

Mekelle, Ethiopia

Potential opportunities for investors
June 2010

KPMG INTERNATIONAL



Terms of reference

This report has been prepared by KPMG in Russia, a partnership registered in Russia and a member firm of KPMG International, a Swiss cooperative. The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as at the date it is received or that it will continue to be accurate in the future.

In preparing this document we have relied upon and assumed, without independent verification, the accuracy and completeness of various sources of information, including public sources.

Details of the sources we have used are given in our report. KPMG in Russia accepts no responsibility or liability to any party in connection with such information or views.

Our core fieldwork and research were performed between September 2009 and December 2009. We have not undertaken to update our report for events or circumstances arising after that date.

Appropriate professional advice should be sought to undertake a more specific examination of the particular circumstances applicable to a potential investor. The contact details of KPMG professionals who can assist in this regard are given at the end of this report.

Acknowledgments

KPMG in Russia would like to thank the Millennium Cities Initiative (MCI) for the opportunity to prepare this report to support its valuable project. We would also like to thank the numerous enterprises and organisations which participated and acknowledge their contribution to the preparation of this report (please see Appendix 1 for more details).

Foreword

As part of KPMG's Global Development Initiative, which focuses KPMG member firms' skills and resources on achieving the United Nations' Millennium Development Goals (MDGs), KPMG in Russia was asked by the Millennium Cities Initiative (MCI) to undertake this report in relation to potential investment opportunities in Mekelle, Ethiopia.

The MCI is an urban counterpart to the Millennium Villages Project and was set up in association with the UN Millennium Project by the Earth Institute at Columbia University. The initiative is focused on helping a number of cities across sub-Saharan Africa to achieve the MDGs through economic development. This report, which explores the investment potential in Mekelle, is one of several being produced by KPMG's Transaction Services practice.

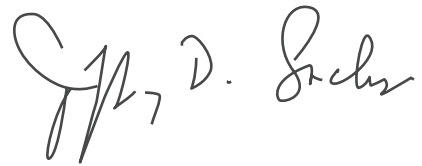
In our opinion, this report is an excellent example of how KPMG member firms and their people are committed to making a difference to the people in sub-Saharan Africa.

Mekelle, the commercial hub in the north of Ethiopia, is a good choice for investment. The area is endowed with natural resources ranging from favourable climatic conditions for honey production to untapped mineral resources. Access to export markets gives Mekelle an advantage over other cities in Ethiopia. Additionally, the expected rapid economic growth and highly supportive regional government has created an investor-friendly environment with immense potential for rapid growth in new investments.

To this extent, we hope that this work will lead to the sustainable eradication of poverty and secure the future of many hundreds of people through work and enterprise.



Lord Hastings of Scarisbrick CBE;
KPMG, International Global Head of
Citizenship and Diversity



Professor Jeffrey D. Sachs,
Director of The Earth Institute at
Columbia University



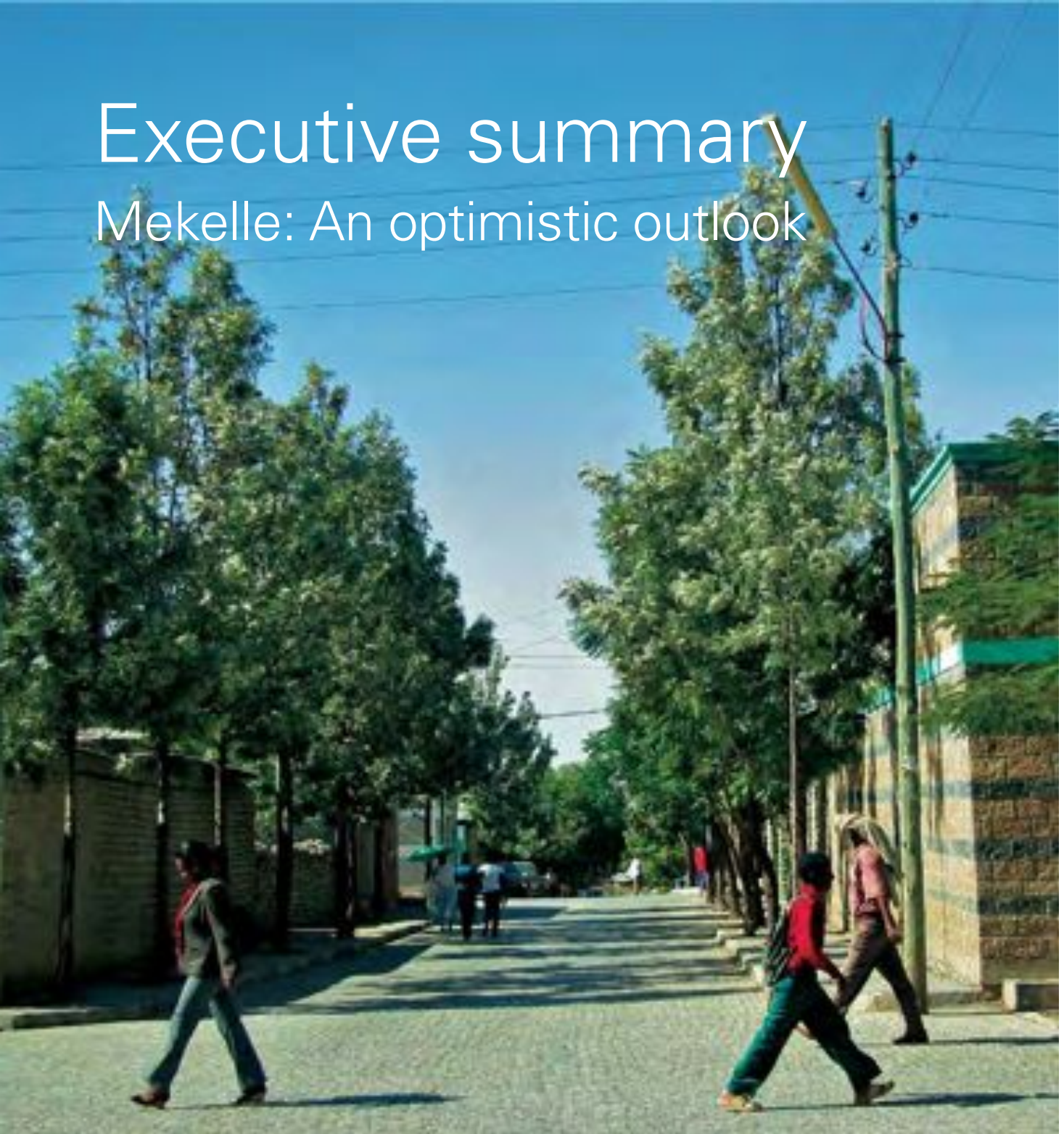
The Millennium Cities Initiative (MCI) is a project of the Earth Institute at Columbia University. Launched by the Institute's Director, Professor Jeffrey D. Sachs in 2006. The MCI seeks to assist, through research and policy analysis, selected mid-sized cities across sub-Saharan Africa to achieve the Millennium Development Goals. Guided by its Co-directors, Dr. Susan Blaustein and Dr. Karl P. Sauvant, the MCI, more specifically, helps the cities involved to arrive at integrated City Development Strategies. Part of this effort is to demonstrate that more investment, including foreign direct investment, can be attracted to these cities, with the resulting employment and economic growth effects.

The staff responsible for working with KPMG Russia and KPMG International on this report were Karl P. Sauvant, Co-director of the MCI and Executive Director of the Vale Columbia Center on Sustainable International Investment; and Jörg Simon, Senior Investment Advisor of the MCI.

<http://mci.ei.columbia.edu/>

Executive summary

Mekelle: An optimistic outlook



The Mekelle region presents attractive opportunities for export-oriented investors.

The improving business climate in Ethiopia provides attractive opportunities for investors capable of bringing financing, technologies and process management as well as creating employment.

Ethiopia has showed impressive economic growth and investment inflow in recent years, driven by political stability, the low cost environment and supportive state policies.

The government has established a particularly investor-friendly environment for export-oriented industries through specific initiatives and administrative procedures, such as exemptions from profit tax for two to five years, carrying forward of losses and duty free import of capital goods for up to 15 percent of the value of capital goods imported for investment purposes.

Financing, a qualified labour force and infrastructure remain the key constraints faced by business in Ethiopia. However, these constraints are partly manageable in the short term by bringing own financing, technology and process management to Ethiopia in order to transfer knowledge processes to the local workforce. Infrastructure constraints are not prohibitive in most cases and can be managed through proper site selection.

The Mekelle region is currently one of the most encouraging investment destinations in Ethiopia, driven by the highly supportive regional government, abundant untapped natural resources and good access to export markets.

Due to its proximity to a former military zone, Tigray State where Mekelle is located, has historically underperformed compared to other Ethiopian states in terms of economic growth and inflow of private investments.

However, the military conflict with Eritrea ended in 2000 and is unlikely to be repeated in the future.

Supportive regional government policies, the development of infrastructure and the availability of land make the Mekelle region an attractive investment destination.

Access to the Eritrean sea port may establish an even stronger competitive advantage for Mekelle but no evidence was provided that this port would be accessible in the immediate future.

Power supply standards were significantly improved in 2009.

The Mekelle region presents potentially advantageous possibilities for investors in export-oriented agro-processing, mining and tourism industries.

Favourable agro-climatic conditions, the availability of appropriate land plots and the proximity to export markets provide an attractive opportunity for growing selected varieties of fruit and vegetables for the Middle East and European markets.

The Mekelle region provides a good opportunity to export meat and leather goods, driven by a large, high-quality livestock population.

Abundant mineral resources in the Mekelle region provide attractive opportunities in relation to stones and industrial minerals.

The Mekelle region provides potentially good prospects for producing high-quality honey to supply Sudan, Middle East, US and European markets. The honey supply shortage, currently the key constraint, is likely to be overcome in the mid-term.

The variety of historic and natural sites in Tigray State has attracted a growing number of local and international tourists. The lack of high-standard hotels on major tourist routes creates the potential for investment in quality lodges in the Mekelle region.

Investment opportunities

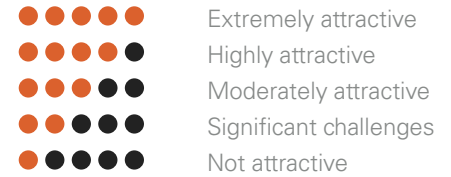
Nine investment opportunities were evaluated for investment purposes against criteria such as domestic and export demand, production and supply, competition pricing and margin profile, and regulatory barriers.

The opportunities are summarised below. Tourism, meat production, honey and leather processing, horticulture and mining were found to be the most attractive for investment, and are examined in greater detail in this report.

Industry	Favourable factors
Tourism	<ul style="list-style-type: none"> Moderate, dry climate Easy access to the most interesting historic, religious and natural beauty sites of Tigray and Afar States Lack of adequate tourist facilities
Meat production	<ul style="list-style-type: none"> Large, good-quality livestock population Special ox breed (Raya) which is more profitable than other breeds due to its bigger size, and more tender and tasty meat
Honey processing	<ul style="list-style-type: none"> Moderate climate favourable for honey production Large bee population Famous high-quality white honey with low moisture content
Leather processing	<ul style="list-style-type: none"> Largest livestock production in Africa Special quality leather — Cabretta and Bati
Horticulture	<ul style="list-style-type: none"> Favourable agro-climatic conditions Availability of appropriate land plots Proximity to export markets
Mining	<ul style="list-style-type: none"> Abundant mineral resources provide attractive opportunities in relation to dimensional stones and industrial minerals
Animal feed	<ul style="list-style-type: none"> Large resource base
Milk processing	<ul style="list-style-type: none"> Large livestock population Favourable climate for high-yield animal breeds
Floriculture	<ul style="list-style-type: none"> Availability of appropriate land plots with suitable water resources Proximity to Europe, one of the largest floriculture markets globally Tigray is one of the Ethiopian states suitable for growing the rare Rose <i>Damascena</i>, due to appropriate climatic conditions and soil composition

Source: Tigray Investment Office, 2009
KPMG in Ethiopia interview programme, 2009

Key



Challenges	Attractiveness
<ul style="list-style-type: none"> Lack of well-trained workforce Insufficient marketing of region Poor image of the North of Ethiopia due to the war with Eritrea Insufficient tourism infrastructure 	●●●●●
<ul style="list-style-type: none"> Instability of live animal supply Meat quality certification required for export Instability of demand in export markets 	●●●●●
<ul style="list-style-type: none"> Honey supply shortage in the short term 	●●●●●
<ul style="list-style-type: none"> Irregularity of supply Quality of raw materials needs to be improved 	●●●●●
<ul style="list-style-type: none"> Poor road and airport infrastructure 	●●●●●
<ul style="list-style-type: none"> Deposits can be difficult to access Quality of roads 	●●●●●
<ul style="list-style-type: none"> Low crop productivity Lack of demand for processed animal feed 	●●●●●
<ul style="list-style-type: none"> Shortage of feed Lack of exotic and crossbred dairy cows High seasonal fluctuations in milk consumption caused by fasting 	●●●●●
<ul style="list-style-type: none"> No operational international airport Road infrastructure is poor for the majority of floriculture land plots around Mekelle The absence of floriculture farms in Tigray State makes small to medium scale flower production a high risk undertaking 	●●●●●

Contents

Introduction to MCI	09
Political climate	10
Investment climate in Ethiopia	11
Economic outlook	12
Investment trends	13
Key inhibitors	15
Mekelle, potential opportunities for investment	16
Introduction to Mekelle	17
Investment climate	18
Infrastructure	21
Select opportunities in Mekelle	24
High quality lodge in the Mekelle environs	25
Meat production for export	32
High quality honey processing for export	36
Processed leather and leather goods for export	40
Out of season fruit grown for export	45
Dimensional stones and industrial minerals	48
Appendices	
KPMG in Ethiopia interview programme	53
Secondary research	54

Introduction to MCI

Aiming at sustainable growth

The Millennium Cities Initiative (MCI) aims to facilitate African countries in reaching the Millennium Development Goals (MDGs) by, among other things, attracting more foreign direct investment.

The initiative is focused on the capitals of the regions where the Millennium Villages Project (MVP) is enabling farmers to transition from subsistence farming to commercial agricultural and non-agricultural activities.

The MCI aims to engender a climate in which investment, especially foreign direct investment, can thrive, thereby creating employment, stimulating enterprise development and fostering economic growth.

As such, the MCI intends to accelerate the attainment of some of the MDGs within selected cities in sub-Saharan Africa.

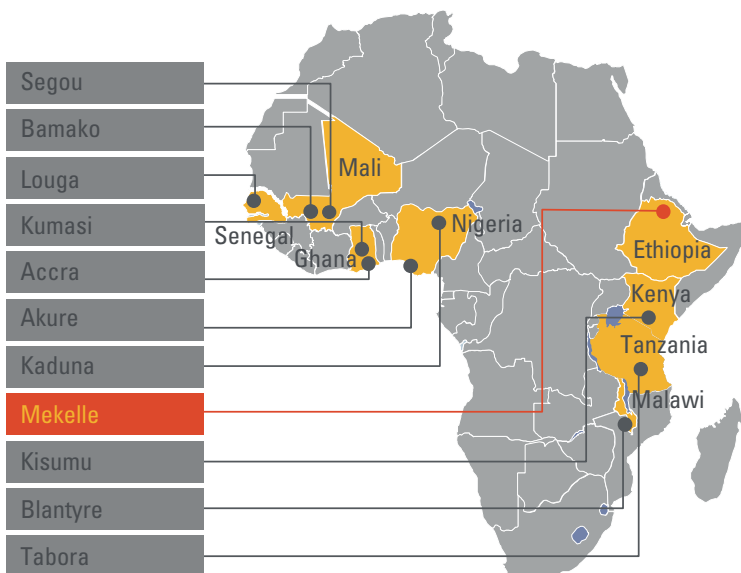
The experience gained in attracting investment and developing business in the Millennium Cities is complementing needs assessments carried out in a wide array of social sectors. As a result of these efforts, the Millennium Cities will be enabled to generate Integrated City Development Strategies that are explicitly predicated on achieving the MDGs.

Korare — the MVP located close to Mekelle — has already made considerable progress in the area of agriculture development. The MVP is exploring dairy collection as an area for increased commercialisation and interaction with urban markets. It is also in the process of instituting a large-scale honey and wax production system across its 11 villages. The focus of the project is to incentivise farmers to consistently improve their yield on agriculture production to generate sustainable income for the village, thereby making it a self-sustaining economic unit.

The following KPMG Investment guides and publications featuring the millennium cities have been produced:

- Investment guide: Kisumu, Kenya
- Investment guide: Kumasi, Ghana
- Working paper: Bamboo bicycles in Kumasi, Ghana
- Investment guide: Ondo state, Nigeria
- Investment guide: Blantyre, Malawi
- Working paper: Sugar in Kisumu, Kenya

The African Millennium Cities



Source: Millennium Cities Initiative Report, October 2009

For these reports and more information on MCI please visit:

www.mci.ei.columbia.edu/

Political climate

Ethiopia is the largest country in East Africa. As a landlocked country, Ethiopia shares boundaries with Eritrea to the north, Kenya to the south, Somalia and Djibouti to the east and Sudan to the west. Its growing population of nearly 74 million (2007) makes it the second most populous country in Africa. The majority of the population (85 percent) is rural and engaged in agricultural production.

Map of Ethiopia with neighbouring countries



Source: Millennium Cities Initiative Report, 2009
Notes: One international airport Bole located in Addis Ababa
No sea ports

Historically, Ethiopia has been isolated politically and culturally from its East African neighbours. This has changed in recent years as the government has committed itself to supporting regional trade and broadening interactions among African countries. Ethiopia is now a member of the Common Market for Eastern and Southern Africa (COMESA) and home to the Africa Union.

Ethiopia is a federal republic, which is ruled by President Girma Woldegiorgis. In 1995, Ethiopia adopted a new constitution that fostered a multi-party democracy and peaceful elections. A two-and-a-half-year border war with Eritrea ended with the signing of a peace treaty on 12 December 2000.

As one of only two countries in Africa that have never been colonised (Liberia being the other), Ethiopia maintains a unique role in Africa's history. It has long been looked to as a source of pan-African culture and leadership. When the Organisation of African Unity (OAU) was established in 1963, Addis Ababa was chosen as its headquarters. Addis Ababa is also home to the United Nations Economic Commission for Africa (ECA) and is a major hub of Non Governmental Organisation activity on the continent.

Investment climate in Ethiopia

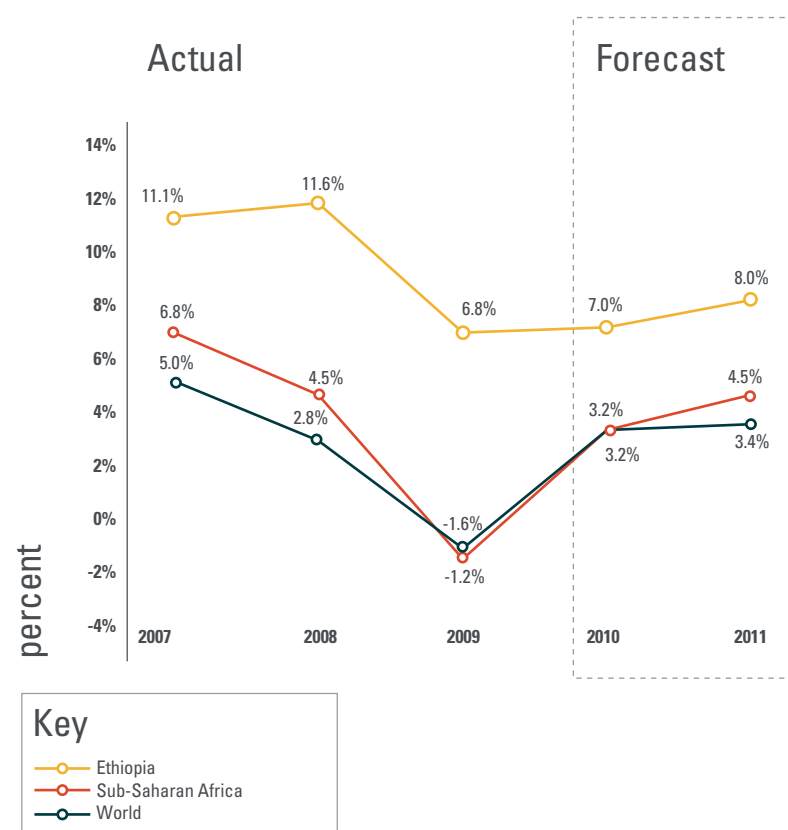
Economic outlook

The improving business climate in Ethiopia provides attractive opportunities for investors capable of bringing own financing, technologies and process management in order to transfer knowledge to the local labour force.

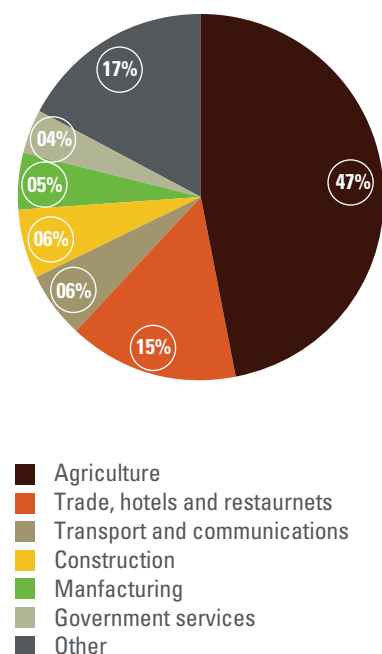
The relative political stability of recent years, cheap labour and supportive state policies have already led to impressive growth in new investments and corresponding economic growth of Ethiopia.

Ethiopian GDP growth significantly outperformed the world average and sub-Saharan Africa's average from 2007 until 2009, and is likely to continue in 2010–2011.

Real GDP growth percentage 2007–2011



GDP distribution by sector 2006–2007



Source: Ethiopia: Economic Structure, Economist Intelligence Unit, 2009

Investment trends

The government leads an investor-friendly environment for export-oriented industries.



Gross capital formation and FDI inflows demonstrated significant growth in 2006 and 2008.

Unlike many other countries in sub-Saharan Africa, Ethiopia now shows relatively low military, criminal and terror risks.

“Ethiopia is a relatively peaceful country. It’s dangerous to go out in the dark in some African countries and you have to order an official car. Here you can pick up a taxi in the night and should not be afraid for life and health.”
An investor from Israel

“Go to a local night club and you will understand everything. It’s a very strong indicator of the criminal situation in the country. Many Europeans visit our discos and they are sure they will be safe.”
Ministry of Industry and Trade

Ethiopia possesses a relatively cheap and educated labour force.

“The labour force is very cheap here. Local people have a proper educational basis and it was not a problem for us to teach them basic skills required for our business.”
Dutch investor in horticulture industry

According to the *Doing business report 2010* by the World Bank, Ethiopia has a strong position in the areas of tax administration and legal practice. This saves investors in Ethiopia significant time and money compared to other countries in sub-Saharan Africa. On average, it takes around 30 percent less time to deal with tax procedures, and the effective tax rate as a percentage of profit in Ethiopia is half that of the sub-Saharan Africa average. The average cost of enforcing contracts is only 15 percent of the claim in Ethiopia, vs. 22–79 percent in comparable countries in Africa.

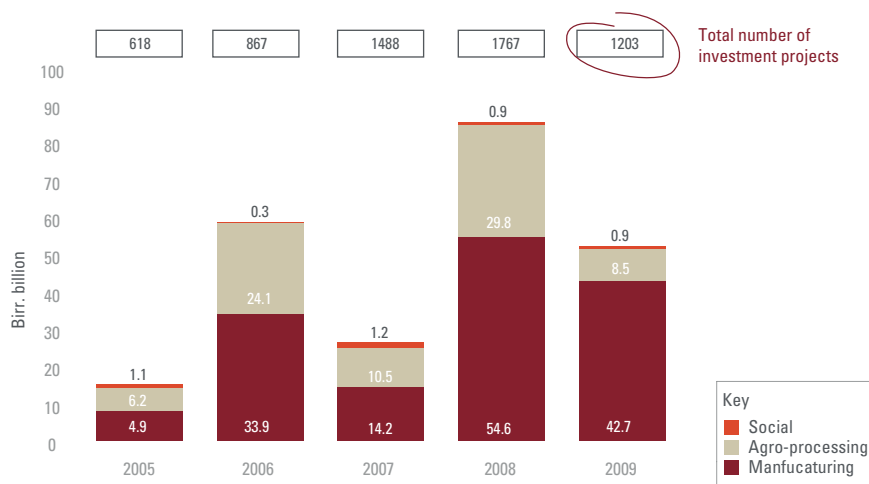
The Ethiopian government takes specific measures to further facilitate new investments. Since it was first adopted in 1992, the Investment Act has been revised several times to remove obstacles to foreign direct investment in Ethiopia.

Privatisation has been ongoing since the Republic's founding in 1995, and the government has sold many mismanaged and poorly performing companies to private investors.

The favourable climate for foreign investment created by the overall economic conditions of the country is further augmented by specific initiatives and administrative procedures to encourage investments. In common with other developing countries, the most important incentives consist of tax concessions. These include:

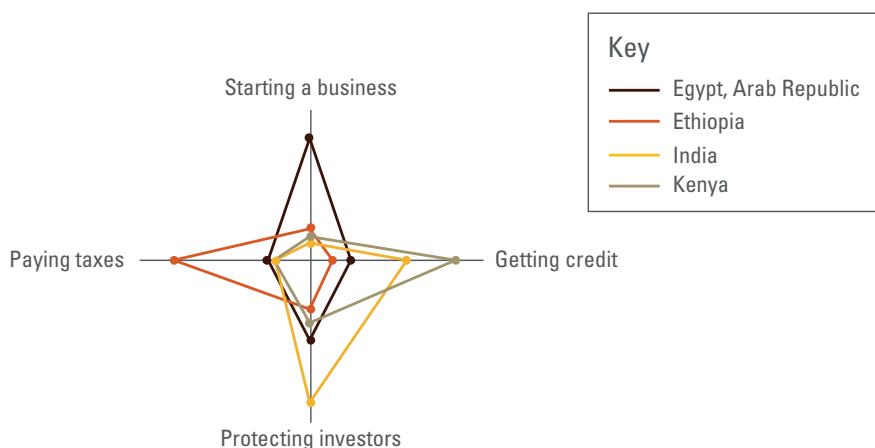
- Exemption from profit tax for a minimum period of two years, and up to five years depending on the type and location of investment, with provision for an additional exemption of two to three years for investment in existing enterprises.
- The carrying forward of losses — an investor who has incurred loss within the period of income tax exemption shall be allowed to carry forward his loss for half of the income tax exemption period after the expiry of such period.
- Duty free import of capital goods — an investor eligible for duty free importation of capital goods pursuant to these regulation shall be given the same privilege for spare parts whose value is not greater than 15 percent of the total value of the capital goods to be imported.

FDI distribution in Ethiopia by sector, 2005–2009



Source: Foreign investment projects, July 92–September 2009, Ethiopian Investment Office

Doing business in Ethiopia ranking, 2010



Source: Doing business, The World Bank Group, 2009

Note: The further from the centre the coloured line crosses the axis, the better performance the country shows

Key inhibitors

Financing, technologies and process management are limited locally and should be brought by new investors.

Financing, a qualified labour force and infrastructure remain the key constraints faced by business in Ethiopia.

However, these constraints are partly manageable by bringing financing, technology and process management to start up, then transferring skills and knowledge to the local workforce.

Infrastructure constraints are not prohibitive in most cases and can be managed by proper site selection.

The Ethiopian Government continues to make progress in relation to infrastructure improvements, particularly with respect to building roads and developing hydropower. With the completion of several high profile energy projects in 2011–2012, Ethiopia is expected to begin exporting electricity to Sudan, Djibouti, and Kenya.

Local businesses require the import of modern technologies and process management in order to improve the efficiency of local personnel.

Foreign investments in the financial sector are still restricted by the government, while local capabilities are limited.

“The labour force efficiency is quite low. Although the salary of the local staff is lower than in China, Chinese staff need less time for sewing.”

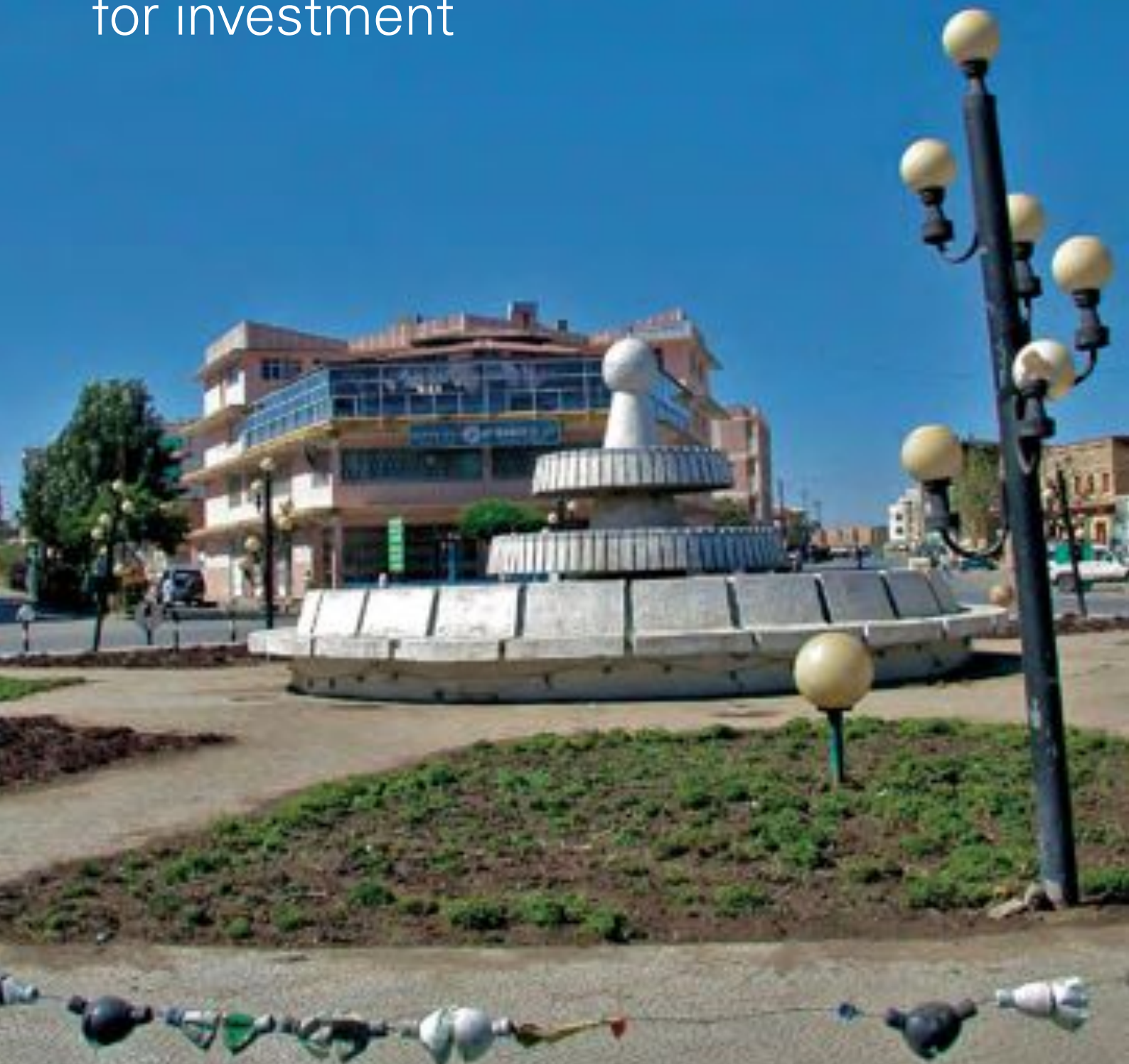
Owner of a textile business with distribution in Europe

Bureaucracy and administrative constraints can be managed through utilising local experience.

“The level of bureaucracy in the country is not high. Of course, there are some problems connected with delays in registration, the unclear system of local cooperation between different authorities, but the local partner undertook all the responsibilities.”

Dutch investor in horticulture industry

Mekelle, potential opportunities for investment



Introduction to Mekelle

The Mekelle region is currently one of the most attractive investment destinations in Ethiopia, driven by a highly supportive regional government, abundant untapped natural resources and good access to export markets.

Tigray State is the northernmost of the nine ethnic regions (Kililoch) of Ethiopia, with a population of 4.5 million in 2008. Eighty percent of the population is rural and 20 percent is urban.

Mekelle is the sixth largest city in Ethiopia and the capital of Tigray State. It is located approximately 780 km from the capital, Addis Ababa, in the Ethiopian highlands.

The Mekelle region enjoys a mild highland climate with an average temperature of 25°C. The rainy season in the Mekelle region is from June to September, while the dry season is from October to May. The average annual rainfall is approximately 579mm.

The total population in the city of Mekelle was estimated at 215,546 in 2008. The annual population growth rate is approximately 2.6 percent.

Location of Mekelle



Source: Millennium Cities Initiative Report, 2009

Investment climate

Due to its proximity to a former military zone, Tigray State has underperformed in terms of economic growth and inflow of private investments and is therefore ripe for investment.

Ethiopia suffered from lack of investment from 1998 as it was at war with Eritrea. The war took place from May 1998 to June 2000.

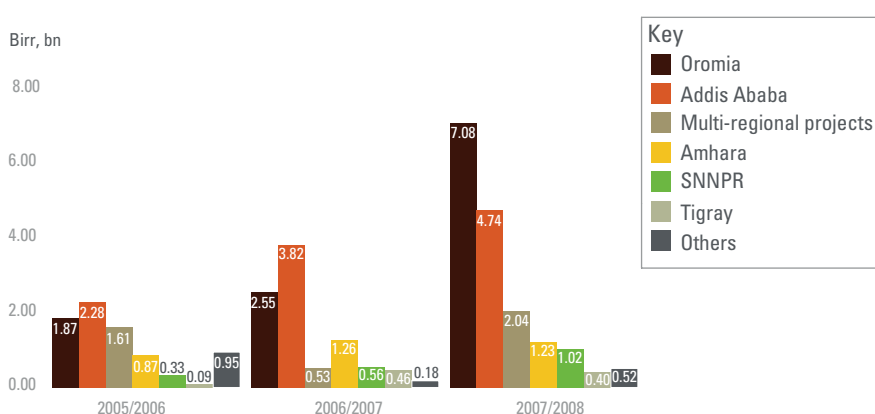
As we can see from the graph of FDI distribution, historically Tigray state underperformed against most Ethiopian regions in attracting FDI.

On 18 June 2000, the countries agreed to a comprehensive peace agreement and binding arbitration of their disputes under the Algiers Agreement.

A 25-kilometre-wide Temporary Security Zone was established within Eritrea, patrolled by United Nations peacekeeping forces. On 12 December 2000, a peace agreement was signed by the two governments.

The relationship between Ethiopia and Eritrea is no longer antagonistic and the political environment is peaceful. Interview feedback indicates that there are no premises for impairment of the situation, although the border is unlikely to be opened in the short term.

FDI by state, 2005–2008



Source: National Bank of Ethiopia, Annual Report, 2008

Supportive state government policies, infrastructure development and availability of land makes the Mekelle region an attractive investment destination.

Investment promotion bodies

The Tigray Investment Office (TIO)

This operates as the official licensing body for all domestic investment and assists foreign investors once the Federal Ethiopian Investment Commission has issued an investment licence. The investment office acts as a 'one-stop shop', providing both pre- and post-approval investment services. The office provides information required by investors, receives investment applications, approves and issues investment permits, provides trade registration services and issues business licences to newly incorporated businesses. The office has 18 branches around Tigray State.

The main office in Tigray State is in Mekelle and was found to be very helpful and knowledgeable.

The Tigray Agricultural Marketing Promotion Agency (TAMPA)

This was established in 2004. Its main objective is to provide a rural development strategy to increase crop volumes and improve the efficiency of farms throughout the state. TAMPA is comprised of three departments: Market Research and Information; Market Infrastructure and Promotion; and Contract Farming and Farming Coordination.

The Tigray Bureau of Rural Development and Agriculture

This oversees cereal crop production, livestock, and irrigation. It also maintains a Natural Resource Development Department that focuses on soil conservation and forestry, and an Agriculture Input and Marketing Department that supplies modern inputs to promote urban-rural linkages and agriculture-based cooperatives.

The Tigray Bureau of Trade and Industry Small Business Investment Promotion

This places an emphasis on improving governance, service delivery and infrastructure. It maintains 40 SME branch offices throughout Tigray State.

The Trade and Industry office also provides loan facilitation that utilises DECSI, a large Ethiopian micro-finance bank, to administer federal loans. These loans are provided at an interest rate that is three percent lower than for the average private loan. Loans are approved on the basis of submitted project profiles.

The Tigray Development Association

The association does not work primarily in investment promotion, but coordinates with an extensive network of Ethiopian Diaspora members. While Diaspora members are typically registered as domestic investors, they are able to access foreign capital and serve as an important bridge to foreign communities. <http://www.tdaint.org/>

The Mekelle Chamber of Commerce

This is another conduit for investment promotion. The Chamber receives support from the Friedrich Ebert Foundation, a German development organisation. One of the agency's major objectives is to develop independent and standardised review mechanisms for accessing credit from local banks.

The following website has contact details for many of the above organisations which may be useful to prospective investors: www.tigraionline.com/business.html

Incentives permitted at state level

Tigray State has established industrial zones supplied with basic infrastructure at nine major towns, namely Mekelle, Adigat, Adwa, Axum, Endaslasie, Alamata, Maichew, Wukro and Humera. This enables investors to obtain land at a lower fixed lease price per square metre for each town.

For some strategic projects (livestock production, dairy farming, manufacturing, construction), land is provided at a negotiable price within and adjacent to industrial zones.

Rental of farming land is possible from the government and/or individual farmers for up to 50 and 20 years respectively. Based on the type of project and investment capital, a grace period of one to seven years related to land lease is provided to any company leasing urban land. A lease price discount is awarded for real estate developers, depending on the number of housing units this can be anything from five to 45 percent.

Labour force

There is an abundant, easily trainable and inexpensive labour force in Tigray State. The average salary is around USD20 per month.

“We pay about 70 dollars per month, which is more than the average salary in the region and it makes the staff more motivated. Our employees don’t want to lose their job, not only because of the salary, but also due to some additional benefits which they get like English lessons, paid sick leave etc.”

Gheralta Lodge Hotel Manager



Infrastructure

The Mekelle region is already well connected via road to other Ethiopian regions and key export hubs; the quality of other infrastructure is rapidly improving.

Road transport

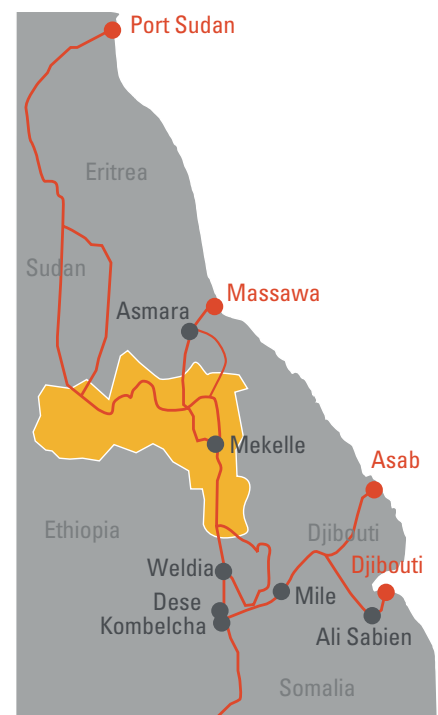
The upgrading of the existing main road that connects Mekelle with the port of Djibouti, Addis Ababa and other regions is underway. The government plans to finish the construction by 2012.

In Tigray State there is a total of 5,900 km of roads, of which 1,420 km are Ethiopian Road Authority administered federal roads, 1,130 km are Tigray State Road Authority administered rural roads and the remaining 3,350 km are dry weather community roads. The road density is 47 km per 1,000 km² of land. The average road density in Ethiopia is 27 km per 1,000 km² of land. Mekelle has 263 km of roadways, of which 40 km are asphalt roads, 63 km are gravel roads and the remaining 160 km are unclassified dirt roads. An additional 88 km of asphalt roads are planned.

Djibouti port is the most convenient for exporters due to its proximity to Mekelle. Massawa port in Eritrea is currently inaccessible for Ethiopian business.

There is a railway that connects Addis Ababa to the port of Djibouti which plays an important role in the transport of goods to and from the capital. Currently, the railway is in a bad condition and has limited accessibility although it is undergoing repairs.

Map of road connections from Mekelle to main ports



Source: Tigray Investment Office, 2009

Road infrastructure in Tigray State



Source: Tigray Investment Office, 2009

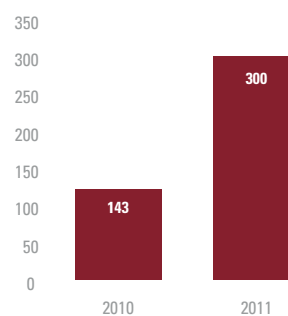
Distance from East African ports to Mekelle

Hotel	Port Sudan		Massawa	Assab	Djibouti				Berbera
Mekelle	1,339 km via Kasala, Humera (under construction)	1,579 km via Kasala, Gedarif, Humera, Shire-Enda Slase (under construction)	391 km via Asmara, Adigrat (closed)	899 km via Eli Dar, Kombolcha, Weldia (closed)	940 km via Kombolcha, Weldia (half under construction)	837 km via Mile, Chifra, Alewha	708 km via Semera, Yallo, Mekonni (under construction)	680 km via Serdo, Afdera, Shiket (under construction)	1736 km via Addis, Kombolcha, Weldia (under construction)
Addis Ababa	1,881 km via Metema, Azezo, Anjibara		1163 km via Mekelle, Weldia, Kombolcha	869 km via Kombolcha	910 km via Gelafi		847 km via Dire Dawa		964 km via Dire Dawa

Source: Tigray Investment Office, 2009
KPMG in Ethiopia interview programme, 2009

The number of dams in the Mekelle region is increasing, providing better conditions for agriculture.

Number of dams within 100 km of Mekelle



Source: Tigray Investment Office, 2009
KPMG in Ethiopia interview programme, 2009

Mekelle airport

Mekelle airport (Alula Aba Nega) has been upgraded recently to comply with international standards. It connects Mekelle with other Ethiopian destinations (Addis Ababa (two to three flights per day), Bahir Dar, Aksum, Lalibela and Shire). Flights are operated solely by Ethiopian Airlines.

The Ethiopian government has a vision for turning Mekelle airport into an international airport in order to support export from the region.

Ethiopian Airlines supports export activities, even at a loss. As an example, one major local meat producer negotiated with Ethiopian Airlines free delivery from Mekelle to Addis Ababa for meat destined for export to the Middle East. The final airfreight rate is similar to that for Addis Ababa exporters.

The Director of Ethiopian Cargo (a branch of Ethiopian Airlines) stated that similar arrangements are possible in the future with any export-oriented company of sufficient scale.

Direct cargo flights from Mekelle to the Middle East or the EU can be started when there are at least 30-40 tonnes of export cargo available per flight. This would be available for any industry and allows exports from Mekelle to be competitive.

“We aim at setting a common rate for Mekelle and Addis-Ababa exporters; however, we will have higher costs for delivering goods from Mekelle”.
Gebremichael Biwota, Director of Ethiopian Cargo

Cooling terminal

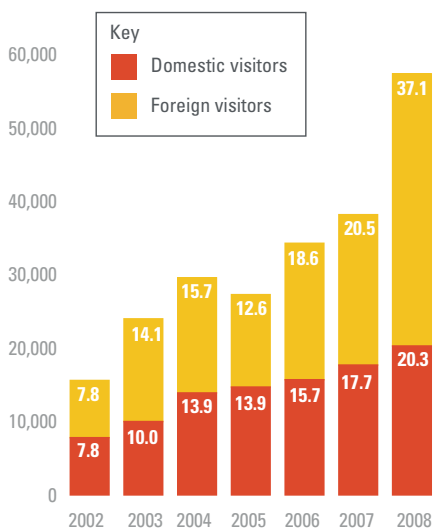
The cooling terminal at Mekelle airport is planned to be completed in early 2011. The total planned capacity is over 400 tonnes: 50 tonnes for flowers, 150 tonnes for fruit and vegetables and more than 200 tonnes for meat.

Select opportunities for investment in Mekelle

High quality lodge in Mekelle region

There is an opportunity to build a high-quality lodge in the Mekelle region. A well located, appropriately priced and equipped lodge in the Hawzein or Asbi areas (within 60–100 km from Mekelle) could be an attractive and immediate investment opportunity.

Number of tourist visitors to Tigray State (2000–2008)



Source: Tigray Investment Office, 2009

The Mekelle region has high potential as a hub for ecotourism due to pleasant natural conditions, easy access to the most interesting historic, religious and natural beauty sites of Tigray and Afar States.

The Mekelle region has a very convenient climate, nature conditions and landscape for the development of ecotourism.

Tigray State is home to Axum, a world-famous UNESCO World Heritage Natural Site, which is located 240 km from Mekelle. Mekelle and Axum have very good asphalted road connections.

The rock-hewn churches are a distinctive feature of Tigray State. They are similar to the world-famous churches of Lalibela, but predate them (7–11 Century in Tigray versus 11–16 Century in Lalibela). Most of the churches are concentrated within 80–150 km from Mekelle.

Facilities for ecotourism in the Mekelle area are underdeveloped; there is only one high-quality lodge in the area.

“Successful ecotourism development in the Mekelle region is not possible without a sufficient lodge chain within this area. We are ready to recommend our guests other lodges on their routes across Tigray, but only on condition that these lodges are of the proper quality”

Manager, high-quality lodge in the Mekelle region



The number of visitors to Tigray state has grown at an annual rate of 24 percent per annum over the period 2002 to 2008 and there is significant potential for a further increase.¹

Tigray State received approximately 15,600 tourists in 2002 and 57,500 tourists in 2008. Total receipts from foreign visitors reached 467 million Birr in 2007 (about USD50 million).

Although Axum still accounts for the majority of tourists coming to Tigray State, there has been an increase in the average number of days spent by foreign visitors in Tigray (from 1.7 days in 1994 to four days in 2007) which indicates that tourists include other Tigray attractions in their trips particularly the world famous rock-hewn churches.

Despite its high potential and fast growth, the tourism industry in Tigray State is underdeveloped. In 2007, the state accounted for only seven percent of the total number of foreign tourists visiting Ethiopia².

Customer profile

There are two main groups of foreign tourists coming to Mekelle for non-business purposes.

Retired people from Europe (mainly German, Italian and French) coming with the purpose of cultural tourism.

This group of visitors is very price sensitive; the main purchasing criteria for them are moderate accommodation cost and high level of services provided.

Expatriate population coming from Addis Ababa for weekend or short vacations. The main purchasing criteria for this customer group is an appropriate level of services provided and a wide range of additional services at a reasonable price (car rental, guard services, etc.).

There is potential demand from young visitors interested in adventure tourism within Tigray State and the Afar depression area. This group of tourists demands low cost accommodation with easy access to natural attractions.

Lack of quality lodge accommodation

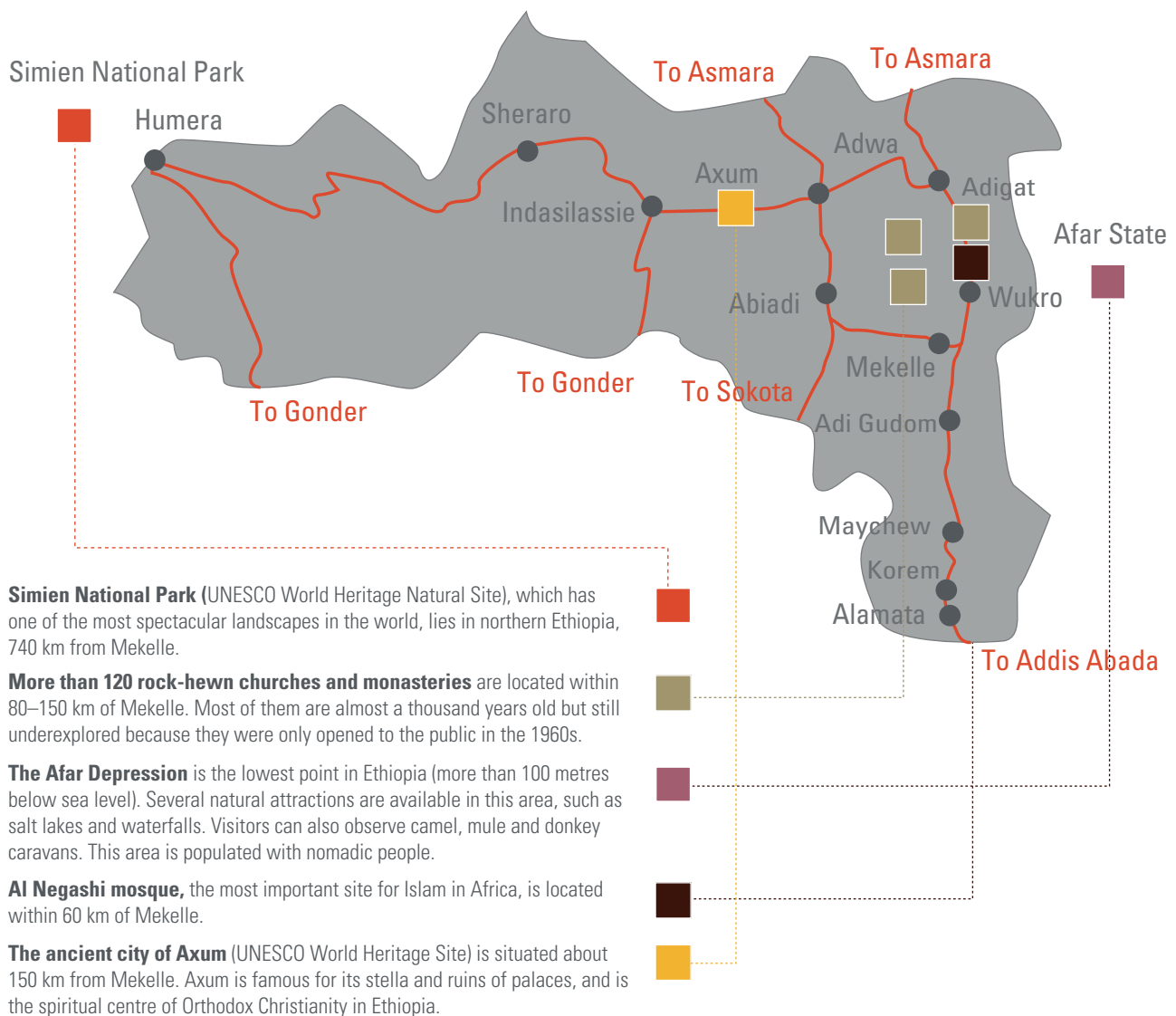
There is only one high-quality lodge run by an Italian investor currently operating in Tigray State (Gheralta Lodge in Hawzien). The lodge has 100 percent occupancy in the high season (some of the rooms are booked several months in advance) which indicates a supply shortage of quality lodge accommodation in the Mekelle region.

There are a number of motel-style lodges in the Mekelle region but the services they provide are not in line with the ecotourism concept. One investor from the UK has started preparatory work for construction of a lodge in the Hawzien area. The Tigray Investment Office has stated it has been contacted by four other investors expressing interest in lodge development in the Mekelle region.

There are plans for the construction of five tent lodges within the Millennium Villages Ecotourism project aimed at the development of community-based ecotourism in Tigray State. The total expected investments in the project amount to USD1.5 million. Possible activities at the sites include horse riding, rock climbing, trekking and cultural tourism³.

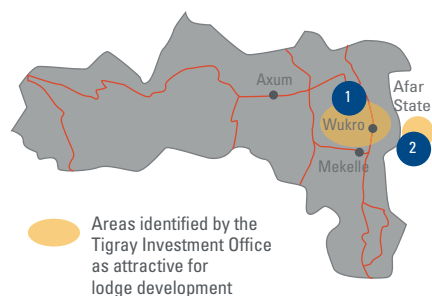
Source: 1. KPMG in Ethiopia interview programme, 2009
2. Tigray Investment Office, 2009
3. Africa News, March 19, 2008

Tourist attractions in the Mekelle region



Source: Tigray Investment Office, 2009
KPMG in Ethiopia interview programme, 2009

Areas identified by the Tigray Investment Office for lodge development



Source: Tigray Investment Office, 2009
KPMG in Ethiopia interview programme, 2009

1 Hawzien area

Potential activities: Religious and cultural tourism, hiking, climbing and horse riding.

Major attractions: About 100 rock-hewn churches; Gheralta mountains with stunning panoramic views.

Road availability: High-quality asphalted road from Mekelle to Wukro (47 km), then unpaved road from Wukro to Hawzien environs (50-80 km).

Utilities: Electricity is available in this area; a water supply check should be performed before starting land plot development.

One lodge is already in operation in Hawzien (Gheralta Lodge).

2 Asbi area

Potential activities: Adventure tourism; religious and cultural tourism.

Major attractions: Depression area of Afar State (including salt lakes; salt-loaded camel caravans; volcano; four famous rock-hewn churches (Mikael Imba, Mikael Debreselam, Mikael Barka, Ghergos Agebo).

Road availability: High-quality asphalted road from Mekelle to Wukro (47 km), then unpaved road from Wukro to Atsbi environs (23-30 km).

Utilities: Electricity is available in this area; a water supply check should be performed before starting land plot development.





There are a number of factors restraining the development of tourism in Tigray state, and Mekelle region in particular.

The lack of a well-trained workforce is identified as the main reason for the lack of services in the tourism industry in Tigray State.

There is no educational institution providing training in tourism in Tigray State. The primary educational institution for the tourism industry in Ethiopia is situated in Amhara State, an average of only 15 students from Tigray State are sent to this institution per year. Most hotels overcome this problem by running their own training programmes for their employees.

Insufficient marketing of the state, particularly at the international level.

In 2009 the Tigray Investment Office only participated in one exhibition abroad. According to representatives of the office this is not sufficient; participation in at least three foreign tourism exhibitions per year is required for sufficient promotion of the state.

The poor image of the north of Ethiopia, primarily due to the struggle with Eritrea in the late 1990s.

Nevertheless, as the political situation has improved, more overseas tour operators are including this region in their tours across Ethiopia and East Africa.

Insufficient tourism infrastructure.

Although the quality of roads has been improved significantly in recent years, the majority of roads to main tourist attractions near Mekelle remain unpaved (four-wheel drive vehicles required). There are only five tour operators in Mekelle providing four-wheel drive car rental services. Due to the shortage of transport facilities in the area, these operators can charge a high price for their cars (about USD100–120 per day).

Underdeveloped air connectivity.

The absence of direct international flights to Mekelle currently restricts the number of foreign tourists. There is an international standard airport in Mekelle, but currently it only serves domestic flights. International visitors can currently only reach Mekelle by air via Addis Ababa, which increases time and cost for potential tourists.

Government policy is directed at helping investors overcome current constraints.

On the federal level, the government supports the international promotion of the country (supplies marketing materials, assists with international exhibitions, covers the cost of the Ethiopian stand, assists in obtaining visas and air ticket discounts for tour operators participating in exhibitions, etc.)

The state government is responsible for promotion of the region. Regional authorities are entitled to define land policy in the region, allowing them to be flexible in relation to land price depending on the specifics of the relevant investment project.

Currently a number of projects are being implemented in the tourism industry:

- **Ethiopian Sustainable Tourism Development Project** aimed at boosting the country's tourism. A grant of USD35 million was provided by the World Bank, USD2.4 million of which is allocated to Axum for rehabilitation of the heritage site, enhancement of basic infrastructure and attraction of visitors¹.
- **Artisanal Crafts Development Project** aimed at re-establishment of ancient handcraft traditions at Axum.
- **Harnessing Diversity for Sustainable Development and Social Change Project** aimed at establishment of ancient handcraft traditions in Tigray (except Axum), setting-up of craft centres, help in design and marketing of craft products.

Source: 1. Ministry of Culture and Tourism, 2009

Process of acquiring a licence for a lodge in Tigray State.

- The investor completes a registration form in the Tigray Investment Office.
- The investor receives a recommendation letter from the Tigray Investment Office for submission to the local authorities.
- The investor identifies a suitable land plot with the assistance of the local authorities.
- The investor provides the Tigray Investment Office with the investment project proposal.
- The Tigray Investment Office supplies the investor with a Temporary Investment Licence (the type of licence depends on the specific project).
- After completion of construction work, the investor applies to the Trade and Industry Bureau for a Permanent Investment Licence.
- The Trade and Industry Bureau inspects the compliance of the lodge with the required standards and provides the investor with a Permanent Investment Licence.

Case study: Gheralta Lodge

Opportunity

- Opened in 2006 by an Italian investor, the Gheralta Lodge offers several comfortable, well designed cottages with terrific views, built in the local style and to high specifications. The average room price varies from USD35 70 per night.
- The land plot was provided to the investor for free for 17 years. The investor covered the cost of resettling local people from this area.
- During the first year the lodge hosted about 3,000 guests; in the last year more than 4,000 people have visited the lodge. On average guests stay in the lodge for 1–2 days. The occupancy rate varies from around 100 percent in high season (September–March) to about 30 percent in low season (June–July).

Challenges

- Skill level of local labour force (lack of technical skills required for hotel service, basic English).
- Access to water.
- Lack of construction skills available.

Meeting the challenges

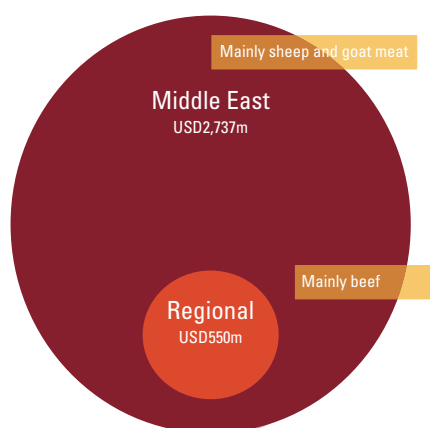
- The lodge is run by highly experienced management.
- There is a strong selection process for the local labour force.
- All lodge employees receive intensive training.
- Special remuneration schemes are applied (bonus for learning of English, pension scheme, sick leave compensation, etc.). The salary of lodge employees is 3–4 times higher than the average salary in the area.
- Two wells were drilled on the land plot (one for drinking water, one for water used for other purposes).
- The local construction labour force worked under the supervision of an Italian architect and experienced supervisors hired in Addis Ababa.



Meat production for export

Mekelle presents an attractive opportunity for investment into the export of Ethiopian meat, primarily to the Middle East and North Africa.

Indicative market size for meat and edible meat offal, 2007



Source: 1. UN Comtrade, 2008
2. KPMG in Ethiopia interview programme, 2009
Note: a. Market size is based on import figures for fresh, chilled or frozen meat
b. Middle East market includes UAE, Saudi Arabia, Yemen, Oman, Kuwait, Qatar, and Jordan. Regional market includes Djibouti, Sudan, Egypt, Tunisia, Morocco and Kenya

Mekelle provides opportunities in relation to meat production due to large livestock resources available in the area, the potential for meat export to the Middle East and North Africa, and weak competition.

The livestock population in Tigray State accounts for seven percent of the total livestock population in Ethiopia, which is the largest in Africa.

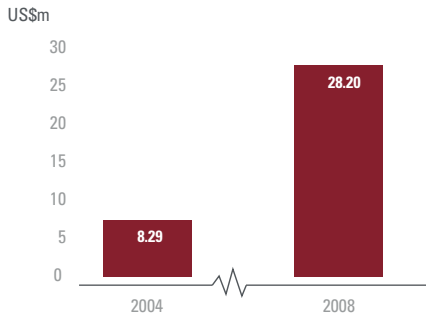
Tigray is well known for its special ox breed (Raya), which is more profitable than breeds from other regions due to its bigger size and more tender and tasty meat.

There are only five slaughterhouses in Ethiopia exporting meat to other countries. Up to three more slaughterhouses are under construction.

As of December 2009, there were no slaughterhouses in Tigray State. The first modern export-oriented slaughterhouse (Abergelle) will start operations in 2010.



Trade value of exports of meat and edible meat offal from Ethiopia



Source: 1. UN Comtrade, 2004, 2008

Ethiopian meat and edible meat offal export increased more than three times in the last five years.

There are limited opportunities for the sale of meat in the local market but significant potential in the Middle East markets.

The local meat market is highly saturated. Meat sold in the local market does not require certification, entry barriers are very low, and a lot of companies are operating in this market. The price for raw meat in the local market is approximately 15 percent lower than in export markets.

There are only five companies in Ethiopia which produce meat for export (who therefore own cooling and freezing facilities, and hold licences and certification). All of these companies are situated around Addis Ababa. These companies exclusively serve export markets, as foreign and local markets require different types of meat.

Currently, 98 percent of Ethiopian meat exports are shipped to United Arab Emirates (UAE) and Saudi Arabia. Nevertheless, the share of Ethiopia in the total import of meat into these countries is insignificant (less than one percent)¹. These markets appear to have a high potential for Ethiopian sheep and goat meat, mainly due to the fast growth of the expatriate population from Asian and African countries. These customers do not seek top quality meat, their major purchasing criteria is a reasonable price.

There are significant opportunities for Ethiopian meat in other Middle Eastern countries such as Jordan, Oman, Qatar and others, as well as in Northern Africa, especially in Egypt, Tunisia and Morocco, which remain under-explored.

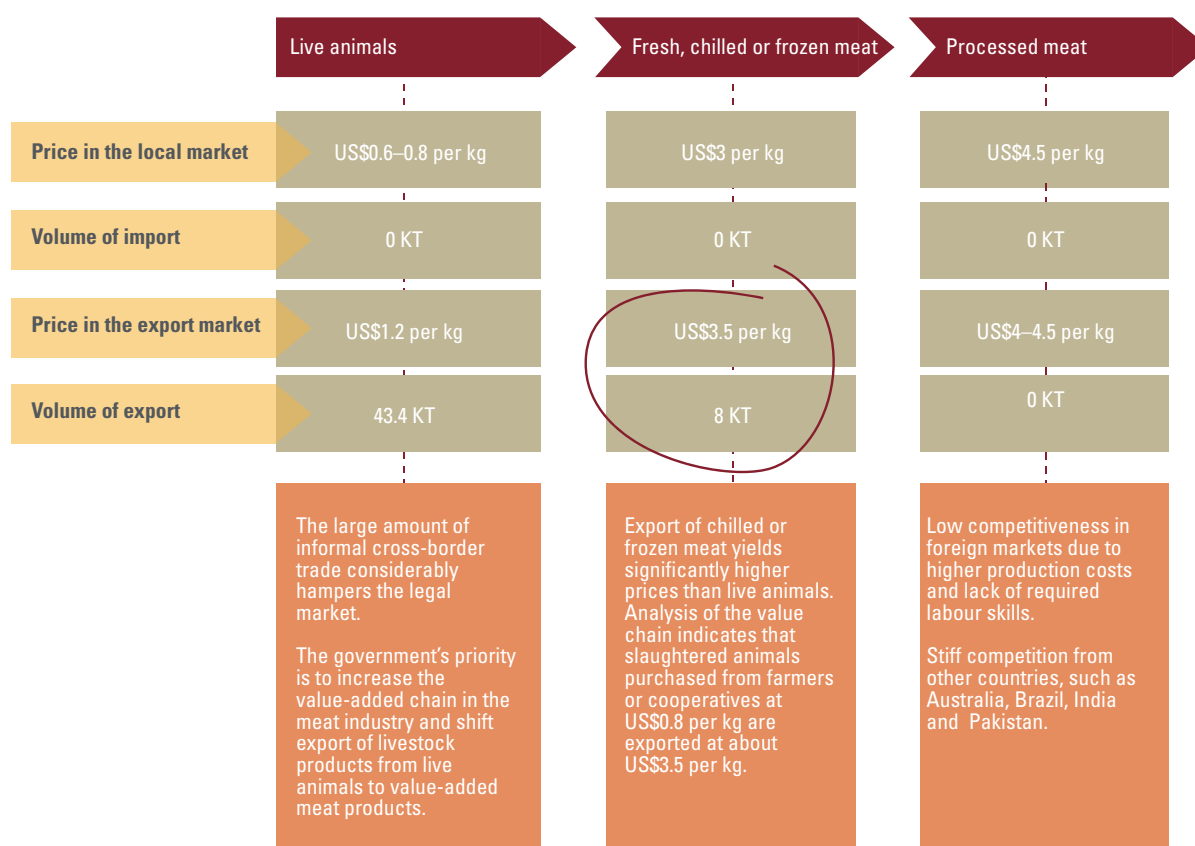
Ethiopian meat is not permitted for sale on European markets due to animal health, which is not in compliance with European quality standard requirements.

Livestock population in Tigray²

	Cattle	Sheep	Goats	Horses	Donkeys	Mules	Camels
Number of animals	2,622,166	813,546	2,399,808	1,894	387,389	7,901	32,777

Source: 1. UN Comtrade, 2004, 2008
2. Ministry of Agriculture and Rural Development, Agricultural Investment Potential of Ethiopia, March 2009

Meat production value chain, 2008



Source: KPMG in Ethiopia interview prog
Note: KT – thousand tonnes

Challenges

The instability of live animal supply, especially during the rainy season (June and July), is the major constraint for meat production.

The majority of households are situated in remote areas connected with unpaved roads which are washed away during the rainy season, making it very difficult for animal collectors to reach these areas. In addition, private households have a lot of feed available for their animals in the rainy season and are less likely to sell them as they are aware that a well-fed, fattened animal will fetch a higher price.

Meat quality certification is a pressing problem when exporting to other countries.

The low meat quality caused by poor feed and animal diseases results in many rejections of Ethiopian meat by export markets. Ethiopian meat has been banned from Arabian countries several times. The last ban lasted around three months from March 2009. Currently, producers do not have the required certification to export to Europe, but if implemented, the lucrative market would be opened up.

The government has taken a number of steps towards improving animal health, such as setting up veterinary services across the country.

Some market players, for example the Abergelle Slaughterhouse, have established European standard check systems within their production lines to control the quality of meat during the production stage.

Investment overview

The indicative costs for setting up a medium-sized slaughterhouse are estimated in the range of USD1.5–1.7 million¹.

Investors should consider this investment within the next 1.5 to 2 years.

Instability of demand in export markets poses a challenge for meat exporters.

As the majority of consumers of Ethiopian meat in the Middle East markets are expatriates from Asia and Africa, demand for meat decreases by up to 20–30 percent when this population returns to their native countries for holidays. Market participants could smooth the demand volatility through market diversification.

Although there are currently no direct flights from Mekelle to target export markets Ethiopian Airlines has said they would schedule direct flights if there was sufficient demand.

Ethiopian Airlines has said that for smaller export quantities they would consider setting up an arrangement where they fly exports via Addis Ababa and not charge for the Mekelle to Addis Ababa leg.

Case study: Abergelle Slaughterhouse

Opportunity

- The first export oriented slaughterhouse in Tigray State is planned to start operations in 2010. The slaughterhouse will produce meat exclusively for the export market (mainly beef due to the large supply of oxen in the region). Target export markets: Middle East and North Africa (primarily Egypt).

Challenges

- The absence of direct flights from Mekelle to target export markets has been identified as the main constraint for the company. The volume projected for export is not sufficient to start direct flights abroad.

Meeting the challenges

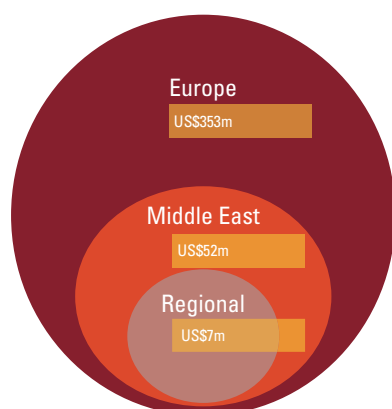
- The slaughterhouse negotiated with Ethiopian Airlines free cargo transportation from Mekelle to Addis Ababa for meat which is destined for export abroad. As a result, the final airfreight rate for Abergelle will be similar to that for Addis Ababa exporters. This arrangement is available for other exporters.

Source: 1. KPMG in Ethiopia interview programme, 2009

High-quality honey processing for export

The Mekelle region provides attractive opportunities for producing high-quality honey for supply to Sudan, Middle East, and European markets. The honey supply shortage, which is currently the key constraint, is likely to be overcome in the mid term.

Indicative market size for honey, 2007



Source: 1. UN Comtrade, 2008
Note: a. Market size is based on import figures for natural honey
 b. Middle East market includes UAE, Saudi Arabia, Yemen, Oman, Kuwait, Qatar, and Jordan. Regional market includes Djibouti, Sudan, Egypt, Tunisia, Morocco and Kenya

The large bee population, superior quality of Tigray honey and promising opportunities for export make honey processing attractive for investment.

Tigray has a moderate climate due to its highland position, which is favourable for honey production.

The Mekelle region has a large bee population (about 37 thousand bee colonies; 20 percent of the Tigray total).

Tigray is famous for its high-quality white honey (made from pollen from white flowers) with low moisture content, which can enjoy a price premium. Tigray honey has a special aroma that would provide a competitive advantage in niche markets.

Compound Annual Growth Rate (CAGR) of honey import for selected markets ¹	
Country	CAGR (2004–2008) %
United Kingdom	10
Yemen	28
Israel	37
UAE	9
France	15

Source: 1. KPMG in Ethiopia interview programme, 2009



There is high potential for supply of Tigray honey to Europe and the Middle East.

In spite of its favourable natural conditions and large bee population, up until 2007, Ethiopia was a negligible supplier of honey to international markets. Almost the entire honey volume produced was consumed locally (mainly for production as a local wine). A very small amount of honey was exported to Sudan and Middle East markets.

Until 2008, the European market was closed for Ethiopian honey producers. As indicated in an interview with a representative of the Honey and Beeswax Producers and Exporters Association, Ethiopia became an accredited country for supplying honey to the EU in 2008. In 2008, revenues from honey export from Ethiopia to the EU amounted to USD120 thousand (98 percent of which was exported to the UK).

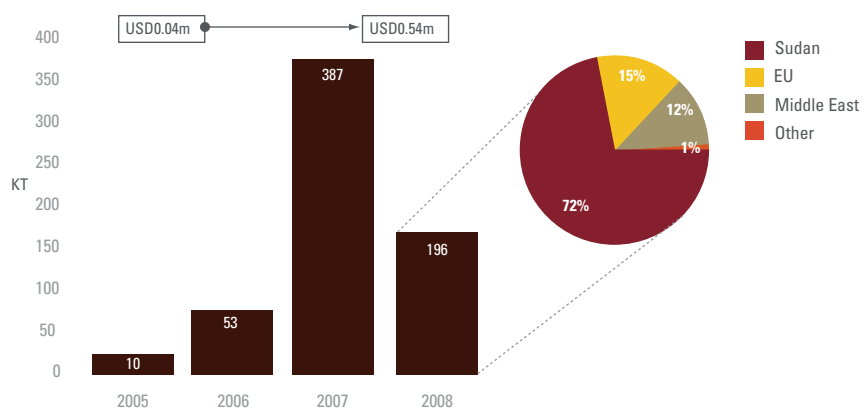
The EU, Yemen, Israel and UAE can be considered as the major potential target markets for Ethiopian honey. The import of honey into these markets has been increasing steadily over the last five years and is expected to continue to increase within the next two to three years.

Beeswax production and export can be considered as a potential opportunity in the short term, but does not appear attractive in the mid and long term.

Although Ethiopia is currently one of the largest beeswax exporters in the world, beeswax opportunities in Tigray State appear to be limited in the mid and long term due to the ongoing replacement of traditional with modern hives.

Despite the fact that modern hives can produce 5–10 times more honey than traditional ones, the wax yield from modern hives is 0.5–2 percent compared to 8–10 percent for traditional hives.

Ethiopian honey export dynamics and structure, (2005–2008)



Source: 1. UN Comtrade, 20045-2008

The local market for honey also shows significant potential for investors. However, the domestic market is not as attractive for processed honey as foreign markets.

Local demand is mainly for raw honey, not the value-add processed honey which commands a higher price.

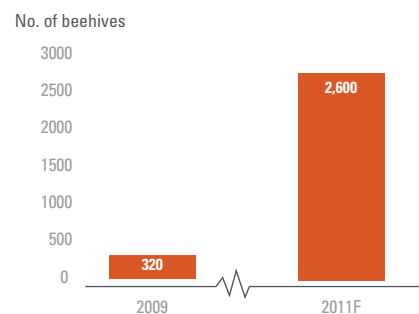
The majority of honey for local consumption is distributed through traditional markets.

Case study: Millennium Villages Honey Project

Opportunity

- The Millennium Villages Project (MVP) is implementing a large scale honey and beeswax production system across its 11 villages in Tigray State. The major goal of the project is to support beekeepers by establishing cooperatives, providing inputs and hives and facilitating distribution of raw honey to customers.
- Ten cooperatives have been established consisting of 1,500 households. Planned investments amount to USD450 thousand.²
- The project is aimed at developing a collection and management system for 4,000 hives capable of producing 240 tonnes of honey annually, for revenue of over USD1.5 million¹. 2,600 modern beehives are expected to be introduced by 2011. 320 hives have already been distributed to 200 farmers². From 2005 to 2008 the MVP provided free inputs for households producing honey. Starting from 2009 inputs have been provided on a credit basis.
- The introduction of modern hives by the MVP will lead to an increase in productivity from the current 8 kg per hive: in the first year to 10 kg per hive; in the second year to 30 kg per hive; in the fourth year 45 kg per hive.²

Number of beehives to be introduced within the Millennium Villages Project



Source: 1. Columbia University – Investment Promotion in Mekelle, Ethiopia, October 2009
2,3. KPMG in Ethiopia interview programme, 2009

Case study: Comel Honey Processing

Opportunity

- Comel was originally planned as an agricultural company focusing on exports. It exports honey to the US and Dubai. Comel's capacity is 3,000 kg per year, although the capacity utilisation is currently only 30 percent. Low capacity utilisation is caused by a lack of supply. The most profitable type of honey is white honey, which is more expensive than other types and is of high demand in export markets.

Challenges

- There was no possibility to supply honey directly from Mekelle to other countries as there is no international airport in Tigray State.

Meeting the challenges

- Comel exports honey to the US through Addis Ababa, which has an international airport.

Source: 1. Ethiopian Beeswax Producers and Exporters Association, 2009
2. KPMG in Ethiopia interview programme, 2009

Investment overview

The indicative cost for setting up a honey processing plant is estimated at USD200 thousand¹. An additional USD80–100 thousand will be required for working capital².

Shortages in honey supply, currently the key constraint, is likely to be overcome in the mid term.

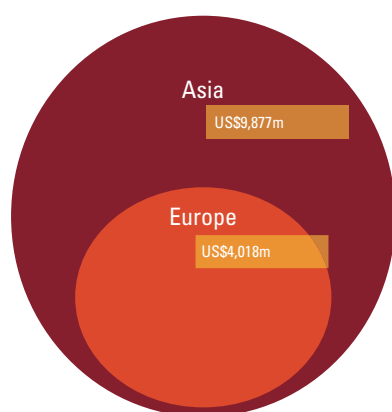
Tigray honey is considered to be of superior quality, which allows local honey producers to charge slightly higher average prices than in other parts of Ethiopia.

The price for honey in Tigray State has skyrocketed from 35–40 Birr (USD2.5–3) per kg in 2008 to 70–80 Birr (USD4.5–5.5) per kg in 2009, driven by the shortage in supply caused by the recent drought. Given that the current price for honey in the export market is not higher than USD3–4 per kg, this makes honey processing and exporting unprofitable. Nevertheless, the price is expected to recover in the next 1–1.5 years provided no droughts occur in the region.

Processed leather and leather goods for export

There are investment opportunities in relation to leather processing driven by the large livestock population and special characteristics of Ethiopian leather. Nevertheless, these opportunities are currently restrained by the quality of raw skins and hides and strong irregularity in supply.

Indicative market size for hides, skins and leather, 2008



Source: UN Comtrade, 2008
Note: a. Market size is based on import figures for hides and skins (other than fur skins) and leather
 b. Asian market includes China, Russia, Hong Kong, Malaysia, Indonesia, Japan

Mekelle provides opportunities in relation to leather processing and leather goods production due to large livestock resources available in the region, the special quality of local leather, as well as the high potential for export to Europe and Asia.

Ethiopia has the largest livestock production in Africa, and the tenth largest in the world. Sheep and goat skins account for the bulk of Ethiopian leather production.

Ethiopian leather is considered to be of premium quality and is in high demand in international markets:

- **Cabretta:** Hide from highland hair sheep is famous for its natural characteristics of flexibility, thickness, strength and compact texture, which makes it especially suitable for high-quality gloves (including industrial gloves) and sports equipment.
- **Bati:** Goat skin, which is in demand for the production of fashionable types of leather, especially suede.



There is potential for export of Ethiopian leather to Asian markets and Europe.

The leather sector is one of the top five export earners for Ethiopia, accounting for 6.5 percent of total export revenues in 2006–2007. Ethiopian tanneries have traditionally exported leather at various stages of processing, but semi-finished leather accounts for the majority of exports. However, there is potential for production of leather goods (shoes, garments etc.) which require only basic processing skills.

Italy, China, the UK, Russia and Hong Kong account for about 75 percent of all skins and hides exported from Ethiopia. Ethiopia's share in total leather imports to these countries is currently small (less than one percent) and could be expanded.

Export opportunities exist in further penetration of current major export markets, as well as in exploring Turkey and South East Asian markets (Indonesia, Malaysia, etc.).

A five percent drop in the total value of imported hides and skins in the global market was observed in 2009 as a result of the global economic crisis¹. Nevertheless, the leather market has a good outlook: Demand and prices are expected to recover in the mid term².

The key challenge is the irregularity of supply.

A key challenge with the leather sector is the by-product status of hides and skins: Livestock is mainly used for meat production, which is why hides and skins arrive when meat is needed, not when they are required for leather processing.

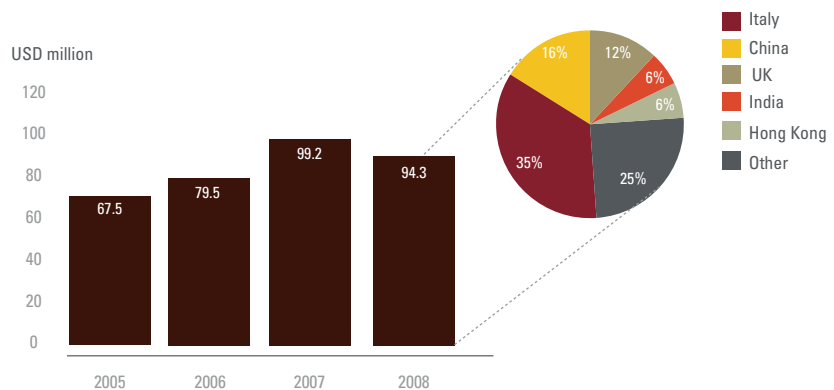
The quality of raw materials is critical.

It was indicated that flay cuts, holes, scratches, dirt, putrefaction and animal diseases, mainly arising from the traditional system of animal husbandry at the household level, negatively impact the leather industry. Once imperfections are attributed to the raw leather, little can be done to improve the leather quality in other stages of the process.

In order to solve these problems, projects are being implemented with the participation of the Eastern and Southern Africa Leather Industry Association (ESALIA), UNIDO, FAO, and others.

Source: 1. KPMG in Ethiopia interview programme, 2009
2. Tigray Investment Office, 2009
3. UN Comtrade, 2007–2008

Ethiopian leather products export dynamics and structure, (2005–2008)



Source: UN Comtrade, 2005–2008

Case study: Sheba Tannery

Opportunity

- Started in 2003, Sheba is currently operating at 50 percent capacity, processing about 3,000 skins per day (the maximum capacity is 6,000 sheep and goat skins and 700 cow hides per day). Sheba exports semi finished and finished leather to Europe and Asia. Capital equipment and specialty chemicals imported for leather processing and leather goods production are duty free.¹
- At present the tannery does not produce finished products but plans to begin producing about 2,000 shoes per day starting from 2010. There are also plans for gloves production. While part of the shoes will be sold in the local market, the gloves in particular will almost exclusively be export items.

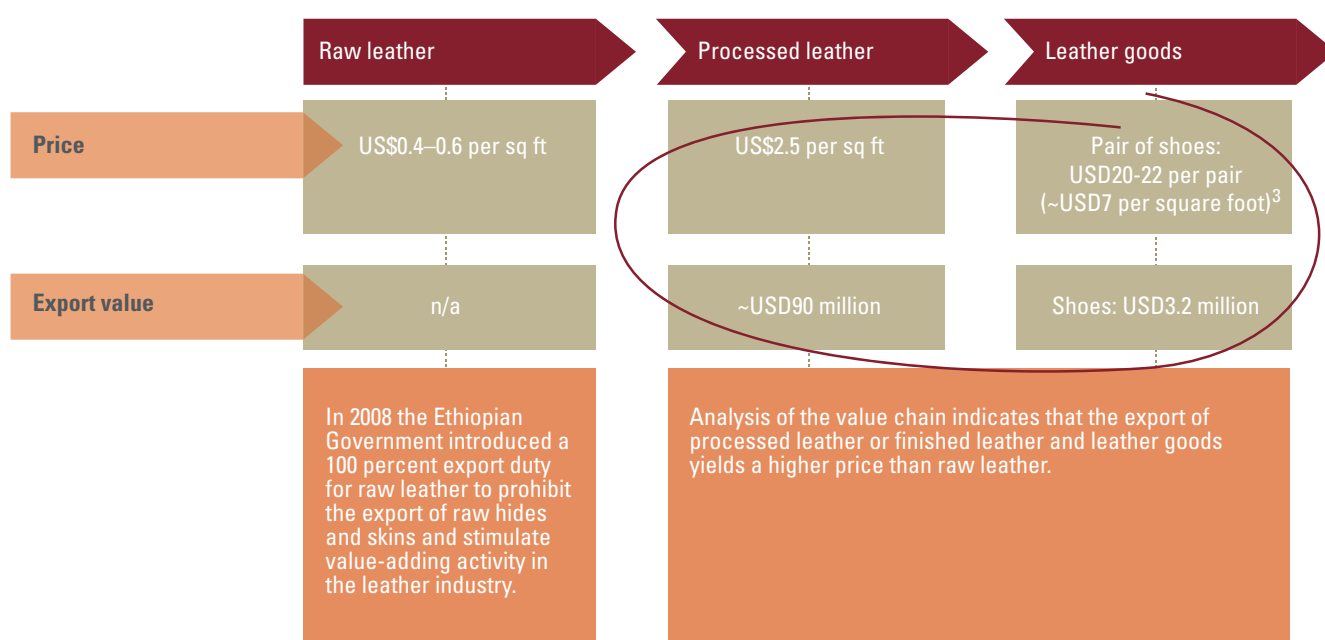
Challenges

- In the first years of operation the tannery faced difficulties connected with the lack of technical skills among its workforce. The low quality of raw hides and skins has proved challenging.

Meeting the challenges

- The company is improving quality issues through extensive test sampling from different suppliers. The workforce has responded well to training.

Leather production value chain, 2008



Source: 1. KPMG in Ethiopia interview programme, 2009

2. Columbia University – Investment Promotion in Mekelle, Ethiopia, October 2009

Note: 3. Based on three square feet of leather required for production of one pair of shoes

Out-of-season fruit grown for export

The Mekelle region presents attractive opportunities for growing selected varieties of fruit and vegetables to supply Middle East and European markets.

Favourable agro-climatic conditions

The climatic conditions of the Mekelle region are particularly good for certain types of tropical and sub-tropical fruit. The region is considered to possess favourable soil types, climate and altitudes for growing pomegranates, grapes, avocados, mangos and other fruit.

The Mekelle region is a highland area with altitudes of 2,200–2,600 metres, consistent climatic conditions and long hours of sunshine, enabling almost uninterrupted, reliable year-round fruit production.

The temperature remains stable during the year, with an average daily maximum of 23–27°C and minimum of 10–12°C.

“You can grow almost any type of fruit over there [Mekelle region]; however, you need to perform a detailed feasibility study to select what particular fruit is best suited for a particular location.”

Investor planning to grow fruit in the Mekelle region

Suitable land plots are available at low cost

There are a number of large (greater than 50 hectares) land plots available for investors with access to water, asphalted roads and power supply.

There is around 2,500 hectares of land suitable for horticulture within a 30–100 km distance from Mekelle. More than 330 hectares of land has good quality water resources for surface irrigation; the remaining area can be irrigated using a combination of underground and surface water resources.

“There are plenty of land plots available in Tigray State. We have been offered five land plots in the Mekelle region and now we need to perform soil and water tests to select the most suitable area for growing export quality avocados.”

International investor with extensive horticulture experience in the Middle East, Latin America and Africa

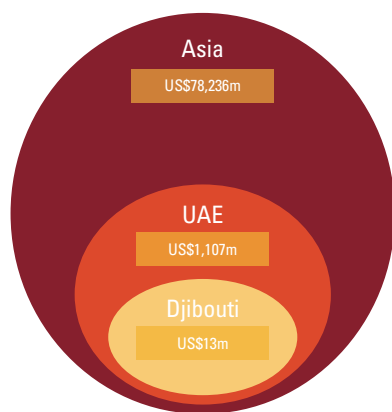
Favourable location to serve export markets

Mekelle has a more favourable location for export compared to the Addis Ababa region, due to its proximity to the Djibouti port via the Mekelle-Djibouti road.

Key Ethiopian fruit and vegetable export markets —Djibouti, the Middle East and the EU — are accessible via the Djibouti border/Djibouti port.



Indicative market size for fruit and vegetables, 2007



Source: FAO, 2009
Note: Based on total import figures for fresh and processed fruit and vegetables

A successful supplier of fruit and vegetables to the Middle East and EU should be able to ensure consistency in quality and supply, and provide recorded and demonstrated traceability of products and production.¹

Source: 1. WUR – *Development Strategy for Export-orientated Horticulture in Ethiopia*, March 2007

Customers in the Middle East and Europe have significant buying power and high quality standards.

Ethiopian suppliers may have competitive supply during low/no production periods in Europe and the Middle East, and can have a cost advantage for labour intensive types of fruit (e.g. grapes).

Ethiopia is virtually the only supplier of vegetables to the European market in the January to March period, due to the absence of production in Europe and unreliable supply from Morocco and Egypt.

There is low local supply of fruit and vegetables in the Middle East during June to September due to very high temperatures and droughts. This presents an additional opportunity.



There is significant potential to supply out-of-season fruit to Europe and the Middle East.

Despite its favourable location and agro-climatic conditions, Ethiopia is a minor supplier to the Middle East and European markets, primarily due to the inconsistent quality and unstable supply of fruit and vegetables.

Ethiopian exports to these markets are negligible and largely fragmented. Ethiopia accounts for less than one percent share in European and Middle East fruit and vegetable imports.

Djibouti

Djibouti's arid climate and rocky soil result in almost 90 percent of fruit and vegetables being imported. Ethiopia is a key supplier of fruit and vegetables to Djibouti, however, export is dominated by small scale traders supplying low value/low quality produce. There is growing demand for high quality fruit and vegetables in Djibouti that can be served by Ethiopian suppliers.

Middle East

Growing demand and limited local production makes the Middle East fruit and vegetable market a very attractive export destination. The United Arab Emirates (UAE), Saudi Arabia and Kuwait, the largest regional markets, are primarily supplied by Egypt, Iran and South Africa. Competition is tough. However, Ethiopian suppliers can benefit from a favourable location and out-of-season fruit supply.

European Union

As one of the largest fruit and vegetable markets globally, the European Union's imports are growing by over 10 percent annually. High quality and safety standards, along with tough price competition, can make expansion into the European fruit and vegetable market quite challenging for Ethiopian suppliers. However, Ethiopia already successfully exports out-of-season fruit and vegetables particularly green beans.

There is growing demand for fruit such as mangos, avocados and grapes in the European market. Customers are willing to diversify suppliers, providing room for Ethiopian exporters.

Ethiopian fruits and vegetables (for example, strawberries and green beans) are available in European supermarkets such as Tesco in UK and Auchan in Russia.

Source: 1. WUR – *Development Strategy for Export-Oriented Horticulture in Ethiopia*, March 2007

Constraints

Djibouti port

Currently, the Djibouti port is the only feasible gateway to the Middle East and European markets. The major constraints in relation to the use of the Djibouti port are the condition of Mekelle to Djibouti road, the time-consuming handling procedures at the port, the poor port infrastructure and infrequent vessel departures.

Mekelle is connected with the Djibouti port by asphalted road with some unpaved areas. Although the condition of the road is a constraint, the road is suitable for transporting all types of goods and exporters do not feel the condition of the road inhibits exports.

“Port personnel usually have a low level of professionalism and poor motivation, resulting in long waiting time.”

Managing Director of export-oriented garment factory in Addis Ababa

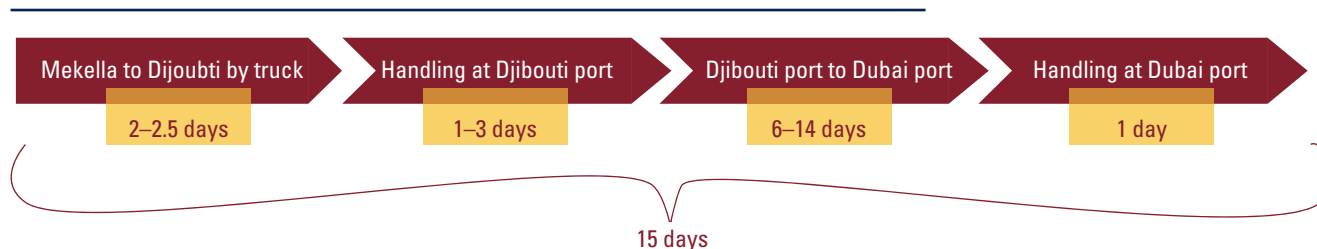
Port infrastructure can make handling some of merchandise flows efficiently difficult. Currently, there are no cooling terminals at the port.

Although there are six international shipping lines operating at the Djibouti port, there are only three to four departures for the Middle East per month.

During the interview programme it was identified that there are plans to upgrade the port to a trans-shipment port, but the timing was uncertain.

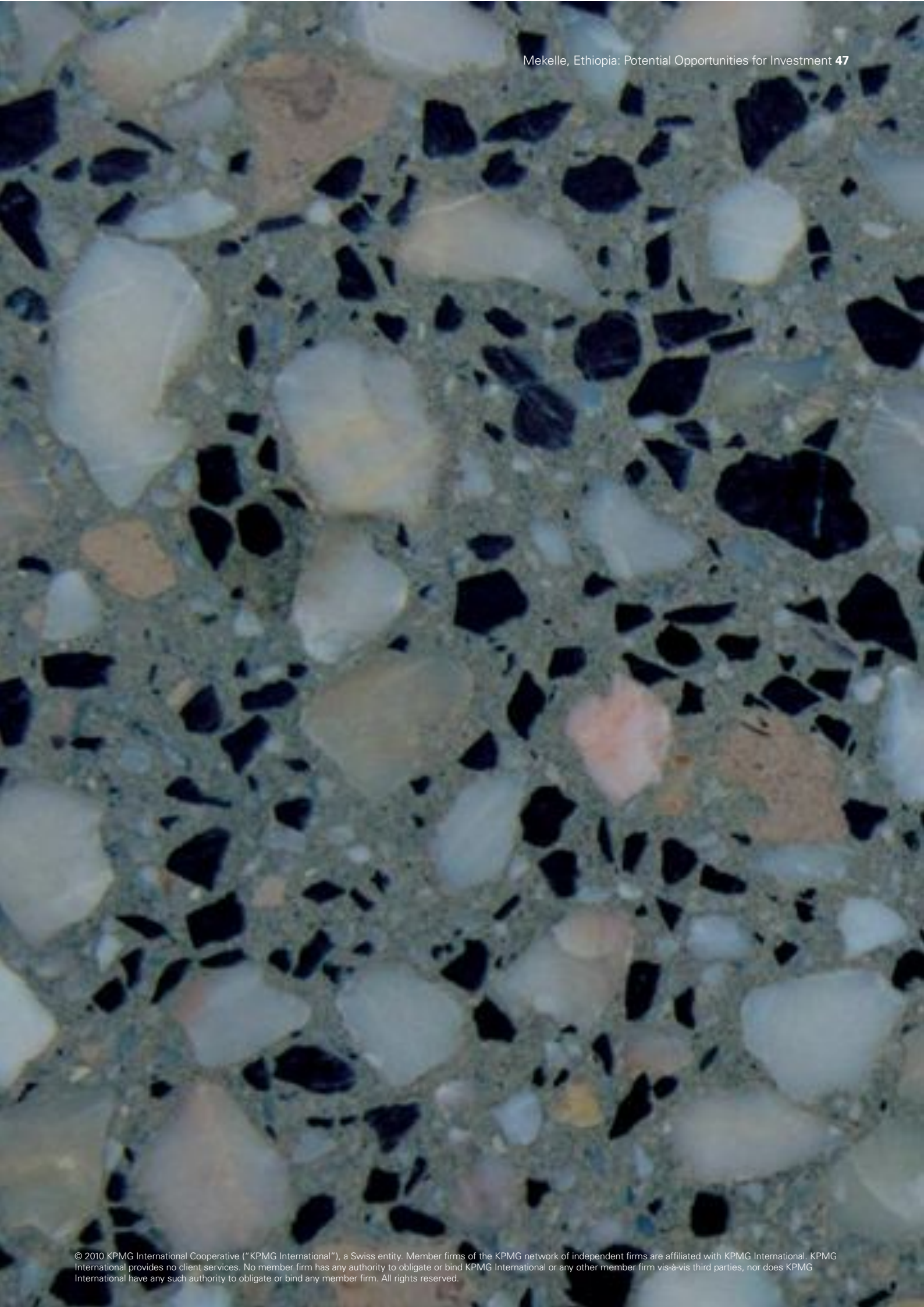
It was identified that the total time required to deliver goods from Mekelle to Dubai via Djibouti port is around 15 days that is almost the same as to take goods from Addis Ababa to Dubai

Average length of time from Mekelle to Dubai port



Source: KPMG in Ethiopia interview programme, 2009
www.searates.com

Note: Djibouti-Dubai transit time depends on the type of goods and timing of vessel transit stops. Transit time to Palermo port in Italy is eight days or more



Dimensional stones and industrial minerals

The Mekelle region provides attractive opportunities in relation to dimensional stones and industrial minerals.

Central and Eastern Tigray has abundant resources of dimensional stones and industrial minerals.

There are significant untapped resources of limestone, granite, marble, slate, silica sand and greenstone to the north and north-west of Mekelle.

Limestone

One of the largest limestone-rich areas in Ethiopia is located in the radius of 30 km from Mekelle. The major African cement producer — Messebo Cement — already sources its limestone, clay and other inputs from deposits around Mekelle. There are still large limestone reserves available for investors. Reserves are located in close proximity to asphalted roads and are easily accessible.

Marble and granite

Central and Eastern Tigray is known for its wide variety of marble and granite. Body colours vary from smoky white and pink to dark grey and black. The largest marble deposit in Ethiopia — Naeder Marble — is located about 55 km from Axum.

The largest Ethiopian dimensional stone processing plant — Saba Dimensional Stone plc. — is located in Adwa town, north-west of Mekelle. The annual processing capacity is about 85,000m² for marble and limestone, 40,000m² for granite and around 100,000m² for terrazzo tiles. Tiles and slabs are sold locally with about 50 percent of sales generated in Tigray State.

Other mining resources

There are three slate localities with total measured aerial coverage of over two million m².

There are two deposits of silica sand located about 90 km north of Mekelle. They are easily accessible from the Mekelle to Adigrat asphalted road. Reserves have not yet been estimated.

Several international companies have obtained gold exploration licences in Western Tigray (over 150 km from Mekelle), however, no mining activities have been started yet.



The construction industries of Ethiopia and Sudan provide attractive opportunities for processed dimensional stones (marble, granite, tiles, slabs).

There is an opportunity to supply marble and granite tiles to the booming local construction industry and export some products to Sudan.

The Middle East and European markets are largely inaccessible for tile or slab producers due to prohibitive transportation costs.

Competitive export sales to Europe and the Middle East are possible if access is obtained to Eritrean sea ports.

Opportunities exist for producing glass from silica sand found in the region.

The Ethiopian cement market is currently very attractive, driven by significant undersupply and extremely high prices. However, new cement capacities to be introduced during 2011 are expected to eliminate the cement shortage and drive prices down.

Road accessibility in some areas is a constraint.

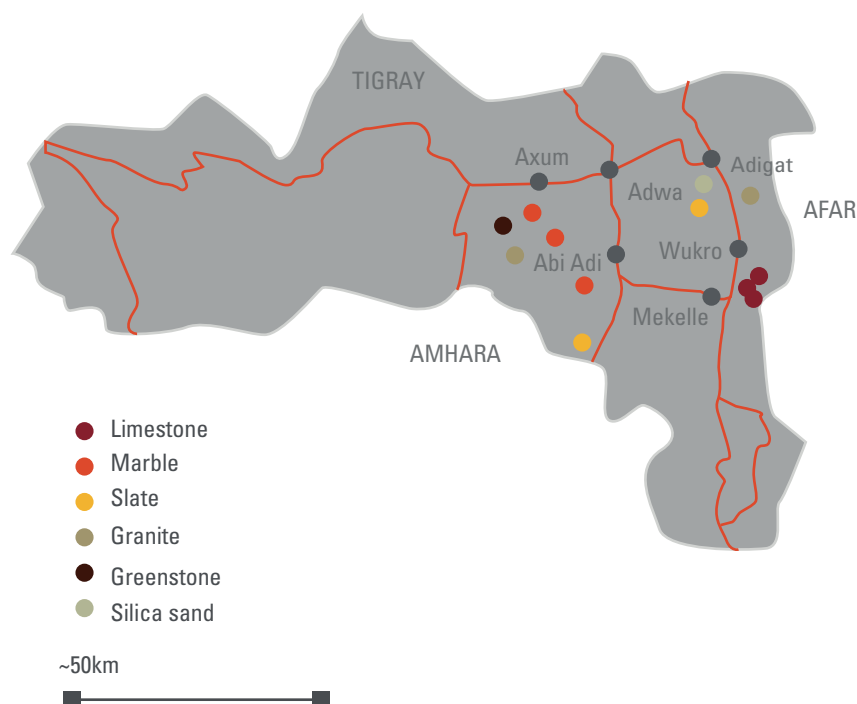
Poor road accessibility to some deposits remains a constraint for mining sector development in Tigray State.

The majority of marble and granite deposits have poor road accessibility resulting in high transportation costs.

“We have to replace spare parts for our machinery very often due to poor road conditions to the majority of our quarries.”

General Manager, Saba Dimensional Stones plc.

Mineral map and estimated reserves, 2009



Estimated reserves of major types of minerals found within 150 km of Mekelle

	Deposit/locality name	Estimated reserves
Limestone	Gogon Da'ero, Sherafo, Neta'et (Ma'alamal) limestone	Over 0.6 million m ³
Marble	Adiwoyane, Taget, Naeder, Newi, Emnizong marble	Over 800 million m ³
Granite	EmbaMadre, Negash granite	Over 58 million m ³
Slate	Chiemite, Guftamne, Gilgile slate	Not estimated
Silica sand	Edaga Hamus and Senkata silica sand	Not estimated
Greenstone	Zana greenstone	About 40 million m ³

Source: Tigray Water Resources, Mines and Energy Bureau

Case study:
Messebo Cement

Opportunity

- Messebo Cement is one of the largest cement producers in Eastern Africa. It was established in 2000 through the EFFORT programme and occupies a 200 hectare site to the north of the city. Messebo currently produces 900,000 tonnes of cement per year, which should increase to about two million tonnes per year after a two year expansion plan is completed. Currently, 40 percent of total cement production is sold to buyers in Addis Ababa.

Challenges

- There were several electricity cuts in 2008 due to an electricity deficit across the country that resulted in production stoppages for around one month.

Meeting the challenges

- Several hydropower dams have been put into operation in late 2008–2009, making Ethiopian power generation sufficient to cover local demand.

The government has developed liberal mining legislation.

Foreign investors are not restricted to exploration, mining, processing and export operations in Ethiopia³.

The Ethiopian mining sector is regulated by the Mining Law, Mining Income Tax Law and Mining Regulations.

Ethiopian mining legislation contains the following provisions:

- Private investors are allowed to perform all kinds of mining operations.
- A one year exclusive prospecting licence and three year exclusive exploration licence are provided to investors, with two renewals of one year each.
- A 20 year exclusive mining licence can be provided to investors, with unlimited renewals of 10 years each.
- The licensee's right to sell minerals locally and abroad is guaranteed by law.
- Minerals not originally specified in the licence may be subsequently added to the licence as discovered.
- An exemption from customs duties and taxes on the import of equipment, machinery, vehicles and spare parts necessary for mining operations is provided.

Cost of licences and royalty payments in Tigray State

Type of minerals	Exploration licence	Small-scale mining licence	Large-scale mining licence	Royalty for small-scale mining (%)
Precious metallic minerals, base metals, and other metal-like minerals	25–40 Birr/km ² (1.8–3 USD/km ²)	40–200 Birr/km ² (3–14.7 USD/km ²)	150–300 Birr/km ² (11–22 USD/km ²)	1–3
Semi-precious stones	20–50 Birr/km ² (1.5–3.7 USD/km ²)	40–150 Birr/km ² (3–11 USD/km ²)	100–300 Birr/km ² (7.4–22 USD/km ²)	n/a
Dimensional stones	30–60 Birr/km ² (2.2–4.4 USD/km ²)	50–120 Birr/km ² (3.7–9 USD/km ²)	150–300 Birr/km ² (11–22 USD/km ²)	1–2.5
Industrial minerals	20–50 Birr/km ² (1.5–3.7 USD/km ²)	30–100 Birr/km ² (2.2–7.4 USD/km ²)	100–250 Birr/km ² (7.4–18 USD/km ²)	1–2.5

Source: 1. Tigray Water Resources, Mines and Energy Bureau
2. Tigray Investment Office
3. Ministry of Mines and Energy
4. KPMG in Ethiopia interview programme, 2009

Investment overview

The indicative size of investment for marble and granite processing plant with an annual capacity of 120,000 m³ is estimated at USD9–11 million.⁴

Appendices

- 1 KPMG in Ethiopia interview programme
- 2 Secondary research



Appendix 1: KPMG in Ethiopia interview programme

Companies

- Gelila Shoes Factory plc
- Sheba Leather Industry plc
- Helimex plc
- Abergelle Slaughterhouse
- Amal Trading plc
- Vitcon plc
- Luna Export Slaughterhouse
- Gobe Farms
- Axum Hotel
- Messebo Cement Factory
- Horn of Africa Travel Agency
- KC AKF (De Heus International)
- Dimma Beekeeping Development and Honey Processing plc
- Comel Honey Processing
- Dairy and Milk Processing Farm (Mulu Negash)
- Dairy and Milk Processing Farm (Tadesa Sebho)
- Ezana Mining Development
- Jittu Horticulture
- Saba Dimensional Stones plc
- Ethiopian Airlines
- EFFORT Group
- IlanTOT plc
- Golden Rose plc
- Ethio-Flora
- Gheralta Lodge

Government organisations

- Ministry of Industry and Trade
- Ministry of Agriculture and Rural Development
- Ministry of Mines and Energy
- Ministry of Culture and Tourism
- National Bank of Ethiopia
- Mekelle City Administration
- Tigray Bureau of Agriculture and Rural Development
- Tigray Water Resources, Mines and Energy Bureau (TWRMEB))

Government organisations

- Ethiopian Investment Agency (EIA)
- Ethiopian Leather Industries Association (ELIA)
- Ethiopian Horticulture Development Agency
- Ethiopian Horticulture Producer Exporters Association (EHPEA)
- Ethiopian Meat Producer and Exporters Association
- Ethiopian Honey and Beeswax Producers and Exporters Association
- Tigray Investment Promotion Office
- Tigray Agricultural Marketing Promotion Agency (TAMPA)
- Millennium Village Project

Appendix 2: Secondary research

- MCI Working Paper No. 10/2009 *Investment promotion in Mekelle, Ethiopia*, October 2009
- Addis Ababa Chamber of Commerce and Sectoral Associations, *Livestock Resource Potentials: Constraints and Opportunities for Intervention by the Private Sector*, 2008
- Ministry of Culture and Tourism, *Ethiopian Sustainable Tourism Development Project*, 2009
- Tigray Tourism, Tigray Investment Office, 2009
- Tigray State Bureau of Water, Mineral and Energy Resources, *Mineral Resource Potential of Tigray Region*, August 2006
- Ministry of Agriculture and Rural Development, *Agricultural investment potential of Ethiopia*, March 2009
- Mekelle City Administration, *City Profile of Mekelle (1872–2009)*, October 2009
- Tigray Tourism, 2009
- Tigray Tourism Commission, *Tigray: The Open-Air Museum*, 2008
- Enderta Dry Midland Livelihood Zone: *Livelihood Profile*, October 2006
- International Livestock Research Institute (ILRI), Addis Ababa, Ethiopia, *Improving Productivity and Market Success (IPMS) of Ethiopian Farmers Project*, 2008
- World Economic Forum, International Bank for Reconstruction and Development (World Bank), African Development Bank, *The Africa Competitiveness Report*, 2009
- World Bank *Ethiopia at a Glance*, 2008
- World Bank, *Doing Business in Ethiopia 2010*, 2009
- World Bank Ethiopia *Toward the Competition Frontier. Strategies for Improving Ethiopia's Investment Climate*, June 2009
- National Bank of Ethiopia *National Bank Report 2007-2008*
- African Development Bank *Country Portfolio Performance Report*, October 2008
- Africa News, *Ethiopia: Tourists number doubles*, March 19, 2008
- Ministry of Mines and Energy Federal Democratic Republic Ethiopia, *Investing in the Minerals Industry of Ethiopia*, 2007
- Ministry of Agriculture, *Oilseed business opportunities in Ethiopia* The Hague, May 2007
- Regional Agricultural Trade Expansion Support Programme, *Cotton-Textile – Apparel Value Chain Report for Ethiopia*
- Federal Democratic Republic of Ethiopia, Ministry of Mining and Energy, *Investment Opportunities in Industrial Minerals of Ethiopia*, Addis Ababa, June 2006
- United Nations Conference on Trade and Development *World Investment Directory. Africa*, 2008
- OECD, *Africa Economic Outlook*, 2009
- IMF website
- Economist Intelligence Unit forecasts, 2009
- CIA
- Census

Contacts

Stefan Dierks, Partner

KPMG Strategy Group
Moscow, Russia
stefandierks@kpmg.ru

Peter Korolev, Manager

KPMG Strategy Group
Moscow, Russia
pkorolev@kpmg.ru

Olga Andreeva, Associate

KPMG Strategy Group
Moscow Russia
oandreeva@kpmg.ru

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2010 KPMG International Cooperative ("KPMG International"), a Swiss entity. Member firms of the KPMG network of independent firms are affiliated with KPMG International. KPMG International provides no client services. No member firm has any authority to obligate or bind KPMG International or any other member firm vis-à-vis third parties, nor does KPMG International have any such authority to obligate or bind any member firm. All rights reserved. Printed in the United Kingdom.

KPMG and the KPMG logo are registered trademarks of KPMG International Cooperative ("KPMG International"), a Swiss entity.

Designed and produced by KPMG LLP (UK)'s Design Services.

Photography credit: Front cover and other report photographs Marie George. Photograph on page 30 Olga Andreeva

Publication name: Mekelle, Ethiopia

Publication number: RRD-194303

Publication date: June 2010

Printed on recycled material.

