clear role in development. There is a perception in the Government that organisations which do not have a membership base are unaccountable and may have political motivations. There is scope for greater civil society engagement in monitoring service delivery and articulating greater 'voice' in the development process.

The Regional Dimension

44. Ethiopia is the lynchpin to regional stability in the Horn of Africa. Ethiopia's relationship with its neighbours has been historically stressful with a history of open hostility and wars. Ethiopia remains at risk of war with Eritrea while the dispute over the boundary remains unresolved. The threat of Ethiopia's becoming embroiled in conflict in Somalia is significant in the absence of any effective regional or international mediation.
45. Regional instability, particularly in Somalia, and with Eritrea, has the potential to undermine Ethiopia's security and lead to violence and unrest in the Ogaden and perhaps other regions of Ethiopia. There is a possibility that this might, in turn, undermine relations between Ethiopia's two main religious groups damaging a relationship that hitherto has been one of tolerance and peaceful coexistence.
46. Commercial and economic links to the sea using Djibouti remain vital for both sides, but especially for Ethiopia as a landlocked country. Ethiopia has close relations with Somaliland whose stability it encourages (and whose port Berbera is now more used) and Puntland, neither of which wish a rise of religious extremism.
47. Ethiopia has close contacts with Sudan. Ethiopia looks to Kenya, Sudan and Yemen (via Djibouti) for access to markets (including for hydro-electricity) and international economic connections. The Nile Basin Initiative is an important framework for co-operation over management of the Blue Nile with Sudan and Egypt.
48. Addis Ababa is the seat of the African Union and UNECA. The HMG team in Addis Ababa is supporting the growing institutional capacity and role of the AU in setting standards and policy for African states, including in efforts for peace and security, better governance and human rights and poverty reduction. The UNECA is an important regional institution providing wider African perspective and policy inputs into African standards, programmes and research.

WHAT WE HAVE LEARNT

49. The period since DFID's last CAP has provided a strong learning experience in Ethiopia. It represented a period of real optimism accompanied by an increase in aid flows by donors, followed by a reversal due to political events in 2005. It also represented a period in which DFID established a country office for the first time and greatly increased our own development effort, from £44 million in 2003-04 to just over £80 million in 2006-07.
50. The Ethiopian Government has demonstrated its commitment to poverty reduction. Its budget is one of the most pro-poor in Africa and, as a result of increased spending on basic services, development indicators are starting to show a sustained improvement. The public service has demonstrated its ability to absorb increased funds and aid donors have indicated their willingness to scale up.
51. It has become apparent that the transition of Ethiopia to a modern democratic state is not going to be a straightforward or a linear one. The opening of political space in the run-up to the elections of 2005, and its subsequent closing down, combined with an increase in political violence, has increased overt polarisation in the country and exposed ethnic differences. With both local and national elections due within the CAP period, we might see a repeat of this cycle. Governance and human rights work needs to be central and sustained throughout the period.
52. Given the complexity of issues in the Horn, we have learnt the need to see Ethiopia through the lens of regional and peace/security dynamics. Without a normalisation of relations between Ethiopia and Eritrea, the tensions can be a distraction from developmental effort. There is also the prospect of increasing tension between Ethiopia and Somali extremists which could further draw attention away from democratic development.
53. The Government of Ethiopia retains very strong ownership and a well-articulated rationale of its development programmes. Experience has shown that the best way to influence policy is through sustained, well-informed engagement and evidence based argument, mutual respect and willingness to share experience and expertise.
54. Civil society plays a key role in both development and humanitarian activities. Civil society is slowly emerging as a more active player in advocacy for change and policy dialogue. Recent estimates of the financial resources provided by NGOs and their reach of the population reflect their extensive operations. We now realise that we need to acquire a greater understanding of the resources available to civil society and the comparative advantage of civil society in meeting the needs of the poor.

55. Gender inequality continues to be a major impediment to the achievement of the Government's poverty reduction objectives. It is both a human rights and a development issue and needs to be addressed explicitly and concretely.
56. Direct budget support, previously the preferred method of aid funding for both Government and donors, was suspended suddenly in 2005. This has been a major factor in financial instability. Both the Government and donors cited a breach of trust by each other suggesting that, over the medium term, all parties must work to understand better the other's perspective on this fundamental issue, to build realistic expectations, trust and predictability. The implications of the donors' decision to suspend direct budget support were not made sufficiently explicit when the decision was first announced, and since donors had not planned for this contingency new instruments had to be created under intense time and political pressure.
57. The federal nature of the Ethiopian state and its commitment to fiscal decentralisation makes it difficult to design sectoral initiatives, because assigning resources to a particular sector undermines the decentralised approach and the mandate of local government bodies to decide on priorities.
58. The recent period has underlined the importance of working as a coherent team both as HMG and in terms of donor harmonisation, which has made great advances in the last three years. While donor harmonisation has reduced transaction costs on the Government, the transaction costs between donors have risen very sharply. The processes of agreeing joint strategies and joint programmes are severely constrained by the human resources that donors have available on the ground and the unequal decentralisation of decision-making among donors.
59. The work and dialogue involved in the move away from projects and the effort put into donor harmonisation has tended to detain DFID staff in Addis Ababa. Effective implementation of this new CAP will require DFID staff to travel to the regions and into rural areas with far greater frequency, in order to develop and reality-check new ideas and approaches.

PART II – UK PARTNERSHIP PLANS OVER THE POVERTY STRATEGY PERIOD

UK AND INTERNATIONAL DEVELOPMENT PARTNERSHIPS

60. In 2005-06, Ethiopia developed a new, strongly nationally-owned poverty reduction strategy, the Plan for Accelerated and Sustained Development to End Poverty (PASDEP). DFID and other donors, including the World Bank, African Development Bank and the European Commission are committed, through their own country strategies, to supporting the poverty reduction and growth enhancing plans on which it focuses. DFID has liaised closely with the main multilateral and bilateral donors in the preparation of this CAP.

Country Strategies of Multilateral Agencies in Ethiopia

The **World Bank Interim Country Strategy 2006-08** focuses on governance and growth.

To achieve this objective, the Bank will strengthen good governance and growth in the following areas: (i) “core” governance—public administration, decentralisation, and public financial management; (ii) the provision of basic services in a fair and accountable way; (iii) the promotion of free enterprise; (iv) improved agricultural productivity; and (v) the development of infrastructure to nurture the growth of small towns and growth corridors.

Key studies and reports that will be undertaken during the strategy period include the institutional and governance review, the joint budget and aid reviews, an investment climate assessment survey update, civil society dialogue, a study on decentralised service delivery, a rural public expenditure review, and a new country economic memorandum on governance and growth.

The **African Development Bank Country Strategy 2006-09** aims to promote growth.

The focus will be on three PASDEP pillars namely: (i) infrastructure development; (ii) agricultural transformation and; (iii) governance. New interventions under ADF X will be limited to infrastructure and governance. The focus within the governance pillar will be on strengthening accountability and transparency in basic service delivery and the focus under infrastructure will be power, water and sanitation and roads.

The Bank will also promote regional integration involving Ethiopia and its neighbouring countries in the broader context of the NEPAD. The priorities will be on infrastructure projects including power inter-

connection projects. Non-financing activities will include policy dialogue and targeted economic and sector work.

The European Commission Country Strategy 2008-12 *currently under preparation - to be completed once we see the final draft*

The **UN Development Assistance Framework (UNDAF) 2007-11** provides a common strategic framework for the operational activities of the UN system in Ethiopia. It focuses on five priority areas (i) humanitarian response, recovery and food security; (ii) basic social services and human resources; (iii) enhanced economic growth; (iv) good governance; and (v) HIV/AIDS.

61. Achieving the MDGs by 2015 in Ethiopia is a very ambitious target. Although human development indicators are improving, Ethiopia is unlikely to meet any of the MDGs by 2015 without a considerable scaling up of external assistance: an MDG needs assessment in December 2004 estimated the cost at \$120 billion. The five year PASDEP has been costed at \$27 billion. Greater funding, and the substantial poverty challenges outlined in Part I, will require donors to work ever more closely together, with the Government, and with civil society. Attention also needs to be paid to sequencing any major increase in development assistance to minimise adverse effects on national competitiveness.
62. Scaling up also requires a sustained focus by the Government and development partners on political and economic governance. The UK's 2006 White Paper on International Development places this at the heart of delivering effective development. Rebuilding the trust breached in the aftermath of the 2005 Ethiopian elections, and assisting citizens to participate more fully is an essential part of the UK and other donors' approach.
63. Donor harmonisation is well advanced in Ethiopia around the Paris principles. There is an active donor group (the DAG), which works well in tandem with the Donor Ambassadors Group. The Government has led the completion of a Harmonisation Action Plan and chairs a joint Government/donor task force on harmonisation. Ethiopia is a pilot for OECD/DAC harmonisation and work is well advanced on an Addis Declaration to enshrine these principles in the local context. EU donors have signed a Road Map committing themselves to greater harmonisation within wider donor harmonisation frameworks.

DFID's areas of focus in Ethiopia

64. DFID has identified the following five overarching objectives to support the PASDEP:

- supporting the development of a capable, accountable and responsive state;
- promoting better service delivery and human development;
- promoting pro-poor growth;
- reducing the vulnerability of the very poorest;
- working with others for more effective development in Ethiopia.

DFID will support the development of a capable, accountable and responsive state

65. The Government's openness to inclusive political dialogue and plurality, along with stronger participation and demands for accountability by the Ethiopian people, will be supported by DFID and the other HMG departments represented in Addis Ababa. All donors' development plans are based on the principles of long term engagement with Ethiopia, in-depth governance discussions with the Government; and the need to work more broadly with civil society.

66. The HMG team will work closely with other donors in developing a joint governance strategy, and in monitoring governance reforms through the PASDEP policy matrix. We will improve our understanding of drivers of development in Ethiopia, exploring ways to develop consensus around contentious issues such as land, federalism and civil society. We will promote the NEPAD governance agenda including the Africa Peer Review Mechanism and, while recognising the Government as our main partner, will broaden links with civil society and the private sector. We will also explore a joint donor/government overarching memorandum of understanding for development in Ethiopia. To improve mutual accountability, partnership and quality dialogue, we will press for objective reports on the performance of donors and the Government to be discussed at annual donor/Government reviews.

67. Without the reform of state institutions, the success of the Government's modernisation programme will be jeopardised. DFID will continue to contribute to the Government-led Public Sector Capacity Building Programme (see below) and provide targeted technical assistance for civil service reform in order to strengthen the accountability, independence, political neutrality and transparency of public institutions and the capability of decentralised governments. We will also consider developing a human security programme to strengthen the state's capacity to handle both internal and external tensions effectively and accountably.

68. While there has been some progress in bolstering the capacity and independence of the judicial and legislative branches of the state, there is still a lack of effective checks and balances on the use of state assets and authority. We will support key accountability mechanisms including federal and regional parliaments, the judiciary, the National Election Board, the Human Rights Commission, the Ombudsman, the Office of the Federal Auditor General and the media through multi-donor funding mechanisms. DFID will promote the adoption of NEPAD governance standards and encourage the Government to participate in the African Peer Review Mechanism.
69. DFID will work with its donor partners to encourage and assist Government initiatives that address the current democratic deficit. We will offer help in building sustainable and effective conflict management and peace building strategies. In the longer term, informed by thorough research and analysis, we will seek ways of working with the Government, to address the current political and institutional barriers to the delivery of safety and security to the people of Ethiopia. We will provide funding for a joint civil society support programme which will improve the regulatory environment for CSOs and their opportunities to engage with the Government in policy processes, as well as building CSO capacity.

DFID will promote better service delivery and human development

70. Although there has been a dramatic growth in enrolments in recent years Ethiopia is unlikely to meet the MDGs for education and signs of distress are emerging, particularly related to the quality of education. The main challenges in the coming five years will be around improving education quality, closing the gender gap, ensuring a balance between investment in the different levels (from primary to tertiary), and developing a more balanced and affordable financing framework.
71. DFID will therefore maintain a strong focus in education to develop a long-term engagement with the Ministry of Education in Ethiopia. We will work closely with the Government to strengthen its capacity to deliver on its Education Sector Development Programme. We will support the Government both in developing policies and activities that emphasise quality in the education sector, particularly in the area of teacher development, and in its strategies that specifically address gender disparities in education. We will continue to work closely with other development partners, especially the World Bank and the Netherlands, in developing joint instruments and to ensure overall harmonisation. Through the Protection of Basic Services (PBS) grant (see below), we will ensure that more resources reach the schools, allowing greater access to quality education.
72. The Government has ambitious plans to extend basic health care to the one-third of Ethiopians who currently have no access to health services, and to ensure universal access to HIV/AIDS prevention,

treatment and care. The Government sees population growth as a threat to poverty reduction and is keen to capture the 'demographic bonus' associated with reduced fertility.

73. Recent trends in contraceptive prevalence, immunisation, child mortality and HIV infection are encouraging, but there has been very little progress in improving maternal health care, mainly because of the general weakness of health systems. The Ministry of Health is leading efforts to improve harmonisation. Trends are encouraging, for example, all health donors and the Ministry of Health signed a code of conduct to improve harmonisation in 2005, but much remains to be done. Large external resources are available particularly for HIV/AIDS through the Global Fund for AIDS, Tuberculosis and Malaria, and the US PEPFAR fund, but there is limited flexibility in the ways these funds can be deployed and the health system must be greatly strengthened in order to put them to good use.
74. DFID will promote health system strengthening and health sector harmonisation through pooled funding instruments (including the Protection of Basic Services grant and the Health Pooled Fund). We will also strive for greater coherence through involvement in the HIV/AIDS Donors Forum and the Global Fund Country Coordination Mechanism. In order to enhance Ethiopia's overall response to HIV/AIDS, DFID will work to strengthen the capacity of the Government HIV/AIDS Prevention and Control Office and that of civil society partners.
75. DFID will continue to contribute to sexual, reproductive and maternal health interventions through government and non-government partners, using pooled funding mechanisms. Contraceptive security and access to family planning and condoms will be addressed through the DKT project, Component 2 of the Protection of Basic Services grant and the Family Guidance Association of Ethiopia. In addition to expediting progress toward the health MDGs, such programmes will enhance Ethiopia's efforts to limit population growth.
76. In line with the high priority given to water and sanitation by both the PASDEP and by DFID corporately, we will provide technical assistance to the sector, complemented by a substantial investment in water and sanitation service delivery. DFID's activities will be developed under the umbrella of the EU Water Initiative, and we will promote this as a means to achieve a more coordinated approach to sector planning, implementation and performance measurement of the sector. We will also promote DFID UK's RIPPLE programme (Research-Inspired Policy and Practice Learning in Ethiopia and the Nile Region) for improving sector policy analysis.

DFID will promote pro-poor growth

77. A major improvement in economic growth is necessary to have a sustainable impact on poverty reduction and to generate a revenue

base sufficient to finance critical investments in social services for human development.

78. Central to improving the economy's performance is development of a policy environment which assists economic growth: one which supports private sector development, increased investment and improved agricultural productivity, and increased access to non-agricultural livelihood opportunities. DFID will work closely with other donors to assist the Government in further developing its policy for pro-poor growth, based on hard evidence, which will facilitate increased investment and help achieve the PASDEP target of 7% growth per annum.
79. The PASDEP confirms the Government's commitment to improving infrastructure to improve access to both internal and external markets and to services. This includes plans to expand the road network, to improve the maintenance of existing roads, and to improve access to water, power and telecommunications for productive as well as social benefits. To date, DFID's investment in economic infrastructure has been in the form of limited technical assistance to the transport sector. Over the period of this CAP we will explore ways of becoming more involved in infrastructure and associated service provision, working with multilaterals such as the World Bank, AFDB and EC. These may focus around the areas of road access, productive investment in the water sector (irrigation, storage and, potentially, hydro-power), rural electrification and decentralised energy services.
80. We will contribute to the policy dialogue by undertaking joint analysis of the social, economic and political factors that currently hamper access by the poor, especially women, to economic opportunities and their full potential to bring about growth. To maximise the effectiveness of our capital investments we will support improvements in economic governance arrangements, institutional strengthening and public investment analysis. Complementary activities through the Public Sector Capacity Building Programme (see below) and other sector-specific assistance will help ensure that there is sufficient absorptive capacity at all levels of government.

DFID will reduce the vulnerability of the poorest

81. A major challenge in Ethiopia is to reduce the vulnerability of the poorest, brought about by a combination of natural and manmade factors. The threat of a major famine remains. The implications on vulnerability of climate change, population growth and long term environmental degradation are becoming more acute. The PASDEP indicates that of the 15 million people who are at risk from food insecurity and other forms of vulnerability, over 8 million are chronically food insecure. This means they can never meet their annual food needs, regardless of shocks, because they lack sufficient assets to be productive. The other 7 million are periodically affected by food insecurity, typically in a year of poor rainfall.

82. Historically, vulnerability was addressed through a system of annual emergency appeals, but the primary function of this system has been diluted through the inclusion of predictable non-emergency needs. The system therefore does not meet its primary objective of mobilising disaster relief resources for critical humanitarian needs, and this translates into inappropriate responses that threaten lives, livelihoods and Ethiopia's progress towards the MDGs.
83. The PASDEP outlines the Government's commitment to improving food security and enhancing rural livelihoods for poor Ethiopians. A consortium of donors including DFID will provide assistance through the Productive Safety Net Programme (PSNP). This programme aims to decrease the vulnerability of poor people to food crises, by providing cash for productive employment through labour-based public works activities, to reduce the repeated need for emergency food handouts. The PSNP builds households' minimum assets to allow up to 8 million people to move away from vulnerability towards more secure livelihoods. It will provide between US\$ 100-200 million in cash transfers into the rural economy each year over the next five years.
84. To achieve its purpose the programme will require improved links to rural development service providers (such as credit and veterinary services), markets, infrastructure development, private sector and small towns. Currently these links are either unavailable or under funded. We and other PSNP donors will work with the Government to identify new ways of ensuring sustainable livelihoods.
85. Both the PASDEP and the UK's White Paper on International Development make commitments to reform the humanitarian response system including the practice of annual emergency appeals. DFID will continue to channel funds through the OCHA-managed UN Humanitarian Response Fund in Ethiopia which provides an effective means to address unpredictable emergency humanitarian needs, and will also support moves towards a single, common UN programme for managing risk and vulnerability in the country.
86. In fulfilling its commitments outlined in the UK White Paper DFID will support processes that increase an awareness of climate change, increase the capacity to address climate and environmental challenges and develop innovative approaches to reduce the human and economic impact of periodic disasters.

DFID will work with others for more effective development in Ethiopia

87. Cooperation and joint working will be a fundamental principle of DFID's engagement in all areas. DFID will continue to operate under the aegis of the overall donor group in Ethiopia, to develop with the Government a harmonisation declaration to implement the Paris aid effectiveness commitments. Within that, we will seek closer collaboration with the EC and other Member States in areas such as diagnostic research. We will continue to participate in joint donor funding evaluations and in the

annual overall monitoring of the PASDEP. This collaboration will be enhanced by improving our understanding of the constraints and challenges facing non-federal government bodies

88. Poverty monitoring and evaluation is important for assessing development effectiveness. Under the SDPRP the Government developed a “Monitoring and Evaluation Action Plan” to enhance its capacity for measuring poverty and informing policy decisions. With financial assistances from donors the Central Statistical Authority (CSA) undertook two major national surveys: the Household Income and Expenditure Survey and the Welfare Monitoring Survey. Good progress has been made in a number of areas such as increasing overall CSA capacity; making CSA information more widely available; and undertaking the first participatory poverty assessment in several years.
89. The focus on monitoring and evaluation remains under the PASDEP with an increasing emphasis on evaluation and a recognition of areas for improvement such as gender analysis, as well as better dissemination of findings to inform policy-makers. We will continue to encourage the Government’s efforts in this area, by emphasising the importance of a comprehensive poverty monitoring system that builds on both quantitative and qualitative sources of information, and that collaborates with a range of actors including CSOs and academia to produce and use such information. We intend to assist the CSA to undertake the 2007 census.

How will the UK deliver its assistance?

90. We will deliver our assistance to reflect the desires of both the Government of Ethiopia and the UK for predictability, a reduction in transaction costs, and strong coordination between donors leading to improved aid effectiveness. Complete predictability, however, depends on a conducive poverty policy and governance environment within which to operate. We will also, therefore, ensure that we can act flexibly, responding with alternative means of support should it become necessary, while seeking always to maintain aid levels. In the medium term we intend to focus around five major aid modalities.
91. First, the Protection of Basic Services grant. PBS was introduced following the suspension of direct budget support by all donors in 2005. PBS resources will be added to the transfers made to regional governments, which are used to finance the delivery of basic services in the education, health, water, roads and agriculture sectors. Funds will flow through Government channels – essential to achieve national coverage. The grant will include a strong focus on developing Government accountability to its citizens. We will aim to build on the PBS with a view to an eventual return to direct budget support.

92. Second, the comprehensive five-year Public Sector Capacity Building Programme (PSCAP) launched by the Government in 2004. We will provide finance, through joint donor funding mechanisms, for activities designed to strengthen the Government's capacity to provide basic services effectively and impartially. We will also provide strategic, demand-driven technical assistance for core areas of civil service reform.
93. Third, the Productive Safety Nets Programme, which allows DFID and other donors to provide continued help for up to 8 million people over five years to purchase food and obtain access to basic services. The Productive Safety Nets Programme is also having an impact on people's ability to access services in rural areas and is a stimulation to rural growth.
94. Fourth, DFID will respond to the major MDG imperative of improving access to water and sanitation, and other areas related to the procurement of essential infrastructure. As far as possible we will combine our resources for infrastructure with other donors' programmes, particularly those of the World Bank, AFDB and EC.
95. Fifth, we will use pooled fund mechanisms under the DAG (see box) to support interventions in other areas such as governance and humanitarian responses and for civil society, education and health. We will seek to share UK experience and expertise within such coordinated frameworks.

Development Assistance Group Pooled Fund Activities

A feature of donor harmonisation in Ethiopia is the use of pooled resources under the auspices of the Development Assistance Group (DAG). DAG members channel finance through the DAG Pooled Fund to finance a range of technical cooperation and harmonisation activities in support of the PASDEP. The Pooled Fund is managed and administered by UNDP on the behalf of the contributing DAG members. It has been operating for four years.

Recent activities financed by the DAG Pooled Fund have been:

- monitoring and evaluation activities which concentrated on building the Government's capacity to collect and analyse data for monitoring poverty and progress towards the Millennium Development Goals;
- support for the involvement of civil society organisations in initiatives such as the Participatory Poverty Assessment, the Citizens Report Card, and Older People's Monitoring Project;
- assistance in the preparation of the PASDEP, including a review of the SDPRP, preparation of the DAG draft policy matrix, and consultations on the draft PASDEP;
- preparation of a draft declaration as follow-up to the Paris Declaration on Harmonisation Alignment and Aid Effectiveness;
- help for the education sector in preparing its annual review, a national strategy on girls education, research on a university strategy, technical assistance for developing financial manuals and assessing textbook availability;
- help for private sector development and trade through the Government's Integrated Institutional and Export Development Programme, and through strategic studies designed to increase Ethiopia's exports and improve its trade development programmes;
- the contracting of a governance adviser and the development of a joint governance strategy.

Possible scenarios

96. DFID's development relationship with partner governments is based upon:

- commitment to and progress on poverty reduction and the MDGs;
- respecting human rights and other international obligations;
- strengthening financial management and accountability.

The provision of support from DFID is conditional upon progress in each of these areas. A violation of any of these commitments might lead to aid being interrupted, reduced, suspended or delivered in a different way.

97. The Government of Ethiopia has a demonstrable commitment to poverty reduction, as set out in Part I – Poverty Context. Ethiopia's fiduciary controls compare well with other African countries and the incidence of corruption is low.

98. DFID suspended its programme of direct budget support in 2005. The Protection of Basic Services grant which replaced it has been designed for a weaker governance environment. It both reduces the Government's discretion over the use of the funds and makes the funds conditional upon improved accountability to citizens.

99. Three scenarios for future level of assistance can be considered:

- *a low scenario*, where the Government of Ethiopia demonstrates a weak commitment towards respect for human rights, where macro-economic management deteriorates, fiduciary standards decline or major conflict breaks out. In this case DFID's programme would decline or, at best, remain at its current level;
- *a middle scenario*, where the Government of Ethiopia demonstrates its continuing commitment to poverty reduction, where policies on growth, fiduciary controls and accountability are satisfactory and where there is some progress on the governance agenda, but insufficient to provide complete confidence for direct budget support to be resumed predictably over the medium-term. In this case, DFID would scale-up to support PASDEP possibly by as much as doubling the value of its assistance by 2010-11;
- *a high scenario*, where progress in all three areas ie, commitment to poverty reduction, human rights and fiduciary controls, is such that DFID would have confidence to return to direct budget support, and provide it predictably over the medium-term. This would allow DFID to scale-up its assistance even more significantly.

List of acronyms

ADLI	Agricultural Development-Led Industrialisation
AFDB	African Development Bank
ART	Anti retro viral treatment
CAP	Country Assistance Plan
CIDA	Canadian International Development Agency
CSA	Central Statistical Agency
CSO	Civil Society Organisation
DAG	Development Assistance Group
DBS	Direct Budget Support
EC	European Commission
EPRDF	Ethiopian Peoples Revolutionary Democratic Party
GDP	Gross Domestic Product
GoE	Government of Ethiopia
HMG	Her Majesty's Government
JBAR	Joint Budget and Aid Review
MDG	Millennium Development Goal
MoFED	Ministry of Finance and Economic Development
NGO	Non-Governmental Organisation
ODA	Official Development Assistance
OVC	Orphans and Vulnerable Children
PASDEP	Plan for Accelerated and Sustained Development to End Poverty
PBS	Protection of Basic Services
PEPFAR	President's emergency plan for AIDS relief
PER	Public Expenditure Review
PRSP	Poverty Reduction Strategy Paper
PSCAP	Public Sector Capacity-Building Programme
PSNP	Productive Safety Nets Programme
OCHA	Office for the Coordination of Humanitarian Affairs
SDPRP	Sustainable Development and Poverty Reduction Plan
UNDAF	United Nations Development Assistance Framework
UNECA	United Nations Economic Commission for Africa
USAID	United States Agency for International Development
VFM	value for money
WB	World Bank
WB ICAS	World Bank Interim Country Assistance Strategy
WFP	World Food Programme