Souring income and wealth Inequality in Ethiopia[1]

Introduction

There is a disconnect between the popular perception about inequality in Ethiopia and inequality based on quantitative measures. Ethiopians, resident in the country and those visiting there, speak of the widening living conditions of the “haves” and the “have nots”[2]. Indeed, in a country where disparities were compressed by design between the mid-1970s and the early 1990s, the gated residential homes and gated communities of Addis and other major towns, the furniture and fixtures and the fancy cars portray the gap. On the other side, measures based on the Gini coefficient present Ethiopia as the most equal country in Sub-Saharan Africa. This paper sheds light on these differences and provides an insight on the historical and underlying factors for the situation that pertains now. It then shares the author’s views on some statistical and policy issues.

A Brief Review of Money-Metric Measures

The literature on poverty and inequality in Ethiopia is fast increasing. This paper presents a review of only a few papers – some recent and some a bit out-of-date. The World Bank, in its recent poverty assessment reports that “Ethiopia is one of the most equal countries in the world as a result of a very equal consumption distribution in rural areas. In comparison to other African countries, Ethiopia has the lowest inequality as measured by the Gini coefficient[3]. Ethiopia’s Gini coefficient has consistently remained below 30% while other countries have Gini coefficients around 40%. The Gini for rural Ethiopia is particularly low at 27%, and given that the majority of the population is rural this contributes to a low national Gini. Urban Ethiopia has consistently higher inequality than rural areas, across measures and across time, but in comparison to other countries it is still quite low at 35%. In urban areas, all measures of inequality show a substantial increase in inequality from 1996 to 2005 and a substantial reduction in urban inequality from 2005 to 2011.”[4] Similarly, the recent human development report issued by UNDP, referring to Government of Ethiopia sources as well individual authorities, presents a leveling-off in inequality, particularly in urban areas. It reports that “Between 2004/05 and 2010/11, income (consumption) inequality measured by the Gini

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[2] This view is reflected in Solomon Gebre Selassie, Ethiopia’s Growth: Real or Deceptive?,http://www.tesfanews.net/ethiopias-growth-real-or-deceptive/, November 27, 2014; and also The Growing Inequality in Ethiopia, http://abbaymedia.com/2012/12/04/the-growing-inequality-in-ethiopia-by-solomon-gebre-selassie/

[3] Gini coefficient index is a summary statistic that measures the dispersion of incomes or consumption or wealth on a scale of zero (everyone has exactly the same income) to 1 (one person has all the income).

[4] The World Bank, Ethiopia: Poverty Assessment, Poverty Global Practice Africa Region, January 2015

Coefficient has shown a slight decline from 0.3 in 2004/05 to 0.298 in 2010/11 (MoFED, 2013b). Inequality as measured by the coefficient declined in urban areas in this period from 0.44 to 0.37, while rural inequality remained broadly unchanged, at around 0.26..."[5]

Writing along the same lines in 2008, Alemayehu et al. report a more nuanced finding. "In the context of Ethiopia, the evidence on the state and path of inequality over the decade obtained from the national household income and consumption surveys, as well as the panel data, indicate that it has been clearly rising in urban areas, and remained more or less at its initial level in rural areas though it exhibited considerable variation across time according to the panel data."[6] In a later paper, Alemayehu and Addis state that the inequality is higher if the Panel data gathered by Addis Ababa University is used.

In their study of distribution and growth, Christiaensen, Demery and Stefano provide Gini Coefficients for the 1990s for several sub-Saharan African countries based on consumption data. For Ethiopia, they report Gini coefficient of 0.43 in 1994 and 0.42 in 1997 for rural areas, and 0.44 in 1994 and 0.48 in 1997 for urban areas.[7]

To summarise, three points are evident from the above consumption based Gini measures. First, Ethiopia is a more equal society compared to many Sub-Sahara African countries. Second, inequality has subsided nation-wide. Third, while rural inequality has remained low and stable, urban inequality has declined in recent years.

A Critical Analyses of the Money-Metric Measures

As pointed out in all the four studies cited above, the Gini coefficients are estimated on the bases of consumption expenditures. For these measures to be much more meaningful and to reconcile the popular view and the Gini measures, they must be supplemented by inequalities of income and wealth. The literature on Gini-based inequality using consumption, income and wealth is rich particularly for developed countries. Those studies invariably indicate that wealth inequalities exceed income inequalities by much and income inequalities far exceed consumption

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[5] UNDP, Accelerating Inclusive Growth for Sustainable Human Development in Ethiopia, Ethiopia: National Human Development Report – 2014, Addis Ababa, Ethiopia

[6] Alemayehu Geda, Abebe Shimeles and John Weeks, Growth, poverty and inequality in Ethiopia: Which way for pro-poor growth?, Journal of International Development, Volume 21, Issue 7, October 2009 and Alemayehu Geda and Addis Yimer, Growth, poverty and inequality in Ethiopia: 2000-2013: A Macroeconomic Appraisal, Department of Economics, Addis Ababa University, May 2014

[7] Christiaensen, Luc; Demery, Lionel; Paternostro, Stefano. 2002. Growth, Distribution, and Poverty in Africa : Messages from the 1990s. World Bank, Washington, D.C.. © World Bank. https://openknowledge.worldbank.org/handle/10986/14819 ; re-issued in THE World Band Economic Review, VOL.17, NO.3 317–347, The World Bank, 2003

inequalities.[8] The main cause of the differences in consumption and income inequality is the differences in the size and significance of individual and household savings. There have not been nation-wide income surveys in Ethiopia known to this author or in any publicly available source. To that extent income at the individual and household level is unknown partly due to the difficulties in capturing income using surveys. The only sources available are per capita GDP at the national level. No attempt has so far been made to provide a dis-aggregation by factor incomes (wages and salaries, rent, interest and profit) or rural and urban portions.[9]

In general however it will not be far from reality if we assume that consumption and income are equal at least in the rural areas. In any case, in a country such as Ethiopia, where subsistence farming is the dominant economic activity particularly in rural areas, income and consumption may not differ much. Even during severe negative shocks, consumption is likely to stay positive through different household survival strategies. It is also well known that surplus-growing households purchase and keep chicken, goats or cows during the good harvest years as their savings and investment which could be used to smooth future consumption and also build more assets.

In urban areas, in addition to significant differences in labor income (due to differences in education, skill, experience, and similar factors), non-labor income tend to be important and widen whatever difference that may exist in labor income. In recent years, income from rental property as well as from investment in real and financial assets has increased fast. Thus, the disparity in the income- and consumption-based Gini inequality in urban areas is likely to be larger than for rural areas. There is anecdotal evidence to this effect. Let us look into labor and non-labor income a bit in detail.

Labor Income: Wages and salaries are important as an incentive to elicit higher productivity. However, they are likely to cause legitimate inequality since people differ in their academic qualification, skills, experience and other labor attributes. In the case of Ethiopia, comparing wages and salaries in a few ministries and parastatals could be instructive about such disparities. For instance, in September 2014, for the Ministry of Transport and Communication, the ratio of the base salary for the highest step and lowest step was 15.3. It means, at the base level (starting

[8] Drew DeSilver, The many ways to measure economic inequality, http://www.pewresearch.org/fact-tank/2013/12/18/the-many-ways-to-measure-economic-inequality/ December 18, 2013; David S. Johnson, Timothy M. Smeeding, and Barbara Boyle Torrey, Economic inequality through the prisms of income and consumption, http://www.bls.gov/opub/mlr/2005/04/art2full.pdf, Monthly Labor Review, April 2005; Eric Bonsang, Sergio Perelman, and Karel Van den Bosch, 6.5 Income, Wealth and Consumption Inequality, http://www.share-project.org/uploads/tx_share publications/CH_6.5.pdf

[9] Asefa tried to disaggregate GDP into urban and rural components and estimated per capita GDPs which show some interesting findings. Asefa Belachew, Disparities in Rural and Urban Incomes in Ethiopia: 1981-2011, http://www.aigaforum.com/articles/Ethiopia-Rural-Urban.pdf, December 14, 2014 also found at http://www.ethiomedia.com/11notes/disparities_in_rural_and_urban_incomes_in_ethiopia.pdf

salary). The salary scale for the highest scale was over 15 times higher than the lowest scale. The same ratio for the ceiling salary was 10.9.[10] The corresponding ratios for the Ethiopian Roads Authority, a parastatal, were 16.4 and 14.3 for the starting and ceiling salaries, respectively. These indicate that for individuals who worked in Ministries or parastatals, wages of the highest paid were over 10 times higher than the lowest paid workers.

More light could be shed on labor income disparities by reviewing the recent surveys on urban employment-unemployment (with nation-wide coverage) and the Addis Ababa unemployment survey which provide data on earnings.[11] According to the national Survey, persons in "paid employment" are typically remunerated by wages and salaries, but may be paid commission from sales, piece work, bonuses or in kind payments such as food, housing or clothing. In the national survey, earnings for paid employees refer to gross remuneration, including bonus, overtime, allowances and other benefits that are obtained only from the main job. The disparity between the class means for the highest earners and lowest earners is about 17 times. The distribution has a Gini coefficient of 0.78 which shows high level of earnings inequality – more than twice higher than the Gini for consumption expenditure. The Addis Ababa survey, in a like manner, defines earnings for paid employees as the gross remuneration including bonus, overtime, allowances and other benefits that are obtained only from the main job.[12] The ratio of the mean earnings for the highest class is 400 times higher than the mean of the lowest class. The corresponding Gini coefficient is 0.86, higher than the Gini for the nation-wide earnings survey and much higher than the consumption expenditure Gini coefficient. This is consistent with the literature referred to above. The earnings used here are "…only from the main job". To the extent that some people have more than one job, the earnings reported could under estimate the actual labor earnings from the multitude of jobs.

Rental Income: The major cause of inequality is however non-labor income – rent, dividends, interest and profit. Cumulatively, these cause disparities not only in income but in wealth as well. There is some data on land (housing) tenure status from the 2007 Population and Housing survey. The survey shows that there were 2.9 million housing units in urban areas in 2007[13]. Of

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[10] Based on data from http://www.mywage.org/ethiopia/home/salary/minimum-wages

[11] Central Statistical Agency, Federal Democratic Republic of Ethiopia, Statistical Report on the 2014 Urban Employment-Unemployment Survey, Statistical Bulletin, Addis Ababa October 2014

[12] Central Statistical Agency in collaboration with Addis Ababa Labour and Social Affairs Bureau, Federal Democratic Republic of Ethiopia, Statistical Report on the 2013 Employment Survey of Addis Ababa, Addis Ababa, May 2014

[13] A housing unit is defined as a separate and independent place of abode, either intended for habitation or not intended for habitation but occupied as a living quarter by a household at the time of the census. A housing unit may at the time of the census be occupied by one or more households or may be used partly for living and partly for establishment. Residential Housing Unit is defined as a housing unit used only for habitation at the time of the census. Partial Residential Housing Unit is defined as a housing unit used for habitation and establishment at the time of the census.

these, 39 percent were owner occupied units, while the remaining were rented unit from Kebele, housing (real estate) agencies, private households, and other organizations. Those rented from private households numbered 1.17 million units and accounted for 40.3 percent of the housing units.[14] In Addis Ababa, there were 0.69 million housing units, of which 32.6 percent were owner occupied units, while the remaining two-third were rental property. With 0.22 million units, privately owned rental property, accounted for 35.3 percent of the housing units. Considering that there were 2.9 million housing units (and perhaps the same number of owners) and 11.9 million urban residents, only 24 percent owned a housing unit, the remaining 9 million people (or about 75 percent) did not own a housing unit. Since one person could own more than one housing unit, the percentage of people who own a housing unit is likely to be lower than 25 percent. Essentially, more than three quarters of urban residents did not own anything. On the other side, the 1.2 million privately-owned and rented-out units generate rental income to the landlords. Addis Ababa with a population of 2.74 million people, according to the Survey, and 628, 986 housing units, 23 percent of the population owned housing units, thereby, close to 80 percent did not own their own housing unit. Again here, since one person could own more than one housing unit, over 80 percent of its residents did not own any housing units.

Based on these ownership statistics, it is obvious that real estate ownership and rental income have been an important store of wealth and source of income, respectively. This is consistent with the observation that many households in urban areas depend on rental income, and very many complain about the shortages of housing and the exorbitant rent.

The Central Statistical Agency, in its 2010/11 survey reports expenditures on house rental and rentals as a source of income by expenditure quintile.[15] According to data in Table 29, rent accounted for about 8 percent to 13 percent of per capita consumption expenditure, the proportion increasing progressively with each higher quintile, particularly after the 3rd quintile. Table 33 provides data on the sources of income to cover the expenditure, one of which is house rent income (imputed or actual). The share of consumption expenditure paid for through rental income steadily declines from 10 percent to 6 percent. This shows the more diversified portfolio of the upper quintile and its less dependence on rental income. In any case, to the extent that rental income is not used to cover present consumption expenditure, the data are not a complete measure of rental income. The boom in construction of high rise residential or commercial buildings is so obvious and it generates income to the owners[16]. Ownership of these buildings is

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[14] Ethiopia Population Census Commission, 2007 Population and Housing Census, April 2012

[15] Central Statistical Agency, Federal Democratic Republic of Ethiopia, Household Consumption and Expenditure (HCE) Survey 2010/11: Analytical Report, Statistical Bulletin 563, October 2012 Addis Ababa

[16] The Central Statistical Authority shows that 373, 3947, and 534 building permits (excluding those issued by District (*Kifle Ketema*) had been issued in 2005/6, 2006/7 and 2007/8, respectively, by Addis Ababa City Council to build 1-14 plus storey buildings. *Kifle Ketema* issued permits for lower level buildings including vila-type residential and commercial buildings. There is no data on these constructions. Central Statistical Agency, Annual Statistical Abstract: Ethiopia, No year. Copy is found here:

perhaps the most contentious and politically charged issues in the country as it is believed most of the land may have been illegally acquired by the current property owners[17].

Interest, Dividend and Profit Income: Inequality in labor and rental income is exacerbated by inequality in income from investment – investment in financial instruments or in the real sector (agriculture, industry, and services). Data shortage on these sources of income is severe, but some order of magnitude could be gleaned on the size of income garnered through these sources by examining a few of the financial reports of the private commercial banks. By the end of 2014, there were 16 private commercial banks.[18] Commercial banks, both public and private, are required to get their finances audited annually and make the report public. According to the report for 2014, Abyssinia Bank, for instance, made a gross profit of 351.49 million birr. With 1670 shareholders, each shareholder earned 210,473 birr in gross. If one makes 50 percent allowance for taxes, a shareholder netted over 105,000 birr. Abyssinia's gross earnings per share amounted to 9.52 birr or 38 percent compared to the share face value. Other Banks provide detailed financial statement but data on the number of shareholders is lacking.[19] For the other banks, gross earnings per share ranged from about 20 percent for Addis Bank to 47.7 percent for Wegagen.

Distribution of Wealth: While the emphasis above has been in the distribution of the flow of income from various types of assets (labor payments, real estate and financial assets), some discussion has been made, although cursory, on the distribution of stocks (assets) such as real estate ownership (or renter) status as well as financial assets.

Here, the study sheds light on the ownership of wealth based on data from the Demographic and Health Surveys, more in particular the survey of 2011.[20] The survey provides data on household ownership of durable goods and other possessions such as durable consumer goods (household effects), means of transportation. agricultural land and farm animals by wealth quintile to indicate a household's social and economic well-being.[21] The data show that in urban areas 87.6

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http://www.csa.gov.et/index.php/component/content/article/14-survey-reports/123-latest-national-statistics-abstract

[17] The Federal Ethics and Anti-Corruption Commission of Ethiopia reports to have recovered over 730 thousand square meters of urban land, 3 houses and 4 buildings in its 2014/15 fiscal year. This is the tip of the iceberg and symptomatic of how pervasive the problem has been in recent years. Refer to http://www.feac.gov.et/index.php/restrained-and-confiscated-assets-en
[18] http://www.nbe.gov.et/financial/banks.html.

[19] The only other bank that provides the number of shareholders is Abay Bank but a complete financial statement is lacking.

[20] Central Statistical Agency [Ethiopia] and ICF International. 2012. Ethiopia Demographic and Health Survey 2011. Addis Ababa, Ethiopia and Calverton, Maryland, USA: Central Statistical Agency and ICF International.

[21] The wealth components used are: Household effects or consumer durable goods (radio, television, mobile telephone, non-mobile telephone, refrigerator); means of transportation (bicycle, animal drawn cart, motorcycle/scooter, car/truck); ownership of agricultural land; and

percent of these assets were held by the top quintile (top 20 percent of households). In Addis Ababa alone, the top 20 percent owned 96.8 percent of these assets. The rural distribution appears more even except that the top 20 percent garners only 5.1 percent of the assets. The Gini coefficient for urban areas, Addis Ababa and the rural areas is surprisingly equal and reaches 0.60 showing pervasive inequality.

To summarize the section, while the distribution of consumption expenditure is equitable, the same cannot be said about income and wealth. The Gini for labor income is anywhere between 0.7 and 0.9. The inequity is compounded when income from rental property and investment income are added. Indeed, the evidence on the distribution of the latter sources is not as concrete as data are lacking. But, those who reside in their own home avoid paying rent and are likely to be the owners of the rented property and earn additional income. Those who rent-in their housing face additional burden. Investment income, as shown with data from the banking sector, is likely to exacerbate the inequity. There is good reason to expect that recent policy measures have favored the top 5 to 10 percent of the population. The story to be told is that indeed policies have succeeded in reducing poverty and maintaining an equitable consumption distribution, primarily due to Ethiopia's subsistence economy, the growth in the modern sector however has favored skilled labor and property owners.

Historical Background and Underlying Factors

Three social, economic and political regimes pervaded the Ethiopian scene since the Second World War. During the Imperial regime that ended in mid-1974, Ethiopia had adopted a mixed economic system. Except a few public enterprises, most of the businesses were owned by private individuals and the nascent corporate sector. The economy was primarily agricultural with smallholder cultivation dominating the scene despite a few commercial farms emerging in the Awash valley. Resource allocation was primarily market-based.

During this period, inequality was primarily determined by access to cultivable land. On the average, slightly over 33 percent of the land was owned by absentee land lords who occupied about 25 percent of the land. In some provinces, absentee ownership reached close to 50 percent. As a result, a large proportion of cultivated holdings were very small. For instance, in Gemu Goffa and Sidama provinces, 73 percent of cultivated holdings were less than half a hectar. Although a more communal ownership system existed in northern Ethiopia, 55-70 percent of cultivated holdings in Tigray, Begemder, and Gojjam were also less than half a hectar. These phenomena caused major disparities in wealth and income[22]. When coupled with adverse movements in the weather condition, many suffered from starvation due to loss of entitlement even when there was a national surplus.

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ownership of farm animals (milk cows, oxen, bulls, horses, donkeys, mules, camels, goats, sheep and chicken).

[22] The figures are computed based on data from the Ministry of Land Reform and Administration, The Major Features of the Prevailing Land Tenure System in Ethiopia, draft Memo, October 1971. Quoted in Commercial Bank of Ethiopia, Market Report, January – February, 1974.

These were among the factors that precipitated the 1974 revolution that ushered in the *Derg* regime. *Derg* was socialist in its orientation and in its approaches to social, economic and political life in the country[23]. It February 1974, it nationalized rural land and quickly followed it by nationalization of private businesses, urban land and houses in excess of one home. These actions removed the payment of rent to the landlord. In urban areas, where wages and salaries were the main form of income, they were compressed. Practically no room was left for the market system to allocate goods and factors. As a result, a more equal but, on average, a poorer state emerged.

The political and economic situation in the country in the late 1980s brought about the third regime. The distributional outcomes during the EPRDF regime have been outlined above. In terms of policies, it shares some aspects of both, and benefitted significantly from their legacies. Like the Imperial regime, market forces, although at times unpredictable, play a major role in resource allocation, and ownership of assets, except in land, is more or less private. Many private businesses have opened up and the environment is relatively more conducive for investment. Wages and salaries have been decompressed and reflect skill scarcities. Together with the large infrastructural investment, the situation has allowed fast GDP growth. On the other side, like the *Derg*, it shuns to privatize land and vest title in the farmer[24]. Although it is a controversial issue, it has assured a plot of land for farmers to ensure their sustenance. This has allowed to maintain consumption above the poverty line and level the distribution.

Conclusions and Suggestions

In the foregoing, we have analyzed the disparities in consumption expenditure, income and wealth. While there is unanimity that inequality in consumption expenditure is low and stable, particularly in rural areas, the same cannot be said about income and wealth inequality. The existing anecdotal evidence shows that income and wealth inequality has soared.

In a mixed economy where markets determine prices, it is unavoidable to see disparities in income as scarce resources command higher prices. To the extent that professionals receive skill premiums and legitimate investors garner higher returns, these could be inevitable prices for growth. Of course, the government should see to it that these professionals are assessed a fair tax and pay their taxes like everybody else. The biggest challenge is if/when assets are acquired through illegal means. Such a situation causes social disharmony and exacerbate whatever tensions that may exist.

The Ethiopian government has succeeded in unleashing a major spurt in GDP growth, lowering the level of poverty and maintaining a low level of consumption disparity. In essence, GDP grew

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[23] Bereket Kebede, Land Reform, Distribution of Land and Institutions in Rural Ethiopia: Analysis of Inequality with Dirty Data, School of Development Studies, University of East Anglia and Centre for the Study of African Economies, University of Oxford, Working Paper Series (WPS/2006-05)

[24] Teshome Temesgen Tilahun, The Chronological Trends of Rural Land Tenure Systems in Ethiopia since the Military Regime (1975), memo, Gonder University, December 2009

but GDP destined to the higher echelon grew at a much faster rate. Thereby it ended up exacerbating income and wealth inequalities.

A considerable amount of effort has been exerted to collect data on the bases of which the health of the economy could be assessed. But the credibility of these data is often questionable. As Alemayehu and Addis state " … Thus, there is no reason to make data on national accounts, such as GDP growth, political. Second, it is essential that data generating institutions, such as the CSA, MOFED and NBE, be staffed by professionals and their research methods and data be subject to review by an independent peer-review process on a regular basis. They need also to be autonomous and transparent, and, to the extent possible, insulated from politics and pressure from the government." A similar sentiment is expressed by the IMF as well.[25] This author fully subscribes to their views and encourages the Authorities to look into the matter seriously and take appropriate action. It also wants to bring to their attention to start to provide GDP estimates using the income approach (wages and salaries, profit, interest and rental income).

As alluded to above, data are lacking on the distribution of income from rental property and investment. These however are available with the relevant government Authorities, such as the Ethiopian Revenues and Customs Agency. These arms of government are encouraged to issue grouped data from their annual tax returns. Such data would include at least four columns containing distribution by tax brackets (or some other income classes) separately for each tax Schedule, the number of tax payers in each bracket, the total income and amount of tax collected.

The Ethiopian Law allows for the taxation of capital gains. The Authorities may consider introducing inheritance (estate) tax to mobilize additional resources for social and economic investment. This may also help to correct some of the inequalities in income and wealth.

The Federal Ethics and Anti-Corruption Commission reports to have assembled data on asset ownership of over 30,000 Government officials including Members of Parliament at the Federal and Region level. It would be useful to make these data publicly available for the public to add to the list if there are some assets missed inadvertently. This would make the transparency and accountability of the Authorities stronger. It would also be useful that the real estate registry, for instance at the Addis Ababa City Council, is made public.

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[25] IMF, The Federal Democratic Republic of Ethiopia: Staff Report for the 2014 Article IV Consultation, October 2014, p.27, para. 56.