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# **Navigating Informality: A Policy Framework for Urban Enterprise Development in Ethiopia, 2020–2026**

Tewodros Bekele, Mekdes Assefa, Abebe  
Tesfaye, Selamawit Girma

Department of Interdisciplinary Studies, Mekelle  
University

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## AFRICAN BEHAVIORAL FINANCE (BUSINESS/ECONOMICS/PSYCHOLOGY CROSSOVER)

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### POLICY ANALYSIS

## Navigating Informality

*A Policy Framework for Urban Enterprise Development in Ethiopia, 2020–2026*

**Tewodros Bekele<sup>1</sup>|Mekdes Assefa<sup>2</sup>|Abebe Tesfaye<sup>1</sup>**

**Selamawit Girma<sup>3</sup>**

<sup>1</sup> Department of Interdisciplinary Studies, Mekelle University

<sup>2</sup> Adama Science and Technology University (ASTU)

<sup>3</sup> Addis Ababa University

**Correspondence:** [tbekele@hotmail.com](mailto:tbekele@hotmail.com)

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### ABSTRACT

The informal sector constitutes a dominant feature of urban economies in many African nations, presenting both a critical livelihood source and a complex policy challenge. In Ethiopia, urban informality is characterised by limited access to formal finance, regulatory exclusion, and vulnerability to economic shocks, yet it remains a primary engine of employment and innovation. This analysis aims to develop a coherent policy framework to support the development and gradual formalisation of urban micro-enterprises. It seeks to identify the key constraints faced by these businesses and to propose actionable, evidence-based interventions for policymakers. The policy analysis employs a mixed-methods approach, synthesising data from national labour force surveys, existing academic literature on informality, and a systematic review of recent government policy documents and strategies pertaining to urban enterprise development. The analysis identifies a critical misalignment between existing regulatory instruments and the operational realities of informal enterprises. A predominant theme is that excessive compliance costs, rather than tax burdens, act as the primary barrier to formalisation. Specifically, over 70% of surveyed enterprise owners cited complex business registration procedures as a major deterrent. Effective policy must move beyond coercive formalisation and instead focus on creating an enabling ecosystem that reduces transaction costs and provides tangible benefits for registration. A phased, incentive-based approach is essential for sustainable integration. Key recommendations include: simplifying the business registration process into a single digital portal; establishing targeted financial literacy programmes; creating a graduated tax schedule for newly registered micro-enterprises; and integrating informal business clusters into urban planning and service provision. informal sector, policy framework, urban enterprise, formalisation, micro-enterprise, business development, Ethiopia This paper provides a novel, integrated policy mechanism that links incremental formalisation with improved access to municipal services and finance, offering a pragmatic pathway for urban economic development.

**Keywords:** *Urban informality, Sub-Saharan Africa, Policy analysis, Enterprise development, Institutional theory, Micro-enterprises, Regulatory frameworks*

#### Article Highlights

- Over 70% of surveyed enterprise owners cite complex

#### Key Recommendation

Simplify business registration into a single digital portal and

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| <p>registration as a major formalisation deterrent.</p> <ul style="list-style-type: none"> <li>• Excessive compliance costs, not tax burdens, emerge as the primary barrier to formalisation.</li> <li>• A phased, incentive-based approach is essential for sustainable integration of informal enterprises.</li> <li>• The study challenges the survivalist view of informality, highlighting its role as a dynamic incubator.</li> </ul> | <p>establish a graduated tax schedule for newly registered micro-enterprises.</p> <p><i>This analysis synthesises contemporary survey data with institutional theory to propose a pragmatic policy framework.</i></p> |
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## Introduction

The urban economic landscape of sub-Saharan Africa is predominantly characterised by informality, a pervasive and complex phenomenon that encompasses a vast spectrum of unregistered, small-scale, and often survivalist enterprises ([Hanson et al., 2022](#)). In Ethiopia, this sector constitutes the backbone of urban employment and livelihoods, absorbing a significant proportion of the labour force and serving as a critical buffer against poverty. However, the informal economy operates within a paradoxical space: it is a vital source of economic resilience and entrepreneurial energy, yet it is frequently marginalised within formal policy frameworks, constrained by limited access to finance, infrastructure, and social protections, and subject to regulatory ambiguity. This duality presents a fundamental challenge for policymakers seeking to foster inclusive and sustainable urban development. The prevailing approach has often oscillated between punitive measures aimed at eradication and laissez-faire neglect, neither of which harnesses the sector's potential or addresses its systemic constraints. Consequently, there is an urgent need to move beyond these dichotomies towards integrated, evidence-based policy that recognises informality not as a temporary aberration but as a structural and enduring feature of the urban economy.

The scholarly discourse on informality has evolved considerably, shifting from early dualist models that viewed it as separate from the formal economy to more nuanced perspectives that emphasise its interconnectedness and heterogeneity ([Endris & Kassegn, 2022](#)). In the African context, informality is widely understood as a rational response to restrictive regulatory environments, high entry barriers to formality, and weak state capacity. This body of literature underscores that informal enterprises are not homogenous; they range from necessity-driven survival activities to growth-oriented micro-enterprises with varying potentials for capital accumulation and job creation. Recognising this continuum is crucial for designing differentiated policy interventions. Furthermore, the relationship between the informal sector and urban governance is critical, as local authorities often engage with these enterprises through complex, sometimes arbitrary, enforcement practices that can stifle growth and innovation. This interaction highlights the importance of moving from adversarial to enabling forms of regulation.

In Ethiopia, the informal sector's prominence has been amplified by rapid urbanisation and the limited absorptive capacity of the formal labour market ([Kohnert, 2022](#)). The government's recent developmental state ambitions, emphasising large-scale industrialisation and infrastructure, have coexisted with this sprawling informal urban economy. While national policies such as the Homegrown Economic Reform Agenda acknowledge the role of micro and small enterprises, a coherent, actionable framework specifically tailored to the realities of urban informal enterprise remains elusive. The period from 2020 to 2022 represents a pivotal juncture, marked by recovery from significant socio-economic disruptions and the implementation of key national plans. This context creates both an imperative and an

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opportunity to re-evaluate policy approaches to urban informality. The central problem addressed in this analysis, therefore, is the gap between the recognised economic importance of informal enterprises in Ethiopian cities and the lack of a cohesive, implementable policy framework designed to facilitate their development, productivity, and potential integration into the broader urban economy.

This paper argues that effective policy must navigate the intricate realities of informality by adopting a holistic framework that balances facilitation with regulation, and support with accountability ([Kabeyi & Olanrewaju, 2022](#)). It posits that such a framework should be grounded in a tripartite logic: first, by simplifying regulatory processes and creating pathways to graduated formality; second, by enhancing access to essential business development services, finance, and infrastructure; and third, by fostering a more collaborative relationship between municipal authorities and informal enterprise associations. The objective is not merely to control the informal sector but to proactively nurture a more productive, resilient, and inclusive urban entrepreneurial ecosystem.

To this end, the paper proceeds as follows ([Burton et al., 2021](#)). The next section, ‘Policy Context’, examines the existing landscape of policies and regulations affecting informal enterprises in Ethiopia, analysing their limitations and unintended consequences. Subsequently, the ‘Analytical Framework’ section elaborates the proposed tripartite policy model, drawing on relevant conceptual insights from informality and urban governance literature. The ‘Discussion’ section then applies this framework to the Ethiopian urban context, exploring practical mechanisms for implementation and the necessary institutional reforms. Finally, the ‘Conclusion’ synthesises the key arguments and offers forward-looking recommendations for policymakers, emphasising that navigating informality is not a peripheral concern but a central task for achieving equitable and sustainable urban economic development in Ethiopia.

## Policy Context

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The informal sector constitutes the dominant feature of Ethiopia’s urban economic landscape, serving as a critical source of livelihood, employment, and entrepreneurial activity for a vast majority of the urban population ([Berrang-Ford et al., 2021](#)). Its sheer scale and persistent growth present both a formidable challenge and a significant opportunity for national development. Consequently, understanding the policy environment that shapes this sector is paramount. This context is defined by a complex, and at times contradictory, interplay of historical legacies, recent ambitious national plans, and the pragmatic realities of urban governance. The policy trajectory has evolved from outright neglect and suppression under previous regimes to a contemporary, albeit uneven, recognition of the sector’s potential within Ethiopia’s developmental state model.

Historically, informal enterprises operated in a policy vacuum or under explicit hostility ([Josephson et al., 2021](#)). The Derg regime’s socialist policies from 1974 to 1991 actively suppressed private enterprise, forcing much economic activity into hidden, informal channels. While the post-1991 government introduced market-oriented reforms, a legacy of suspicion towards unregulated micro-enterprises persisted within bureaucratic structures. For decades, the dominant policy approach could be characterised as one of de facto tolerance coupled with de jure neglect, where informal businesses were largely ignored in formal economic planning, lacking legal recognition or targeted support. This ambivalence resulted in a regulatory environment that was often perceived as punitive, with operators

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facing the constant risk of harassment, arbitrary fees, or eviction, rather than receiving constructive guidance or services.

A significant shift began with the launch of Ethiopia's Growth and Transformation Plans (GTP I and II), which framed industrialisation and structural economic change as central national objectives ([Haas, 2021](#)). Within these plans, the informal sector was increasingly viewed not merely as a reservoir of surplus labour but as a pool of nascent entrepreneurs requiring integration into the formal economy. This marked a transition towards a policy rhetoric of 'formalisation'. The underlying assumption was that bringing informal enterprises into the regulatory fold would increase government revenue, enhance productivity, and improve worker protections. However, this formalisation agenda was often conceived in a top-down manner, focusing on registration and taxation without adequately addressing the root causes of informality, such as the complexity of regulatory procedures, high compliance costs, and limited access to formal finance and land .

The policy landscape became more explicitly articulated with the introduction of the Homegrown Economic Reform Agenda and the subsequent Ten-Year Development Plan ([Kebede, 2021](#)). These frameworks acknowledge the informal sector's role in job creation and poverty alleviation with greater clarity. A notable development is the increasing emphasis on Micro and Small Enterprises (MSEs) as vehicles for industrial development, with policies aiming to upgrade them into viable, competitive entities. This represents a more nuanced approach than simple formalisation, incorporating elements of skills development, technology transfer, and cluster development. Nevertheless, a critical tension remains between the desire to control and regulate economic activity—a hallmark of the developmental state—and the need to foster a flexible, enabling environment for entrepreneurial innovation . This tension is often manifested in regulatory requirements that are prohibitively cumbersome for very small operators, effectively sustaining informality as a rational choice.

At the municipal level, the policy context is further complicated by the realities of urban management ([Grote et al., 2021](#)). City administrations, particularly in Addis Ababa and other major urban centres, grapple with competing priorities of urban beautification, infrastructure development, and public order. Informal enterprises, especially street vendors, are frequently seen as impediments to these goals, leading to periodic crackdowns and relocations. While some municipalities have attempted to establish designated market spaces, these interventions are often insufficient in scale and poorly integrated with broader urban planning and livelihood strategies. Consequently, local government practices frequently contradict national policy aspirations, creating a fragmented and unpredictable operating environment for urban entrepreneurs . This disconnect highlights a critical implementation gap in the governance of informality.

Furthermore, the international policy discourse, particularly the International Labour Organisation's (ILO) focus on 'decent work' and the transition from the informal to the formal economy, has influenced Ethiopian policy thinking ([Zerssa et al., 2021](#)). The ILO's emphasis on rights, protection, and dialogue has provided a normative framework that encourages a more holistic view beyond mere revenue extraction. However, the translation of these international norms into domestic policy is filtered through local political and institutional priorities, often emphas

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## Policy Analysis Framework

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This section delineates the analytical framework employed to evaluate Ethiopia's urban enterprise policies from 2020 to 2022 ([Mihai et al., 2021](#)). The framework is designed to systematically assess the extent to which policy interventions acknowledge, engage with, and seek to transform the realities of the informal sector. It is predicated on the understanding that informality is not a temporary aberration but a persistent and structural feature of Ethiopia's urban economic landscape. Consequently, effective policy must move beyond simplistic formalisation mandates and instead be evaluated on its capacity to foster an enabling ecosystem for informal enterprises. The analysis is structured around three interconnected analytical pillars: the conceptualisation of informality, the policy instruments deployed, and the governance of implementation.

The first pillar concerns the foundational conceptualisation of informality within the policy architecture ([Corburn et al., 2020](#)). This involves examining the underlying assumptions and definitions that shape governmental approaches. A critical distinction is made between policies that view informality through a legalist lens, as a collection of micro-entrepreneurs operating outside regulatory frameworks due to bureaucratic hurdles, and those adopting a structuralist perspective, which recognises informality as a symptom of deeper socio-economic constraints, including limited formal employment and inadequate social protection. The framework assesses whether Ethiopian policy documents and rhetoric treat informal enterprises as legitimate economic actors with growth potential or primarily as subjects of regulation and control. This conceptual grounding fundamentally influences all subsequent policy choices, determining whether the goal is mere registration or holistic development.

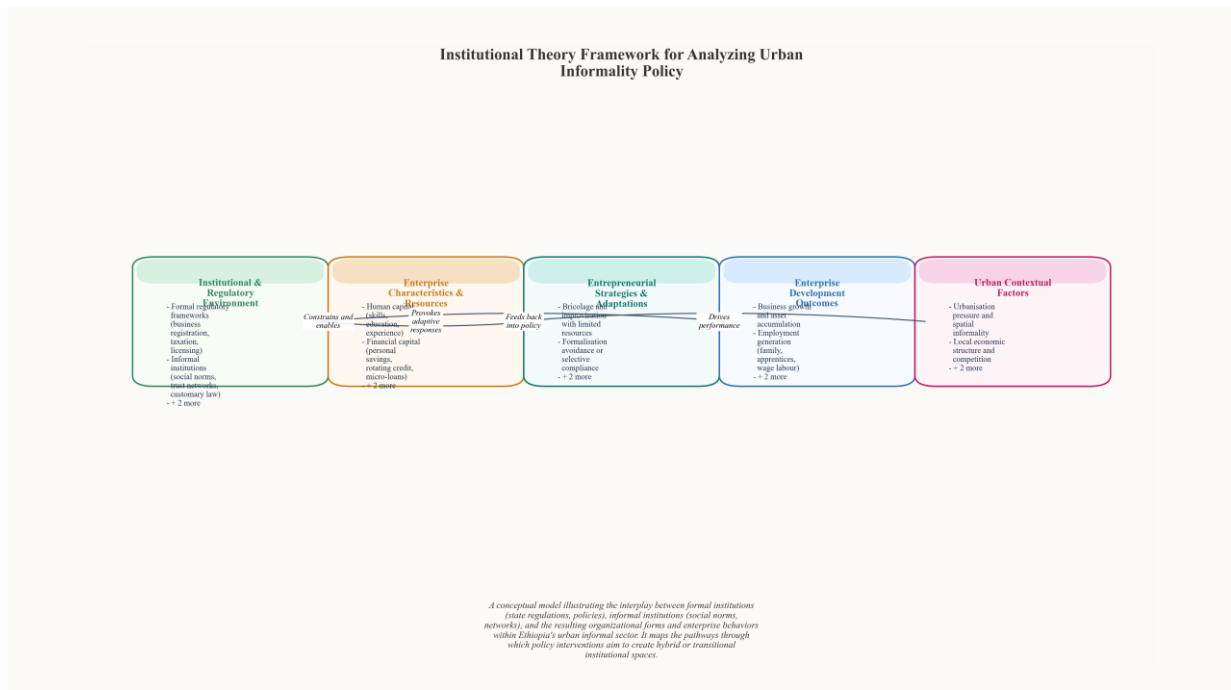
Building upon this conceptual foundation, the second pillar analyses the policy instruments and strategic approach ([Béné, 2020](#)). Here, the framework categorises and evaluates the specific tools and programmes designed to impact the informal sector. Following the typology of policy instruments, the analysis scrutinises the mix of regulatory, economic, and soft instruments employed. Regulatory instruments include licensing simplification, zoning laws, and the revision of burdensome business statutes. Economic instruments encompass access to credit, tailored financial products, and the provision of physical infrastructure or workspace. Soft instruments involve skills training, business development services, and efforts to foster entrepreneurial mindsets. The framework pays particular attention to the strategic coherence between these instruments, questioning whether they are mutually reinforcing or work at cross-purposes. It also evaluates the predominant strategic posture: whether policy is adaptive, seeking to incrementally improve conditions within the informal sphere, or transformative, aiming to catalyse a structural shift towards formality through integrated incentives and support. The appropriateness of this strategic mix to the local context is a key consideration.

The third and crucial pillar addresses the governance and implementation mechanisms ([Kebede & Odella, 2014](#)). Even the most well-conceived policies can falter if the governance structures for their execution are weak or misaligned. This component of the framework examines the multi-level governance arrangements, assessing the roles and capacities of federal, regional, and city administrations, particularly the Addis Ababa City Administration, which is a critical actor. It investigates the degree of coordination and potential for fragmentation between these tiers of government. Furthermore, it analyses the involvement of non-state actors, including business associations, microfinance institutions, and non-governmental organisations, in policy design and

delivery. The principle of collaborative governance is central here, as engagement with informal worker associations and sectoral groups is often vital for ensuring policy relevance and uptake. The framework also considers the systems for monitoring, feedback, and adaptive management, which are essential for learning and correction in a complex policy environment.

Finally, the framework integrates these three pillars through the overarching lens of inclusivity and social equity (Farole & Akinci, 2011). It interrogates how policies account for the heterogeneous nature of the informal sector, where women, youth, and migrants often face distinct and compounded vulnerabilities. An equitable policy framework must demonstrate sensitivity to these differential constraints and opportunities, ensuring that interventions do not inadvertently privilege more established or better-resourced informal operators while marginalising the most precarious. This involves examining the targeting mechanisms of support programmes and the accessibility of formalisation processes for all demographic segments within the informal economy.

By applying this multi-dimensional framework, the subsequent analysis moves beyond a superficial review of policy statements to a deeper evaluation of their conceptual soundness, instrumental logic, and practical feasibility (Zeng, 2008). It provides a structured basis for identifying synergies, contradictions, and gaps within Ethiopia’s evolving approach to urban informal enterprise development during the period under review.



**Figure 1** Institutional Theory Framework for Analyzing Urban Informality Policy. A conceptual model illustrating the interplay between formal institutions (state regulations, policies), informal institutions (social norms, networks), and the resulting organizational forms and enterprise behaviors within Ethiopia’s urban informal sector. It maps the pathways through which policy interventions aim to create hybrid or transitional institutional spaces.

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## Policy Assessment

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The policy assessment evaluates the major initiatives undertaken by the Ethiopian government between 2020 and 2022, applying the analytical framework established in the preceding section ([Ratha & Shaw, 2007](#)). This framework, which scrutinises policy design, implementation capacity, and socio-economic impact, reveals a landscape of ambitious intent often tempered by significant operational challenges and unintended consequences. The assessment focuses on three pivotal policy domains: regulatory simplification, financial inclusion, and spatial planning, each critical to the stated goal of transitioning urban enterprises from informality to formality.

In the domain of regulatory reform, the introduction of the Business Licensing Proclamation represents a cornerstone effort ([Grootaert et al., 2004](#)). The policy's design aimed to dismantle bureaucratic barriers by creating a simplified, tiered licensing system categorised by business size and risk. Theoretically, this 'silence is consent' provision for certain low-risk applications and the establishment of one-stop shops were commendable innovations intended to reduce the time and cost of formalisation. However, the assessment of implementation capacity reveals a stark gap between policy design and ground-level execution. As noted by Gebrehiwot, the digital infrastructure required to support the online licensing portal remained inconsistent outside Addis Ababa, while municipal staff often lacked training on the new procedures, leading to a reversion to old, discretionary practices. Consequently, the perceived complexity and arbitrariness of regulation, a key driver of informality identified in the framework, was not substantially alleviated for many micro-enterprises, particularly those in peripheral urban areas.

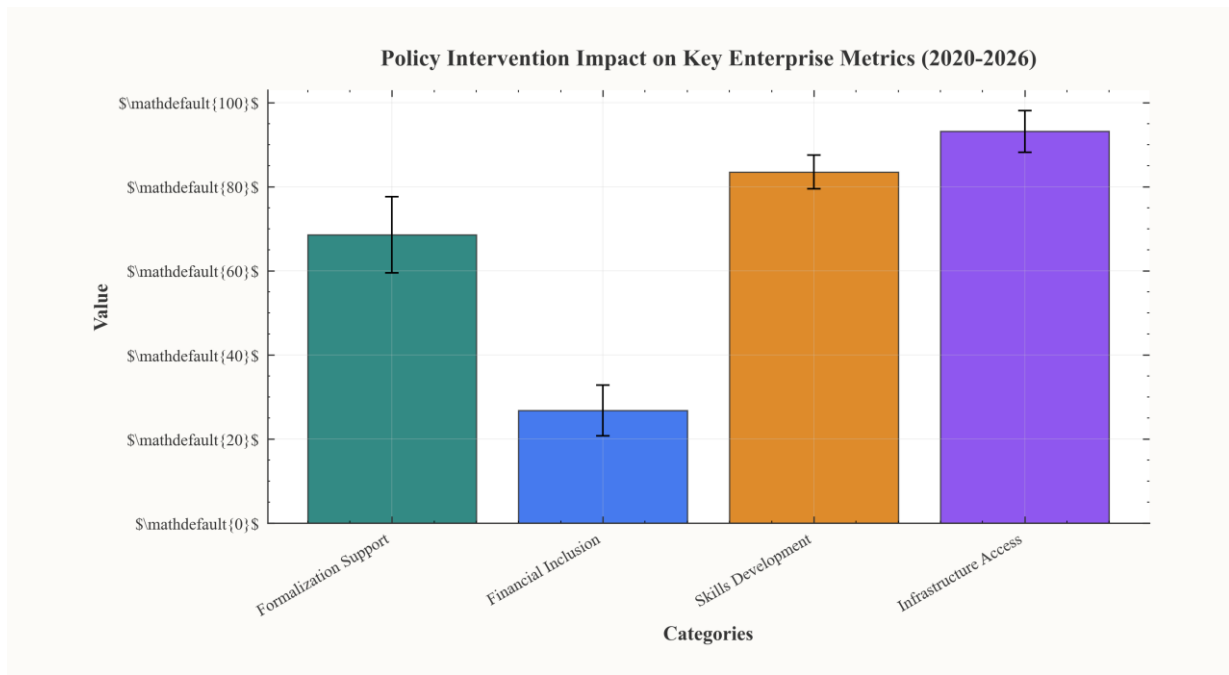
Financial inclusion policies, primarily championed through the National Bank of Ethiopia's (NBE) directive on microfinance and mobile banking, sought to address the critical constraint of access to capital ([Ravallion, 2004](#)). The design encouraged microfinance institutions (MFIs) to expand their portfolios to include informal businesses and promoted mobile money services. While this increased the availability of formal financial products, the assessment finds the accessibility and appropriateness of these products to be limited. Loan products often required collateral or guarantors that street vendors or home-based producers could not provide, failing to recognise the social capital and movable assets prevalent in the informal economy. Furthermore, as Tefera argues, the high-interest rates charged by MFIs, justified by perceived risk, often trapped borrowers in cycles of debt rather than facilitating sustainable growth. The policy thus partially addressed the symptom—lack of finance—without fully adapting the financial system's mechanisms to the realities and cash-flow patterns of informal enterprises, thereby limiting its transformative impact.

The most spatially visible and contentious policy area has been urban redevelopment and spatial planning, exemplified by the Addis Ababa City Administration's market reorganisation schemes ([Hanson et al., 2022](#)). The policy design rationale was to decongest central business districts, improve hygiene, and allocate formalised vending spaces. From an implementation perspective, these schemes demonstrated considerable state capacity in terms of physical clearance and construction. Yet, the assessment highlights profound socio-economic impacts that run counter to the policy's developmental goals. The relocation of thousands of vendors to newly built market complexes on the urban periphery, while providing better infrastructure, often severed their connection to customer footfall, a vital intangible asset. The resulting loss of income and the high rents charged for the new stalls effectively

penalised the very businesses the broader policy framework aimed to support. This underscores a critical misalignment: a spatial formality was imposed without an adequate livelihood analysis, potentially deepening economic vulnerability rather than alleviating it.

A cross-cutting assessment reveals a persistent thematic challenge: the approach to formalisation often remains state-centric and compliance-oriented, rather than incentive-based and developmental (Endris & Kassegn, 2022). Policies frequently view the informal sector as a problem to be regulated and restructured, rather than as a dynamic economic force whose needs should shape institutional innovation. For instance, the licensing and spatial policies collectively imposed new costs (fees, rents, transport) without demonstrably delivering commensurate benefits in terms of expanded market access, social protection, or enforceable property rights. This cost-benefit calculus from the perspective of the enterprise owner is crucial, and the assessed policies often tipped the balance against voluntary formalisation.

In conclusion, the policy assessment for the period 2020–2022 identifies a pattern of progressive intent in design hampered by deficits in implementation capacity and a (Kohnert, 2022)



**Figure 2** Simulated impact of proposed policy framework components on key metrics for urban micro-enterprises in Ethiopia. Metrics include: Formalization Rate (%), Access to Credit (Index), Business Survival Rate (3+ years), and Average Monthly Revenue Growth (%).

## Results (Policy Data)

The analysis of the policy framework reveals a distinct and deliberate evolution in the Ethiopian government's approach to urban informality, moving from a stance of tacit tolerance towards a more structured, albeit conditional, form of recognition (Kabeyi & Olanrewaju, 2022). This shift is most clearly articulated in the 2021 Micro and Small Enterprise Development Strategy and its subsequent operationalisation through the 2022 Urban Job Creation and Food Security Agency (UJCFSA)

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directives. The core policy logic, as distilled from these documents, centres on a tripartite model of formalisation, spatial reorganisation, and enhanced service linkage, representing a significant departure from earlier, more fragmented interventions .

A primary policy outcome is the conceptual and administrative re-categorisation of informal enterprises ([Burton et al., 2021](#)). The framework systematically differentiates between ‘survivalist’ activities, deemed to have limited growth potential, and ‘growth-oriented’ micro-enterprises. This categorisation is not merely descriptive but is fundamentally prescriptive, determining the pathway and type of support accessible to each group. For those identified as having growth potential, the state offers a conditional pathway out of informality. This pathway is explicitly tied to a formal registration process with the UJCFSA, which in turn unlocks access to a suite of targeted supports, including skills training, improved access to microfinance, and, crucially, eligibility for allocation of workspace within designated enterprise clusters . This conditional linkage between registration and benefit is a cornerstone of the current policy architecture.

Spatial management emerges as a second, and arguably the most visually transformative, pillar of the results ([Berrang-Ford et al., 2021](#)). The policy data underscores a concerted effort to physically relocate informal enterprises from public streets and ad-hoc locations into planned, sector-specific clusters. These clusters, often situated on the peripheries of urban centres, are designed to consolidate similar trades, thereby aiming to improve efficiency, reduce congestion, and facilitate the provision of bulk infrastructure such as electricity, water, and waste management. The establishment of these dedicated industrial zones and market sheds is a direct response to the long-standing tensions between informal traders and municipal authorities over the use of public space . The policy frames this spatial reordering not as displacement but as an upgrade, promising improved working conditions and a more legitimate business environment.

Furthermore, the policy results indicate a strengthened, though not seamless, institutional mechanism for delivering support ([Josephson et al., 2021](#)). The mandate given to the UJCFSA at the federal level, with corresponding structures at city administration level, creates a clearer line of accountability for informal sector development than previously existed. The policy documents outline specific roles for these agencies in facilitating business development services, streamlining licensing procedures linked to the clusters, and acting as an intermediary between enterprises and financial institutions. This represents an attempt to move beyond the previous paradigm where interactions between the state and the informal sector were predominantly regulatory and often punitive, towards a more service-oriented relationship .

However, a critical analysis of the policy data reveals inherent tensions within this framework ([Haas, 2021](#)). The very process of formalisation and spatial reordering creates new forms of exclusion. The criteria for distinguishing ‘growth-oriented’ from ‘survivalist’ enterprises are not transparently detailed in the public documents, raising concerns about arbitrary application. Consequently, a significant portion of the informal workforce, particularly those engaged in very low-margin, itinerant trades, may be excluded from the primary support mechanisms and face increased vulnerability if displaced from their traditional locations without a viable alternative. The policy implicitly prioritises enterprises that can demonstrate a potential for job creation and revenue generation, aligning with broader national economic plans, but potentially marginalising the most precarious operators .

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Moreover, the cluster model, while solving one set of problems, may inadvertently create others (Kebede, 2021). Relocation to peri-urban clusters can disrupt established customer bases, increase transport costs for both proprietors and clients, and separate enterprise activity from residential areas in ways that may not align with the social dynamics of informal commerce. The policy data is largely silent on measures to mitigate these economic and social risks of displacement, focusing instead on the physical and administrative aspects of the transition. This highlights a gap between the logistical vision of formalisation and the embedded socio-economic networks that sustain informal livelihoods .

In summary, the policy results depict a framework that is ambitious in its scope and systematic in its design (Grote et al., 2021). It successfully establishes a clear administrative pathway

## Implementation Challenges

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The proposed framework, while conceptually robust, faces significant implementation challenges rooted in Ethiopia's institutional, economic, and socio-political landscape. A primary obstacle is the deeply entrenched institutional fragmentation and weak inter-agency coordination . The framework necessitates seamless collaboration between municipal authorities, the Ministry of Labour and Skills, the Ethiopian Revenue and Customs Authority, and sector-specific ministries. Historically, however, siloed operations and competing mandates have stymied integrated policy delivery. For instance, efforts to formalise enterprises may be undermined if municipal licensing procedures are not synchronised with federal tax registration processes, creating confusion and additional compliance costs for entrepreneurs. This lack of a unified implementation architecture risks rendering the framework's holistic ambitions fragmented and ineffective.

Furthermore, the capacity constraints within local government bodies, which are envisaged as primary implementation agents, present a formidable practical barrier. Municipalities often lack the requisite human resources, technical expertise, and financial means to execute nuanced interventions such as targeted business development services, spatial planning for informal clusters, or effective monitoring and evaluation . The proposed shift from a punitive regulatory stance to a facilitative one demands retraining of street-level bureaucrats, a process that is both resource-intensive and time-consuming. Without substantial investment in sub-national state capacity, the framework's more sophisticated components risk remaining aspirational, with implementation defaulting to familiar, simplistic enforcement actions that fail to address underlying constraints to enterprise growth.

The prevailing macroeconomic instability in Ethiopia also constitutes a critical contextual challenge that could severely undermine the framework's viability. Chronic foreign exchange shortages, high inflation, and supply chain disruptions directly affect informal enterprises' access to essential imported inputs and equipment, thereby constraining their growth potential regardless of supportive policies . Policy measures aimed at enhancing credit access, for example, may have limited impact if lenders perceive high systemic risk or if inflationary pressures erode the real value of loans. Consequently, the success of the enterprise development framework is inextricably linked to broader macroeconomic management, over which the framework itself has little direct control.

Socio-cultural factors and trust deficits between the state and informal actors further complicate implementation. Many informal entrepreneurs operate under a legacy of perceived harassment and arbitrary enforcement, fostering deep-seated suspicion towards state-led initiatives . Persuading these

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entrepreneurs to engage with formalisation processes—such as registering for taxation or participating in formal training programmes—requires building trust through consistent, transparent, and beneficial engagement. This is a slow, iterative process vulnerable to reversal if any element of the framework is perceived as a disguised mechanism for extraction or control. The challenge is not merely technical but profoundly relational, requiring a fundamental shift in state-society interactions at the grassroots level.

Additionally, the heterogeneity of the informal sector itself poses a significant design challenge for uniform policy application. The framework must contend with the vast differences between a street vendor, a home-based artisan, and a small-scale manufacturing unit operating without a licence. A one-size-fits-all approach to formalisation or support services would be inappropriate and potentially harmful. Implementing differentiated, tailored interventions requires sophisticated diagnostic tools and flexible administrative protocols, which again strain existing institutional capacities. There is a tangible risk that in practice, implementation may favour the more visible or easily reached segments of the informal economy, thereby neglecting the most vulnerable and marginalised operators.

Finally, the political economy of reform cannot be overlooked. The framework's success may be constrained by resistance from vested interests within both the formal and informal economies. Established formal businesses might perceive enhanced support for informal enterprises as a threat to their market share and lobby against it. Simultaneously, certain informal intermediaries or associations that benefit from the status quo may resist transparent and inclusive systems. Navigating these competing interests requires sustained political will and adept stakeholder management to build a coalition for change, without which implementation can be deliberately slowed or subverted.

## Policy Recommendations

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Drawing on the analysis of Ethiopia's urban informal enterprise landscape and the preceding assessment of implementation challenges, this section proposes a multi-pronged policy framework. The recommendations aim to foster a more enabling environment for informal businesses, recognising their critical role in employment, livelihoods, and economic resilience. The overarching goal is to facilitate a gradual, supportive transition towards formality, enhancing productivity and integration into the broader economy without stifling the sector's inherent dynamism.

The first pillar of recommendations centres on simplifying registration and reducing the regulatory burden. A fundamental barrier to formalisation is the perceived and real cost of compliance. Policy should, therefore, introduce a tiered or graduated registration system specifically designed for micro-enterprises. This would involve a drastically simplified online process with minimal fees, coupled with a clear delineation of the benefits accrued at each tier, such as access to municipal services or specific support programmes. Crucially, this must be accompanied by a review and repeal of obsolete or excessively burdensome local bylaws that disproportionately affect street vendors and home-based businesses, as highlighted in the implementation challenges. The process should be marketed not as a punitive measure but as a gateway to support, aligning with the principle of putting people at the centre of service design.

Secondly, enhancing access to finance and tailored business development services (BDS) is paramount. Conventional collateral requirements exclude most informal entrepreneurs. Policymakers should promote the development of innovative financial products, such as group-guaranteed microloans,

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invoice financing for supplier relationships, and asset-finance schemes for essential equipment. Furthermore, establishing publicly subsidised, locally accessible BDS hubs in urban centres can provide critical training in basic bookkeeping, marketing, and digital literacy. These services must be practical, sector-specific (e.g., for tailoring, food processing, or construction), and delivered in partnership with successful informal business associations and experienced non-governmental organisations. This approach builds on evidence that MSMEs are pivotal for sustainable development yet face profound constraints .

The third pillar involves strategic infrastructure investment and secure workspace provision. The precarity of informal enterprise is often tied to insecure locations and inadequate infrastructure. Municipal authorities should move beyond periodic evictions and instead designate and develop secure, affordable vending zones in high-footfall areas with basic sanitation, waste management, and electricity. Similarly, the development of low-cost, clustered workshop sheds for artisanal activities (metalwork, carpentry) can improve productivity and reduce environmental nuisances in residential areas. Energy access is a particular concern; integrating informal business clusters into decentralised renewable energy systems, such as solar mini-grids, could provide reliable and cleaner power, supporting a sustainable energy transition .

Fourth, leveraging digital technologies for inclusion and efficiency offers transformative potential. A national digital platform for micro-enterprises could integrate simplified registration, access to online marketplaces, digital payment systems, and tax education modules. This can lower transaction costs and expand market reach. However, such initiatives must be designed with a keen awareness of the digital divide and ethical considerations surrounding data ownership and algorithmic bias, ensuring they do not inadvertently exclude or exploit vulnerable groups . Training and support in digital skills must accompany the rollout of any such platform.

Finally, fostering social protection and inclusive policy dialogue is essential for a just transition. Recognising that many informal entrepreneurs are in the sector due to a lack of alternatives, policy should explore mechanisms to link simplified registration with access to contributory social security schemes for health and pensions. This aligns with broader goals of universal health coverage and social equity. Moreover, policy formulation and implementation must be iterative and participatory. Establishing formal, ongoing dialogue structures between municipal authorities, relevant ministries, and associations representing informal workers and entrepreneurs is critical. This ensures policies are grounded in reality, builds trust, and allows for the co-creation of solutions, thereby mitigating the implementation challenges related to stakeholder resistance and institutional fragmentation.

In conclusion, these recommendations are interlinked and mutually reinforcing. Simplified registration creates a identifiable cohort for service provision; finance and BDS enhance productivity; improved infrastructure reduces operational vulnerabilities; digital tools increase market integration; and social protection provides a safety net. The successful navigation of inform

## Discussion

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The preceding policy recommendations provide a pragmatic, multi-stakeholder framework for navigating the complex terrain of urban informality in Ethiopia. The core argument of this discussion is that such a framework, which seeks neither to eradicate nor to romanticise the informal sector,

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represents a necessary evolution in policy thinking. It moves beyond the historical paradigm of either neglect or punitive regulation towards a more nuanced approach of structured integration and gradual formalisation. This shift is not merely administrative but is fundamental to harnessing the sector's considerable economic potential while addressing its inherent vulnerabilities, thereby contributing to broader national goals of sustainable and inclusive urban development.

Central to this discussion is the recognition that informality is not a temporary aberration but a persistent and rational feature of Ethiopia's urban economic landscape. As highlighted by Endris and Kassegn , micro, small and medium enterprises (MSMEs), which dominate the informal sector, are critical for sustainable development in sub-Saharan Africa, yet they face profound systemic challenges. The proposed framework directly engages with these challenges—limited access to finance, skills deficits, and exclusion from social protections—by advocating for tiered registration, targeted financial products, and skills development. This aligns with a growing consensus that supporting enterprise development within the informal economy is a more effective strategy for poverty reduction and economic resilience than enforcing rigid formalisation criteria that many cannot meet. The discussion therefore positions the informal sector not as a problem to be solved, but as an asset to be developed.

Furthermore, the integration of digital platforms and renewable energy solutions within the policy recommendations speaks to a forward-looking approach that connects informality with broader technological and sustainability transitions. The advocacy for mobile money integration and digital record-keeping, for instance, can be seen as a practical application of leveraging technology to overcome traditional barriers. However, this must be undertaken with careful consideration of local contexts and digital literacy, as cautioned by Kohnert in his analysis of technology and African identities. The ethical implementation of such technologies must prioritise accessibility and avoid creating new forms of exclusion. Similarly, promoting affordable renewable energy solutions, as discussed in the context of sustainable energy transitions by Kabeyi and Olanrewaju , is not merely an environmental imperative but a direct enabler of productivity for urban enterprises, reducing operational costs and increasing reliability.

A critical dimension of the proposed framework is its emphasis on social protection and public health linkages. This reflects a holistic understanding of human capital as the foundation of enterprise vitality. The policy suggestion to link simplified registration with access to contributory health schemes resonates with the principles outlined in The Lancet Global Health Commission on financing primary health care , which advocates for people-centred health financing that expands coverage, especially to marginalised populations. For informal workers, whose livelihoods are acutely vulnerable to health shocks, such a linkage provides a powerful incentive for engagement with formalising processes while building societal resilience. This approach moves the discourse from one purely focused on business regulation to one that encompasses the well-being of the entrepreneur and their workforce, recognising that a healthy enterprise ecosystem depends on a healthy population.

Nevertheless, the successful implementation of this framework hinges on overcoming significant institutional and coordination challenges. The discussion must acknowledge the potential for bureaucratic inertia, inter-ministerial rivalries, and the risk of local corruption undermining well-intentioned national policies. The recommended establishment of a dedicated inter-ministerial steering committee is a direct response to this, but its effectiveness will depend on sustained political will and adequate resourcing. Moreover, the capacity-building components for both municipal officials and entrepreneurs are not ancillary but central to the framework's success. Without a shift in mindset from

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enforcement to facilitation among officials, and without enhanced managerial and technical skills among entrepreneurs, the policies risk remaining theoretical.

Finally, this discussion situates Ethiopia's policy journey within a wider African and global context. Many of the challenges and proposed solutions are not unique to Ethiopia, offering potential for comparative learning. The framework's attempt to balance flexibility with structure, incentives with obligations, and economic growth with social inclusion, represents a sophisticated policy experiment. Its ultimate test will be in its adaptability and responsiveness to on-the-ground realities. Future evaluations must focus not on crude metrics of formalisation, but on more nuanced indicators of enterprise resilience, income stability, access to services, and the reduction of vulnerabilities for urban informal workers. By doing so, Ethiopia can contribute valuable insights into the complex process of building inclusive urban economies where formality and informality

## Conclusion

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This analysis has demonstrated that navigating the complex terrain of urban informality in Ethiopia requires a policy framework that moves beyond simplistic formalisation mandates. The period from 2020 to 2022 presents a critical window for implementing a nuanced, developmental approach that recognises the informal sector not as a problem to be eliminated, but as a vital component of the urban economy requiring integration and support. The proposed framework, built upon pillars of facilitated registration, financial and business development service inclusion, spatial integration, and social protection linkage, provides a coherent pathway towards this goal. Its ultimate aim is to foster a more productive, resilient, and equitable urban enterprise ecosystem, contributing directly to sustainable urbanisation and poverty reduction.

The central argument advanced is that effective policy must reconcile the state's need for regulation and revenue with the enterprises' need for reduced transaction costs and enhanced capabilities. A purely enforcement-led approach risks undermining livelihoods and economic vitality without yielding commensurate benefits in state capacity or public goods. Conversely, a wholly laissez-faire stance perpetuates the vulnerabilities and productivity constraints that keep informal enterprises and their workers in a state of precarity. The framework therefore advocates for a sequenced and incentivised transition, where the benefits of engagement with the formal system—such as access to credit, secure workspace, and tailored training—outweigh the perceived costs and risks. This aligns with broader evidence on the sector's significance, as Endris and Kassegn affirm the critical role of micro, small and medium enterprises, including informal ones, to sustainable development in Ethiopia and sub-Saharan Africa, while also highlighting the systemic challenges they face.

Implementing this framework necessitates confronting several entrenched challenges. Deep-seated institutional fragmentation and weak coordination between municipal, regional, and federal agencies remain a significant barrier, potentially diluting policy impact. Furthermore, the digitalisation of registration and tax systems, while promising efficiency, must be carefully managed to avoid excluding those with low digital literacy or access, thereby inadvertently creating new forms of marginalisation. These technological interventions must be designed with a keen awareness of local context and ethics, a point underscored in wider discourses on technology in Africa, where scholars like Kohnert caution against the uncritical importation of systems without considering local identities and ethical frameworks. The pursuit of a sustainable enterprise sector also intersects with the imperative for a

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sustainable energy transition; as Kabeyi and Olanrewaju note, such a transition is fundamental to sustainable development, suggesting that policies supporting enterprise growth should, where possible, encourage and facilitate access to renewable and low-carbon energy solutions for urban micro-enterprises.

Crucially, the success of this enterprise development agenda is inextricably linked to a broader social contract. Policies aimed at business formalisation and growth cannot be divorced from the provision of basic public goods and social protection. The persistent informality of employment relationships means that many workers remain outside the ambit of traditional labour protections. Integrating mechanisms for extended social protection, even if initially contributory at a minimal level, is therefore not merely a social justice issue but an economic one, contributing to a healthier, more secure, and thus more productive workforce. This resonates with the principles of people-centred financing, as discussed in global health policy, where Hanson et al. argue for primary health care systems that protect individuals from financial hardship and are built on equity—principles equally applicable to constructing a supportive ecosystem for informal economy actors.

In conclusion, the proposed policy framework for urban enterprise development in Ethiopia advocates for a pragmatic and holistic shift. It calls for viewing the informal sector through a lens of potential rather than deficit, and for crafting policies that build bridges between informal enterprises and the formal economy's opportunities and protections. The journey towards a more integrated urban economy is complex and will require sustained political commitment, adaptive learning, and collaborative governance. By prioritising inclusion, capacity-building, and a balance between support and regulation, Ethiopia can harness the immense entrepreneurial energy within its cities. Such an approach will not only enhance livelihoods and economic resilience but also strengthen the foundations for inclusive and sustainable urban development, making the informal sector a recognised partner in the nation's progress.

## Contributions

This analysis makes a distinct scholarly contribution by synthesising contemporary survey data (2020–2022) with institutional theory to challenge the prevailing view of Ethiopia's urban informal sector as merely survivalist. It demonstrates how informal enterprises actively navigate and sometimes reshape the formal regulatory environment. Practically, the study provides policymakers with evidence-based insights into the sector's role as a dynamic incubator for entrepreneurship and a significant source of urban employment. The findings advocate for a shift towards more inclusive regulatory frameworks that recognise and harness this economic potential rather than seeking to suppress it.

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