



**CAPITAL MARKET OPERATION IN ETHIOPIA: POTENTIAL
CHALLENGES AND OPPORTUNITIES**

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DECLARATION

I, Kalkidan Daniel declare that the work included in this research proposal is my work carried out by me under the guidance of my advisor. The research proposal has not been submitted to other higher education institutions for another purpose. I also declare that I have adhered to the principle of academic honesty and integrity and have not misrepresented fabricated or falsified any idea/data/fact/source in my research proposal submission. The source used is dually acknowledged. I understand that any violation of academic integrity will be the cause for disciplinary action by the university.

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ADDIS ABABA UNIVERSITY SCHOOL OF COMMERCE
CORPORATE FINANCE: SPECIALITY IN INVESTMENT MANAGEMENT
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LIST OF ACRONYMS

- ASE** – African Securities Exchange
- CAPM** – Capital Asset Pricing Model
- CBE** – Commercial Bank of Ethiopia
- CML** – Capital Market Line
- ECMA** – Ethiopian Capital Market Authority
- EMDEs** – Emerging Markets and Developing Economies
- EMH** – Efficient Market Hypothesis
- FDI** – Foreign Direct Investment
- FSC** – Financial Stability Council
- GDP** – Gross Domestic Product
- IFRS** – International Financial Reporting Standards
- IMF** – International Monetary Fund
- IPO** – Initial Public Offering
- MoF** – Ministry of Finance (Ethiopia)
- NBE** – National Bank of Ethiopia
- OECD** – Organization for Economic Co-operation and Development
- PBC** – Public Enterprise Holding and Administration Agency
- SEZ** – Special Economic Zone
- SME** – Small and Medium Enterprises
- UNCTAD** – United Nations Conference on Trade and Development
- WB** – World Bank
- WEF** – World Economic Forum

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ABSTRACT

This study examines the operational challenges and challenges that exist in the capital market formulation in Ethiopia, a country that is implementing significant financial reforms but has no well-established capital market. The study aims to assess the preparedness of regulatory, institutional, and technological infrastructures, government, private financial institutions, and the academia. With a descriptive research design, the research collected both quantitative and qualitative data employing structured questionnaires and semi-structured interviews. Under the questionnaires, 137 of the respondents belonging to regulatory authorities, the Ethiopian Securities Exchange (ESX), private commercial banks, trainees at the School of Commerce (SOC), and university researchers took part. In addition, five qualitative interviews were also gathered from ESX's senior experts and private banks with finance, investment, and advisory capabilities. Evidence shows that the capital market infrastructural setup in Ethiopia continues to exist and is plagued by such low-level legal structures, technology platforms, financial literacy, institutional coordination, and small professional numbers. The prevalence of the reality of there being no functioning stock exchange and restricted access to information regarding the market. Yet, the study identifies potential opportunities like significant government support, establishment of the Ethiopian Capital Market Authority (ECMA), and the growing interests of institutional stakeholders. The study concludes with a suggestion for the formal launching of a stock exchange, investment in electronic trading platforms with a focus on targeted investment, promotion of financial literacy, tax benefits, and stronger collaboration between financial institutions, regulatory bodies, and academia to have an efficient and sustainable capital market in Ethiopia.

KEYWORDS: Capital Market, challenge, ECMA (Ethiopian capital market authority), ESX (Ethiopian securities exchange, opportunities)

CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND OF THE STUDY

The capital markets are where people in need of extra money look for others looking to invest their surplus. They are also places where participants can manage and spread their risks (Chishoim, 2009). And according to (Gitman, 2007) A capital market is any market which deals with the purchase or sale of long term securities like stocks, bonds and other financial instruments that are used in raising funds for projects that are long term in nature and which are measured in years. These markets are very important in the transfer of funds to in productive the uses economy and hence contribute to growth of economies through efficient allocation of resources. Capital markets are of two main types depending on the nature of market, primary market and secondary market. The primary market is that market which is concerned with the issuance of new securities and the secondary market is the market which deals with already existing securities.

Various scholars articulate definitions of capital markets contingent upon their individual perspectives. Contemporary literature posits that stock markets render services that enhance economic growth and facilitate the attainment of national objectives. In accordance with the research conducted by (Ruecker 2011), the financial market constitutes an arena in which financial assets are generated or transferred, effectively channeling capital from those who do not require immediate utilization to those who do possess such needs. It serves as a venue for the transaction of diverse financial instruments, including stocks, shares, and bonds (Gomez, 2013), and exemplifies a mechanism for efficient financial intermediation. Among the global stock markets, the London and New York stock exchanges are recognized as the oldest and most systematically organized in the world. As illustrated by (Edosa 2014), these markets provide essential facilities for stock brokers, investors, and corporations to engage in stock trading. Various instruments such as bonds, stocks, commodities, derivatives, options, currencies, and others are actively traded (Mishkim and Eakins, 2006).

Financing of development projects is a critical area that is well addressed through capital markets as a mechanism of raising capital for long term projects, industrial developments and other investments. As it plays an important role in fostering economical sustainability. Unlike money market instruments, which have original maturities of less than a year, financial instruments in the capital market have maturities of more than a year. The stock market, bond market, mortgage market, and futures market are all parts of the capital market (Rose 2001).

In the global scenario, there is capital market which facilitates the buying and selling of financial assets like shares, debentures and the like. They allow both business and government to raise long-term capital, an integral part of building infrastructure, embarking on expansion and facilitating technological advancement (Levine, 2005). As in well-functioning markets, the security market through sensational purchases and sales of securities in the secondary market takes the responsibility of valuation and ensuring the liquidity of these securities (Fama, 1970).

For growing economies, capital markets are important for helping the economy grow and bringing in foreign investment. Aizenman (2003) says that countries with strong capital markets often have higher economic growth because they use resources better and can gather savings for useful investments. In Africa stock markets seem to be at different levels of growth and development, as is the economic profile as well as challenges that each country faces. For instance, countries such as South Africa, Kenya, and Nigeria have gone a long way in establishing and developing their capital markets and such countries serve as important case studies for several other countries in Africa. According to Ngugi (2003), South Africa's Johannesburg Stock Exchange (JSE) is one of the best in world ready for use backed up with various financial instruments sought after by investors across the globe. The launch of green bonds and mobile trading platforms at the Nairobi Securities Exchange in Kenya has also broadened the access to the market (Omondi, 2019). Nevertheless, several other African markets face hurdles such as underdeveloped markets, lack of liquidity, poor legal enforcement, and insufficient investors' confidence (Yartey & Adjasi, 2007). However, the degree of optimism and possibilities would also be immense, considering an active strategy for collaboration, technological advancement in various sectors would lead to a robust capital markets in Africa.

Capital markets are significant financial mechanisms by which long-term securities such as stocks, bonds, and derivatives are exchanged. They are central to economic development through

mobilization of savings, efficient capital allocation, and investment prospects (Mishkin & Eakins, 2006). Capital markets provide companies with the channel by which they are able to acquire funding for expansion while governments have access to funding for government undertakings via issuance of bonds. Capital markets are typically divided into primary markets, which sell new securities, and secondary markets, where outstanding securities are traded among investors (Fabozzi & Modigliani, 2013).

Efficiently operating capital market relies on a number of factors, including regulatory institutions, financial intermediaries, infrastructural technology, and market agents. Stock exchanges, investment banks, brokerage firms, and regulating bodies collaborate to enhance market efficiency and transparency. Efficient operation of capital markets achieves economic stability through encouraging investment, risk diversification, and intermediation (Levine, 1997). However, no matter what role they play, capital markets, particularly those of developing nations, are linked with a variety of challenges that hamper their development.

Capital markets play a vital role in economic development by providing fund mobilization and investment. However, the capital markets at times face different challenges that may reduce their efficiency and level of development. The liquidity issue is one of the challenges facing the capital markets, particularly in the emerging markets such as the ones in Africa. Low market liquidity increases the difficulty of investors buying or selling securities without having to experience huge price variations, thereby reducing the level of market efficiency (Yartey & Adjasi, 2007).

Another significant challenge is regulatory and legal barriers. Poor legal frameworks, absence of uniform regulation enforcement, and weak investor protection discourage participation in capital markets. Without a proper regulatory framework, market participants will be hesitant to invest due to fear of fraud and unfair business practices (Ruecker, 2011).

Besides, market infrastructure vulnerabilities pose challenges to capital market development. Vulnerabilities in robust technological platforms and efficient trading systems can impede market accessibility and operating efficiency. In the lack of developed infrastructure, trade

becomes cumbersome, making capital markets unattractive to foreign and domestic investors (Gomez, 2013).

Investor confidence is yet another primary driver impacting participation in capital markets. Low levels of financial literacy and a lack of trust in market manipulation reduce confidence in the system, thus leading to participation levels being low. Investor education on how the market works and the transparency of transactions are key steps to foster confidence and investment (Mishkin & Eakins, 2006).

Furthermore, macroeconomic instability will negatively impact capital markets. The sources of inflation, foreign exchange volatility, and political instability bring uncertainty, and this dissuades long-term investment. Macro-economic stability is paramount to the long-run growth of capital markets (Zena, 2021).

To address such problems, the governments and the regulatory authorities have to implement policies that foster confidence in the markets, enhance institutional and legal infrastructures, and promote investor education. By refining market infrastructure, ensuring transparency of regulations, and promoting financial education, capital markets can be streamlined and attract both domestic and foreign investment.

Ethiopia for instance once had an early commodity market called the Addis Ababa Share Dealing Group, set up in 1965. But following the socialist regime that took power in 1974, this was soon closed down as the country embraced a command economy. Since the 1990s, with Ethiopia moving towards market-based economic reforms to reboot the country's economy, calls for introducing a capital market have increased (Tiruneh, 2012); largely on private demand and by the development partners. With historic bias to fortress banking, fueled by absence of capital market; last mile access to alternative financial resources was hindered resulting to overreliance on the banking system which unfortunately is an organism with relatively short-term financing. But the absence of a capital market has resulted in financial difficulties, reliance on short-term banking financing, and restricted access to alternative investment options (World Bank, 2020).

Although the capital market in Ethiopia is at an embryonic stage and plays fundamental role in promoting economic growth by absorbing long term funds, savings mobilization and efficient allocation of resource, (World Bank, 2020), Recent developments indicate trends towards the creation of a capital market. The government of Ethiopia enacted the Capital Market Proclamation No. 1248/2021 into law to authorize the Ethiopian Capital Market Authority (ECMA) to regulate and build the securities market of the country (Muluken, 2021).

Over the last two decades, Ethiopia has one of the fastest growing economies in the world with an average GDP growth rate of over 10.3% between 2005 and 2015. Unfortunately, the gains have failed to translate into structural transformation as financial sector remains weak and private sector cannot be sustained (World Bank 2018).

Ethiopia has a long way to go in terms of building its capital market but feats this promise a number of obstacles. Important bottlenecks are the absence of sufficient financial literacy, adequate legal and regulatory framework, as well as weak finance systems. Moreover, the inadequate presence of pension funds, insurance companies and other institutional investors, that normally help stock markets in other second economies, remains another hurdle (Yartey & Adjasi, 2007). In addition, political instability and macroeconomic challenges for problems in the development of a working securities market have been other concerns which have been added to interest rates, inflation and foreign exchange shortages (Zena, 2021).

In spite these issues, research by (Tessema 2003) suggests that a healthy Ethiopian securities market could offer improved capital mobilization, effective capital allocation, economic sector savings mobilization, increased corporate finance flexibility, the development of an efficient financial system, and long-term funding. In addition, (Tessema 2003) suggested that the establishment of a capital market in Ethiopia could benefit the country's accounting and auditing standards, provide useful tools for monetary and fiscal policy, support an open and effective privatization process, stimulate the growth of the private sector, boost economic expansion, reduce unemployment, and ultimately reduce poverty.

Contrarily, the development of capital market is a major prospect for Ethiopia. Though a capital market may have the potential of increasing financial inclusion by encouraging more people to participate in wealth creation by investments. It may also bring in foreign direct investment (FDI) through a clear and controlled system for providing investors the necessary mechanism to

fund large scale projects such as infrastructure, manufacturing and energy etc. (Burger & Warnock 2006) In addition, a robust capital market can support Ethiopia industrialization agenda by channeling long term capital to private sector (Mulatu, 2016).

As stated by Dawit (2019), a stock market needs people resources with the necessary training, reliable accounting data, and technological infrastructure. In order to safeguard the rights of creditors and investors and to ensure transparency in the administration of listed companies, a legislative framework and governance system are also required. The foundation of the stock market is timely, transparent, and trustworthy public data. The expansion of stock markets in every economy depends on the flow of long-term capital, which is maintained by pension funds and life insurance firms. These entities, however, lack the capacity to provide the long-term capital needed for a stock market.

Realizing these opportunities the Ethiopian government enacted the Capital Market Proclamation No. 1248/2021 to authorize Ethiopian Capital Market Authority ((ECMA) which is under authority of PBC with guaranteed development and regulation functionalized securities market. As such, the ECMA is expected to provide equity in market operation by ensuring the fairness and transparency of efficiency leading the economy transformation in the country (Muluken, 2021).

1.2 STATEMENT OF THE PROBLEM

One significant component of the financial system that is crucial to the growth of the economy is the capital market. It is a method for effectively mobilizing resources and allocating them to profitable ventures. Risk sharing, money allocation, investment facilities, company finance, and capital raising are just a few of the many opportunities it offers to governments, corporations, and investors (Madura, 2014). The capital market facilitates the flow of money and the distribution of resources, both of which are critical to the growth and sustainability of the economy. Stock markets are used by developed nations to finance their corporations, emerging nations to raise long-term capital for massive industrializations that result in economic growth and development, and African nations to trade shares and distribute resource they have developed stock markets to finance their corporations, and all of these countries have established capital markets (Mulatu, 2016).

Ethiopia has moved to work towards the development of a capital market as part of its financial reform document. Yet, in order for such a market to operate effectively and sustainably in the long run, there are some issues that need to be dealt with along with harnessing the opportunities that are at hand. Ethiopia is reported, as one of the fastest growing economies in Africa, with wide potential for socioeconomic change. But it modernized without a capital market, which is a key tool in "dissolving" domestic savings, attracting Foreign Direct Investments, and funding long-run projects (Chewaka, 2014). Bekele (2021) has found over-reliance on such a market to be largely dependent on traditional banking systems which are largely unsuitable to deal with long-term financial requirements for business or infrastructure alike. Consequently, this has been a bar to the widening of the economy and its potential for investors and entrepreneurs in Ethiopia.

Ethiopia possesses the biggest African economy but still finds itself among the smallest number of nations lacking a well-developed capital market. Although the development of a capital market has long been targeted, its lack has constrained the capacity of corporations to access long-term funding and individuals to invest for diversification (World Bank, 2022). The economy has relied considerably on bank-based finance, which lacks enough to meet the growing demand for funds in productive sectors and creates limited private sector development, limited employment creation, and untapped entrepreneurial potential (IMF, 2023).

Recent reforms by the government, such as the issuance of the Capital Market Proclamation No. 1248/2021 and institutionalization of the Ethiopian Capital Market Authority (ECMA) in 2022, are a milestone development to fill in these structural gaps (NBE, 2023). In addition, final preparations are underway for the operationalization of the Ethiopian Securities Exchange (ESX), which is set to become operational in the near future (African Financial Markets Initiative, 2023). However, opening a market of this size in an emerging bank-driven financial system has been plagued by issues including low financial literacy, poor technological infrastructure, weak institutional capacity, and poor governance and transparency concerns (UNCTAD, 2022; OECD, 2023).

If these bottlenecks are not solved, Ethiopia risks missing out on the potential benefits of a capital market mobilization of domestic savings, improvement in resource allocation, and

attraction of foreign investment that are essential for achieving structural transformation and sustaining economic growth (World Bank, 2022; AfDB, 2024). The need thus exists to explore the challenges and opportunities of Ethiopia's capital market development in operation because it will provide valuable lessons to policymakers, regulators, and investors.

Despite these issues, the growth of Ethiopia's capital market is a wonderful opportunity. Having a capital market would provide businesses alternative sources of finance, increase public participation in economic activities, and attract FDI (Desta, 2022). The expansion of Ethiopia's capital market is bound to enhance financial inclusion, create investor confidence, and facilitate overall economic growth (Biazin Waktola, 2022). Besides, digital financial services growth could help bridge infrastructure gaps to facilitate faster and less expensive market development. Reforms in the financial sector in Ethiopia and the country's economy potential make a compelling argument for capital market development (African Development Bank, 2021).

While existing literature has analyzed the theoretical foundations and potential benefits of a capital market in Ethiopia, there are few that have reported empirical evidence of operational issues, institutional ability, and readiness of the stakeholders. Most literature has adopted theoretical analysis or policy suggestions without utilizing grounded data from participants in the market and regulators. This study bridges this critical knowledge gap by producing both quantitative and qualitative information on the operational challenges, capacity constraints, and market perceptions of operationalizing Ethiopia's capital market. Through that, it assists in closing the policy intention-execution reality gap. The study offers policymakers, financial institutions, and investors valuable insights on how to better understand the systemic challenges and opportunities. Lastly, this study supports strategic development of a solid capital market that can help fill the financing gap of Ethiopia, stimulate private sector growth, and foster sustainable economic development.

1.3 BASIC RESEARCH QUESTIONS

1. What are the key operational challenges to operate a capital market in Ethiopia, considering regulatory, institutional, infrastructural, human resource, and investor-related aspects?
2. How ready are financial institutions, regulators, investors, etc., to offer supporting facilities required for functioning a capital market in Ethiopia?
3. What opportunities can a capital market provides for economic growth, investment, and enhancing financial inclusion in Ethiopia?
4. What are strategic measures to be taken in order to conquer operational challenges and improve the prospects of Ethiopia's capital market?

1.4 OBJECTIVE OF THE STUDY

1.4.1 General Objective

The general objective of this study is to analyze the operational challenges and the opportunities of a capital market in Ethiopia, and so present practical recommendations to encourage its efficient implementation and sustainability.

1.4.2 Specific Objective

The specific objective of this study is :

1. To identify and analyze the key operational challenges affecting the operation of a capital market in Ethiopia, with specific focus on regulatory, institutional, infrastructural, human resource, and investor-related factors.
2. To assess readiness and ability of core stakeholders, such as financial institutions, regulators, and investors, to facilitate a working capital market.
3. To identify opportunities for growing economic development, investments, and financial inclusion using a capital market.
4. To formulate some practical suggestions to overcome the operational constraints and increase the potential of the Ethiopian capital market

1.5 SIGNIFICANCE OF THE STUDY

This study will have a significant implication, as it addresses one of the major development concerns of Ethiopia's economy, targeting the operational challenges and opportunities that will serve to operate a capital market. The policy makers will be benefited since the findings guide them in formulating policies in overcoming the existing bottlenecks such as regulatory weaknesses, low financial literacy, and inadequate financial infrastructure. It also provides great insight into the understanding of various private sector stakeholders on capital market opportunities that might come through an effective capital market in terms of better access to long-term financing and economic diversification.

It therefore provides insight into the risks and benefits associated with capital market development in Ethiopia for financial institutions, regulatory bodies, and investors. It will, hence, be important to academics in filling the gap in the literature regarding comprehensive analysis of the financial landscape within which Ethiopian financial markets play the functions assigned to them by the source of literature toward informing successive studies in finance, economics, and development. Conclusively, the contribution of the Ethiopian economy in attaining stability and growth through better resource allocation, investment attractiveness, and facilitating investment activities.

1.6 SCOPE OF THE STUDY

The paper deals with the capital market operations in Ethiopia amidst prospective challenges and opportunities likely to be facing it. In this research work, an understanding of the current status of the capital market, examination of regulatory frameworks, and the readiness of the major stakeholders that constitute investors, financial institutions, and regulatory bodies become limited in scope. While the study tends to analyze some dimensions of the capital market operations, such as market structure and governance, it does not go further to conduct an exhaustive global review of good practices in the capital market, or their applications in Ethiopia directly. Moreover, it narrows down to socioeconomically contextualized challenges at the legal, institutional level-finite financial literacy, capacity in limits of regulatory infrastructure limits- and points at a number of opportunities like unused investment potential and also economic growth together with regional integration. The data collection restricts its data sources only to

primary and secondary sources; it contains interviews with expert people present within the industry in policy documents or academic literature. The study excludes real-time performance of market and or detailed financial modeling, given the capital market in Ethiopian is in the nascent stages. These delimitations ensure that the study remains focused on providing actionable insights for policymakers and other stakeholders who are committed to developing a sound and sustainable capital market in Ethiopia.

1.7 LIMITATIONS OF THE STUDY

One of the most critical limitations of this study is related to the unavailability of reliable and complete data because of a non-existence or completely operational capital market in the country. Limitations may thus occur concerning depth and accuracy in analysis. Moreover, the focus on operational challenges may lead to the overlooking of emerging or unforeseen problems that could face the market while it is being developed. Another limitation is the dynamic nature of the regulatory and political environment in Ethiopia, which may affect the relevance and applicability of the findings over time.

The study is further limited in comparative analyses with operational markets in similar economies by the fact that Ethiopia is a country without a functioning capital market.

There could also be a limitation on stakeholder bias, in the sense that interviews or surveys conducted may reflect subjective opinions guided by personal or institutional interests. Finally, resource and time constraints may limit the study from being able to do more extensive field research or include broader international perspectives and advanced quantitative analyses.

1.8 DEFINITION OF TERMS

Capital Market: A financial market in which buyers and sellers trade financial securities, such as stocks and bonds, and this is often long-term in nature for raising funds for economic activities.

Operational Challenges: The operational obstacles and impediments in the way of setting up and managing a functional capital market, which relates to regulatory, infrastructural, and institutional challenges.

Opportunities: These are the possible benefits and advantages that one can get from a capital

market, including increasing financial inclusion, investment growth, and economic diversification.

Financial Literacy: Knowledge and an ability to understand concepts of personal finance that are sufficiently developed to enable informed decisions about the use of capital market instruments by an investor.

Securities Exchange: An institution or system in which securities are bought and sold, notably providing a fair, efficient, and transparent marketplace.

Institutional Investors: These are organizations that invest enormously in financial markets and include pension funds, insurance companies, and mutual funds. They play a critical role in the development of capital markets.

Regulatory Framework: Laws, rules, and regulations laid down for the operation of the capital market to ensure it always operates fairly in a transparent way that will provide protection to its investors.

Macroeconomic Stability: The state of an economy in which the level of inflation, rate of interest, and rate of exchange are relatively stable; a pre-requisite for the development of a strong capital market.

Financial Inclusion: It is a process in which financial services are available and affordable to all households and corporate entities, including the underprivileged sections.

1.9 ORGANIZATION OF THE PAPER

The paper is organized into six sections and attempts a systematic exploration of the operational challenges and opportunities of capital market development in Ethiopia. The Introduction provides an overview of the research topic, objectives, and significance of the study, apart from the identification of research questions that will guide the study. The Literature Review covers related theoretical and empirical studies on capital markets, pinpoints gaps in the existing literature, and builds a conceptual framework relevant to the context of Ethiopia. This section also covers the methodology through research design, methods of data collection, and analytical tools employed to investigate various challenges and opportunities pertaining to capital market operation in Ethiopia.

The section of Findings and Discussion presents the results and, in this regard, analyzes the findings against both theoretical frameworks and empirical evidence. The Conclusion and

Recommendations summarize key findings into actionable recommendations for the stakeholders involved, such as policymakers and financial institutions, while suggesting avenues for future research. Finally, the References section lists all cited works, adhering to the Harvard referencing style, to ensure academic rigor. Additional supporting materials, such as raw data or supplementary analyses, are provided in the Appendices, enriching the paper's overall content and utility.

CHAPTER TWO

2 LITERATURE REVIEW

This chapter provides a comprehensive review of recent research on the operational challenges and opportunities for the Ethiopian capital market. It seeks to establish a theoretical and practical foundation for addressing the research question while identifying gaps in prior studies.

2.1 THEORETICAL REVIEW

2.1.1 Capital Market Theory

Capital market theory provides a framework relationship that dictates how financial markets operate in allocating scarce resources efficiently. The risk-return tradeoff is the theory's theoretical foundation, under which rationality and equilibrium in the market are emphasized. The Capital Market Line (CML) describes the risk-return tradeoff of portfolios of a combination of the risk-free asset and a risky asset portfolio in the market (Sharpe, 1964; Lintner, 1965). CAPM has been widened over time to encompass additional factors of risk, besides systematic risk, such as liquidity constraint and market inefficiency, particularly in emerging economies (Fama & French, 2004; Zhang, 2020). Current studies highlight that employing local market dynamics, behavioral finance insights, and technology advancements can further the applicability of CAPM in emerging economies (Li & Wang, 2021; Brown & Taylor, 2023).

Capital markets help develop the economy by allowing financial intermediation and investments. Capital markets are described by Mishkin and Eakins (2015) as the major channels of savers and borrowers, allocating capital to productive investments such as infrastructure, industry, and technology. Their effectiveness, however, depends on liquidity, investor confidence, and robust regulatory structures (Burger & Warnock, 2006; Zhang, 2020). Recent research highlights that technology innovations, such as blockchain and fintech, enhance market transparency and access and therefore make capital markets more efficient (Arner et al., 2021; Chen et al., 2022). Technological developments in artificial intelligence (AI) in financial analytics also enhance the precision of market forecasts and risk assessment, enhancing market resilience (Gupta & Sharma, 2023).

Despite their significance, capital markets, especially in emerging markets, are faced with various challenges. Lack of liquidity distorts proper trading, discouraging participation. Zhang (2020) refers to the manner in which liquidity restrictions distort risk-return equilibrium in emerging markets, requiring localized CAPM adjustments. Inadequate legal infrastructure, uneven application, and lack of investor protection discourage investment. Sound institutions are increasingly needed to deliver investor confidence (World Bank, 2021; Johnson et al., 2023). Inefficient trading platforms and clearing systems also limit efficiency. The emerging economies are greatly benefited by the inclusion of financial technology (FinTech), which enhances trading mechanisms and enhances market access (Arner et al., 2021; Chen et al., 2022).

Market participation is dependent on financial literacy and transparency, and low investor education and fear of manipulation reduce participation. Evidence indicates government initiatives to improve investor awareness and public confidence (OECD, 2021; Thompson & Lewis, 2022). Macroeconomic factors such as inflation, exchange rate volatility, and political uncertainty create uncertainty in markets, deterring long-term investment. Evidence shows that regulatory protection and macroeconomic policy stability are crucial to capital market resilience (IMF, 2022; Garcia & Patel, 2023).

Ethiopia is currently relying on its banking system for intermediation of finances, limiting long-term funding options. The growth of a capital market provides an opportunity to address this gap through the mobilization of domestic savings as well as foreign direct investment (FDI). Seeing this, the government of Ethiopia enacted the Capital Market Proclamation No. 1248/2021, which conferred authority to the Ethiopian Capital Market Authority (ECMA) for regulation and controlling the operations of the market (Muluken, 2021). Evidence proves that the market will become more transparent, there will be improved investor confidence, and the foundation of overall economic transformation of Ethiopia (World Bank, 2021; Assefa & Mekonnen, 2023).

Capital markets are central to economic growth as they provide investment opportunities, reallocate resources, and create financial stability. Yet, market imperfections in the form of liquidity shortages, regulatory weaknesses, and macroeconomic shocks still hamper growth, especially in developing countries such as Ethiopia. Fixing them requires strong institutions, digitalization of the infrastructure, and policies that instill investor confidence. Lessons from the

development of the regulatory framework for a capital market in Ethiopia from the best practice can ensure sustainable growth of the financial sector.

2.1.2 Efficient-Market Hypothesis (EMH)

Market efficiency is a situation in which market prices reflect all available information. Efficient Market Hypothesis (EMH) was introduced by Fama (1970), and he divided efficiency into weak, semi-strong, and strong. The weak efficiency suggests that prices reflect all information on past trading, i.e., past prices and volumes. The semi-strong form includes publicly available information, i.e., financial reports and macroeconomic data. The strong form assumes that all information, public and private, is fully reflected in market prices and that it is impossible for investors to consistently achieve more than market returns.

To investors, EMH suggests that active management techniques will not outperform the market in the long term. Passively managed techniques, for instance, by investing in index funds, yield a more tangible outcome (Malkiel, 2021). To policymakers, EMH speaks to the importance of transparency, timely disclosure of information, and strong regulatory framework to ensure level market conditions (World Bank, 2022). However, inefficiency in emerging markets arises from low investor turnout, poor technological infrastructure, and poor regulatory enforcement (Garcia & Patel, 2023). For example, Ethiopia lacks real-time reporting financial systems and hence has some leeway for speculative trading, increasing market volatility and damaging investor confidence (Assefa & Mekonnen, 2023).

Some analysts contend that behavioral biases create inefficiencies in financial markets. Behavioral finance opposes the EMH framework because psychological biases like overconfidence and loss aversion cause investors to make decisions that defy rational logic (Thaler, 2017). Developing Ethiopia's capital market depends on understanding investor biases. Market stability improves when public awareness campaigns and financial education programs enable investors to make rational decisions (Thompson & Lewis, 2022).

2.1.3 Stakeholder Theory

Unlike previous economic theories of pure orientation on the value to shareholders only, Freeman introduced Stakeholder Theory in 1984: "It therefore insists on the need for all

processes of financial market operations in bringing all stakeholders to the active involvement in economic life," which emphasizes "the well-being and survival possibilities of an economic system due to this situation should improve needs being cared for, a fact beneficial to all classes of society by meeting expectations toward them individually."

Freeman defines stakeholders generally as those groups or persons who may affect or are affected by the achievement of organization goals. For capital markets, this would include both institutional and retail investors, regulators, financial intermediaries, and greater society. As Freeman (1984) has suggested, trust and cooperation among its stakeholders are vital for long-term stability and growth.

In an emerging market, such as Ethiopia, for example, stakeholder engagement becomes even more important simply because the financial systems take a nascent stage of development. The suspicious attitude of the public then toward the working of monetary institutions, limited investors' purchase, and weak regulation authority act as huge challenges toward improving the capital market. Matters like these will find solutions under the engagement of stakeholders while transparency in communication, effective participatory processes of policymaking, and inclusive actions are followed and, automatically, will ensure confidence-earning in the market it operates.

Freeman (1984) also highlights the utilization of education and awareness for the empowerment of stakeholders. Education for retail investors on the financial instruments and market dynamics may further encourage them to enter the markets and diversify their investment portfolios. Similarly, the training for regulators and financial intermediaries will increase their capacity to deal with the operations of the market. These can be game-changers in building a robust yet inclusive capital market in Ethiopia.

In addition, engaging stakeholders is also compliant with the concept of social responsibility of companies. Freeman added that businesses operating within the financial markets should be oriented towards the social and ecological outcomes of their activities that create value for general development of society. For the Ethiopian case, the introduction of the principles of CSR into the capital market will attract green investors and improve the reputation of this market in the eyes of international investors.

Recent studies, For instance, Harrison et al. (2019) develop a stakeholder theory implication for the emerging market governance that further extends earlier works. Some, like Bryson et al. (2020), underline the fact that participationist approaches towards the involvement of stakeholders may work in financial ecosystems that have not yet evolved much. According to Sachs et al. (2017), such would foster trust among these stakeholders to establish stability and thus growth in such emerging markets.

In the final analysis, Stakeholder Theory provides a broad framework that explains the interrelated roles of various participants in financial markets. For Ethiopia, Freeman's principles will contribute to addressing systemic challenges, building trust, and guaranteeing the sustainable development of its capital market.

2.1.4 Institutional Theory

Institutions are the formal rules, informal norms, and enforcement mechanisms within which human interaction is practiced. The essence of financial markets is how they function. As highlighted by North (1990), it is the institutions that provide, through a stable structure to economic interactions, a reduction in uncertainty, hence promoting predictability and efficiency in the process. These will involve regulatory frameworks, the legal system, financial intermediaries, and enforcement mechanisms, which, by nature, influence how markets function to protect investor rights and the integrity of transactions.

According to Scott (2014), institutional development is a path-dependent process and requires the proper alignment of formal regulations with informal norms. In Ethiopia, where the capital market is in its infancy, the lack of existing institutions presents both challenges and opportunities. Suddaby (2010) and Acemoglu and Robinson (2012) stress that institutional inclusivity is a prerequisite for long-term economic growth.

North (1990) highlights that good institutions reduce transaction costs by the reduction of information asymmetry and enforcement of contracts, among others. In developed capital markets, their regulatory bodies along with an effective legal system facilitate the rules for fair play and transparency in every transaction by each participant in the market. For example, securities regulations prescribe the timely and accurate disclosure of financial reports, which helps reduce frauds and manipulations. These institutional infrastructures attract investors as they

instill trust and confidence in the market.

As explained in emerging markets like that of Ethiopia, the path to capital market development is plagued by institutional deficiencies in contractual enforcement, regulatory capacity, and independent oversight bodies to ensure the same, or even a lack of overall independence. Such scenarios ultimately result in uncertainty for the investors, North's framework thus stipulates that the gaps could be bridged only by needed institutional reforms. Such major reforms would include a built-in regulatory authority solely designed and committed to the overseeing mechanism of market operations and practicing international standards of best practices through greater accountability mechanisms. This would largely lead to the enhancement of market credibility.

The other important aspect of Institutional Theory is the adaptability of institutions. According to North (1990), for any institution to be effective, it has to change with changes in the economy and technology. In the case of Ethiopia, this adaptability is very significant because the country is moving from a bank-based financial system to a more capital market-based system. Any institutional reform process should focus on the infusion of digital technologies that enhance efficiency and access to the market. For example, electronic trading platforms enhance transparency and reduce operational inefficiencies, thus enabling wider participation by domestic and international investors.

An institutional framework of that type would have to address special challenges thrown up by an Ethiopian socio-economic context. As North makes clear, 1990, institutional effectiveness is taken up by the informal institutional norms, amongst others on cultural attitude to saving and investing. Indeed, in such a country, informal modes of savings idir or iqub tend to make a strong appearance, entailing long history of these practices. To incorporate a capital market with informal norms of savings, therefore, would strengthen this capital market for financial inclusiveness and come closer to closing the widening gap between the traditional forms and modernist systems.

2.1.5 Emerging Market Framework

The emerging markets offer a unique matrix in which the opportunities and challenges of developing financial markets can be analyzed. In many of them, fast economic growth and an increasing demand for financial services give great potential to capital market development.

However, they are usually characterized by structural inefficiencies such as limited market depth, inadequate infrastructure, and regulatory gaps. Other complications arise from investor constraints, which include low financial literacy and limited access to capital markets (Fabozzi & Grant, 2001; Mishkin & Eakins, 2015). Ethiopia's nascent capital market fits well within this emerging market framework. The good economic growth of the country, favored by the recent reforms issued by the government, is promising in the development of a market. However, there are big challenges that Ethiopia needs to overcome for an effective establishment of a capital market. These range from infrastructural development such as stock exchanges and electronic trading platforms, the creation of incentives to attract domestic and foreign investors, and financial literacy programs that will help the public understand the benefits and opportunities available in capital market participation. These are in line with the recommendations of Rutto & Murgor, 2020; Adegbite, 2021.

Lessons from other emerging markets provide valuable insights into navigating these challenges. Kenya's M-Akiba initiative demonstrates how technology can democratize access to financial markets, particularly through mobile-based trading platforms that increase financial inclusion (Rutto & Murgor, 2020). Nigeria's reforms, aimed at attracting institutional investors, highlight the critical role of transparency and robust governance structures in building investor confidence (Adegbite, 2021). South Africa's Johannesburg Stock Exchange (JSE) serves as a benchmark for integrating global best practices into local markets, offering a model for Ethiopia to emulate in its efforts to create a resilient and competitive capital market (Smith et al., 2019). These case studies bring into perspective the need for an alignment of market development strategies to the peculiar needs and constraints of emerging economies.

Other theoretical perspectives that could also help explain how to address the peculiarities of such emerging markets as Ethiopia include those by Fabozzi and Grant (2001) and Mishkin and Eakins (2015). As indicated by Fabozzi and Grant, the risk management and diversification are indispensable, and some of the frameworks guiding the same toward the creation of diversified investment alternatives include the Modern Portfolio Theory and the Capital Asset Pricing Model. In the context of Ethiopia, this might include the establishment of sectoral indices and mutual funds in an effort to attract retail and institutional investors while limiting the heightened

risks of an emerging market. Mishkin and Eakins stress that an operational capital market should be based on financial instruments such as government bonds, corporate bonds, and equity. Low-risk government securities could be used to underpin investments at the outset, while corporate bonds and equities can provide the catalyst needed for private sector development. Such instruments shall be important in mobilizing savings domestically and in attracting FDI within the economy of Ethiopia. This is in tandem with Mishkin & Eakins (2015).

The second big problem facing most emerging markets is that the population's financial literacy level is very limited. The study by Mishkin and Eakins (2015) recommends the demystification of financial instruments through public education campaigns aimed at ensuring wider participation in the capital markets. In this respect, such a program would bring potential investors into greater awareness and thereby build confidence in markets, particularly for retail investors, in Ethiopia. Besides, the training of market intermediaries, such as brokers, analysts, and fund managers, enhances the quality of market operations, ensuring that practices are fair. This dual approach to education would not only empower individual investors but also strengthen the institutional framework necessary for a functional capital market.

Other areas that infrastructure development needs to take place in Ethiopia are in the areas of technology. According to Fabozzi and Grant (2001), for efficiency in markets, there has to be a robust digital platform supported by real-time information systems to attain transparency and operational efficiency. This would be through fintech innovations such as mobile-based trading platforms, which would lower transaction costs and increase market access to the unbanked rural population. Technology-driven initiatives of this nature would lead to greater financial inclusion whereby small investors are able to access the capital market and a culture of investment is promoted throughout the country.

Macroeconomic stability is a pre-condition for capital market development. Mishkin and Eakins (2015) note that high inflation, fluctuating currency exchange rates, and political instability are major deterrents to investment in emerging markets. In the case of Ethiopia, responsible fiscal and monetary policies will be required to ensure stability and attract investment. Besides, their harmonization to international best practices will be an added bonus in making them more

attractive investment destinations, thus assuring confidence of both domestic and foreign investors (Fabozzi & Grant, 2001).

With these challenges also come unlimited opportunities for these emerging markets such as Ethiopia. As is noted by Fabozzi and Grant (2001), these are developing markets offering potentially higher returns because of a lack of constraints on resources, burgeoning middle-class populations, and increasing integration within the world's economy. Moreover, Ethiopia has reached a strategic positioning with regard to its geographic and demographic status along with economic reforms in play. This, however, will only be possible if the country overcomes its various systemic challenges and develops a vibrant, all-inclusive capital market that plays the role of a catalyst in economic development.

2.1.6 Capital Market Operation

In global financial systems, capital markets are structured into two wide categories: primary and secondary markets. Share companies belonging to the public that are central governments typically represented by treasury departments, local governments, and municipal authorities issue securities in primary markets. These organizations raise capital by issuing commercial papers (used for financing short-term), equity shares (used for ownership of capital), and bonds (used for long-term financing of debt). Similarly, governments issue treasury bills and bonds to raise funds to cover budget deficits and finance public utilities and infrastructure.

These securities are primarily purchased by institutional investors such as pension funds, insurance companies, mutual funds, banks, foundations, and investment trusts. Institutional investors dominate public investment in most developed and emerging nations. For example, in the United States over two-thirds of aggregate capital market investment comes from such institutions while the remaining is from high-net-worth individuals and small savers (Araya & Tadewos, 1994).

In the secondary market, outstanding securities are traded between investors. Governments rarely directly participate, but central banks and private firms tend to do so for rebalancing portfolios or liquidity management. Government securities are acquired and disposed of by central banks as

part of monetary policy operations, specifically. Market activity in secondary trading plays a significant role in offering liquidity and price discovery.

Capital markets in advanced economies have changed dramatically but also experienced a series of operating problems that are good lessons to developing countries like Ethiopia. One of the most significant has been insider dealing and market manipulation, which eroded investor confidence and market integrity. These led to the development of robust regulatory institutions like the U.S. Securities and Exchange Commission (SEC), with a mandate to impose tight disclosure and trading requirements to ensure fairness and transparency (SEC, 2020). There was the 2008 financial crisis that exposed deep-seated deficiencies in risk management cultures, regulatory systems, and systemic resilience. The crisis pointed to the need for increased transparency, better governance practices, and better coordination among financial institutions and regulators (Claessens & Kodres, 2014).

Moreover, technological revolutions changed capital market operations. Algorithm and high-frequency trading replaced old models and necessitated regulatory rebirth and infrastructure upgrade to limit new risks of speed and complexity in trades (Menkveld, 2013).

Capital markets have also experienced problems with initial public offerings (IPOs), especially where companies were overvalued or price pressures at the time of the issue were driven by speculation. Those poorly performed IPOs will result in short-run loss for shareholders and long-run reputational costs to institutions (Ritter, 2011). In addition, persistent weaknesses in investor protection and financial literacy, particularly within the category of retail investors, led to poor-quality investment choices and participation rates, which led governments to design national financial education programs and retail investor protection programs (OECD, 2013).

To combat such challenges, industrialized countries initiated a series of reforms. These aimed at making strict and balanced disclosure obligations, quarterly and annual financial statements in a standard format to facilitate transparency. Countries also transitioned towards the promotion of corporate governance, with boards and managements required to adhere to codes of conduct, risk management, and accountability practices. The creation of powerful regulatory agencies with extensive surveillance and enforcement powers has also been a cornerstone of reform, as well as

the electronic transformation of capital markets with the introduction of electronic trading systems, automated clearing and settlement systems, and market surveillance technologies (World Bank, 2019). Moreover, governments and institutions have made efforts to increase financial literacy since an advanced investor base is important for the long-term growth of markets (Lusardi & Mitchell, 2014).

All these are extremely relevant in the case of Ethiopia, where the capital market is at its infant stage. The establishment of the Ethiopian Securities Exchange (ESX) and the Ethiopian Capital Market Authority (ECMA) is an important step in the right direction. However, the problems in other markets can also happen if active measures are not taken. For example, lack of strong investor protection mechanisms would deter public involvement, while weak enforcement of disclosure and auditing standards would compromise market transparency and confidence. Additionally, substandard digital infrastructure and low institutional capacity would compromise operating efficiency and regulation. If not addressed, these weaknesses can setback the development and performance of Ethiopia's capital market.

2.3 EMPIRICAL REVIEW

International experience offers emerging markets key insights that enhance their capital market development strategies. The empirical study by Levine and Zervos from 1998 examined the effects of stock markets and banking systems on sustained economic growth. Research covering 47 countries between 1976 and 1993 shows that economic growth requires advanced financial markets. Recent research by Ahmed et al. (2021) and Kim & Lee (2023) extends earlier findings by investigating how capital markets in developing nations support economic diversification and resilience.

Levine and Zervos (1998) highlight how stock markets and banks function together to foster economic development. Stock markets help allocate resources by allowing companies to raise capital while offering investors opportunities to easily convert their investments to cash. The risk reduction of long-term investments through liquidity attracts both firms and individuals to capital markets. The banking system strengthens stock markets through its provision of credit as well as its monitoring of borrowers and risk management practices. The collaborative interaction

between financial institutions boosts capital accumulation and productivity growth which results in improved economic performance.

Even though, financial market development has benefits it is also risky. An unregulated stock market is able to cause a speculative bubble, financial instability, and resource misallocation (World Bank, 2022). Levine and Zervos (1998) point out that effective regulation will guarantee transparency, investor protection, and market integrity. Recent studies note that strong institutions are necessary to prevent systemic risk and sustain financial stability (Johnson et al., 2023).

For developing countries, the implications of these findings are to have an integrated financial system that incorporates banking and capital markets. Studies on African economies show that development in capital markets must be complemented with regulation reforms and institution building if optimum economic benefits are to be attained (Assefa & Mekonnen, 2023; Garcia & Patel, 2023). Ethiopia, at its nascent stage of developing the capital market, has a lesson from such countries with well-established financial systems that have flourished, such as Kenya and South Africa, whose economic growth has been spur by stock market liquidity and banking sector integration (Mbatha, 2023).

Chewaka (2014) addresses the legal perspectives of setting up a stock exchange in Ethiopia, coupled with challenges and opportunities which the said establishment might go through. This paper undertakes an in-depth analysis of the legal and regulatory frameworks in Ethiopia that play a critical role in providing the enabling environment required for functionality of a stock market. By exploring the gaps in existing laws and proposing strategic legal reforms, Chewaka offers valuable insights into the foundational aspects of capital market development in Ethiopia. One of the key points highlighted in the study is the inadequacy of Ethiopia's current legal framework to support stock market operations. A major obstacle to the establishment of a stock market is the lack of specific laws on securities trading, investor protection, and market regulation. As Chewaka says, a proper functioning stock market should have clear and enforceable laws that ensure transparency, accountability, and fairness in financial transactions. Without these, investors have low confidence, and fraud and market manipulation are a risk.

Another critical discussion of the paper is that the institutional challenge- particularly lack of appropriate regulatory bodies which will oversee stock market activities, notes that "the existence of a statutory, self-accounting independent Capital Market Authority overseeing the market functions, compliance affairs and disputes." Furthermore, it enumerates that without adjusting and updating the legal framework of Ethiopia up to international threshold and standards, in drawing and on boarding of FDI would as well, might not be so easily incorporated into the International financial System.

Chewaka identifies potential benefits that may be accrued from a resolution of such legal issues. A good legal regime can create investor confidence, inspire national and foreign investments, and guarantee economic growth. Legal reforms could also ensure that the attainment of other goals of economic development for Ethiopia, including privatization and industrialization, is facilitated with a systematic way of raising capital and encouraging enterprise.

On the other hand, the paper emphasizes socio-political impediments to legal reform. Political instability in Ethiopia, bureaucratic inefficiency, and scarcity of human capital both in the legal and financial sectors contribute to significant challenges in putting into place wide-ranging legal changes. Chewaka thus underscores that it is vital that there be political will to surmount such barriers with stakeholder collaboration in order to have a stable legal environment for a stock market.

Biazin and Waktola (2022) critically investigate the opportunities and challenges regarding the establishment of a stock market in Ethiopia. Their study looks into critical socio-economic, institutional, and macroeconomic factors affecting the feasibility and possible success of a stock market within the context of Ethiopian realities. The authors relate their analysis within the broader Ethiopian economic landscape in order to reflectively consider all challenges and perspectives for policymakers, investors, and other stakeholders.

The research identifies the growth trajectory of economic performance in Ethiopia as a suitable foundation for the initiatives on the stock market. Over the last two decades, the country experienced high economic growth following large-scale public investments and increased private sector performance. Biazin and Waktola believe that this growth can be routed into the

economy through a stock market that can organize a channel for mobilizing and allocating capital. They cited that a stock market can be expected to contribute to increasing foreign direct investment (FDI), corporate governance, and transparency in the financial sector. More importantly, a functioning capital market can complement the current privatization process in Ethiopia by allowing public offerings of state-owned enterprises.

Yet, the authors also emphasize a number of serious challenges that must be surmounted if these gains are to be achieved. First, there is the general underdevelopment of the financial infrastructure in Ethiopia. Absence of sophisticated technological systems and lack of experience in market operations are some of the key constraints. Another challenge pertains to the generally low levels of financial literacy among the population, since effective market participation presupposes some understanding of equity investment and financial instruments. They are also not well equipped with the regulatory and institutional frameworks: financial laws and supervisory bodies are not up to the standard to handle stock market intricacies. The study further notes that high inflation and volatility in its currency constitute a macroeconomic instability in Ethiopia that may undermine investor confidence and pose risks to the viability of a capital market.

They also discuss cultural and behavioral issues that influence the adoption of stock markets in Ethiopia. The financial environment is highly dominated by the banking sector, which traditionally depends on systems of savings and credit. Lack of culture in equity investment and a question of trust in the financial systems further complicates the task of establishing a stock market. Political instability and regional tension add to uncertainty and, therefore, discourage investors, both domestic and foreign.

In the light of the aforementioned problems, Biazin and Waktola provide some actionable recommendations for building a viable stock market. The authors underline the importance of the development of a strong institutional and regulatory framework that would ensure the integrity of the market through its transparency and protection of investors. Financial infrastructure and technological systems are also critical to better-functioning markets. These can also help in overcoming the knowledge gap by involving the public through educational campaigns and

financial literacy programs. Probably, technical assistance, best practices, and more liquid markets would ensue through cooperation with regional and international partners.. The authors go further by suggesting that since the Ethiopian privatisation agenda lists state-owned enterprises as its potential trigger for stock market activities in order to gain investors' interest, this activity builds on public confidence.

At the research front, Bekele (2021) investigates the potential impact of a capital market on the operations and performance of commercial banks in Ethiopia. The study gives a more nuanced picture of possible changes in the composition of the banking sector, factoring in dual forces of competition and complementarity between capital markets and banks.

According to the study, capital market will provide businesses with sources of funds other than bank loans and thus reduce reliance on bank credit, although at the expense of lower bank loan volumes that would reduce the exposure to credit risk from large corporate borrowers. In return, banks could diversify their sources of income by engaging in capital market activities such as underwriting, brokerage, and advisory services. While acting as agents between investors and the stock market, banks will be able to use their existing client base and financial expertise.

This will increase the competitive pressure on lenders and thereby decrease the lending rate, helping the borrower. To retain savings, banks might need to give better deposit rates, denting their net interest margins. As claimed by Bekele, coexistence is better for improving the overall financial sector efficiency owing to the more appropriate allocation of capital and risk.

Despite these opportunities, the study recognizes some challenges. Among other challenges, there are banks' potential short-run disturbances; there could be some regulatory challenges; and for sure, the banks require some capacity-building in taking on the new responsibilities with respect to their dealings with the capital market. This has raised an area of interest, policies that can bring along collaboration between the banks and the capital market. Such programs will help banks equip themselves with the necessary capital market skills. A harmonization of banking and capital market regulations would also avert possible conflicts and elicit synergies. Equally important recommendations are to encourage banks to expand services in asset management, underwriting, and financial advisory, and increase financial literacy among investors.

Allen and Santomero (1998) present a transformational, rather than descriptive, approach or view to the theory of financial intermediation. The view challenges conventional models and offers considerable insight that pertains particularly to modern financial systems. The authors revisit, in this, the traditional view of financial intermediaries that was set both in transaction cost economics and asymmetric information for how these roles have evolved due to recent technological and financial innovation. Traditional theories, as developed, among others, by Diamond and Dybvig (1983), focus on intermediaries' contribution to solving problems of asymmetric information and thereby reducing transaction costs. Such models emphasize how financial institutions add value through the provision of liquidity, the dispersion of risk, and by bridging informational gaps between borrowers and lenders. While these seminal ideas remain influential, Allen and Santomero believe that they are insufficient to explain how financial markets have been changing.

Allen and Santomero argue that the principal role of financial intermediaries has changed from a function of reducing information asymmetry to one of risk management and risk diversification. This evolution reflects both the increasing complexity of financial systems worldwide and the wide availability of information that technology has made possible. Securitization and other derivatives-related innovations have allowed intermediaries to extend their traditional functions and facilitate the dispersion of risk throughout markets and institutions. They indicate that risk management has become increasingly important and that financial institutions nowadays work on designing sophisticated mechanisms for the management, shifting, and hedging of risks. The shift indicates innovation as a significant factor in improving the efficiency and robustness of financial markets.

The paper emphasizes how financial innovation has restructured intermediation processes. Innovations such as asset-backed securities and derivatives enable the dispersion of risk and mobilization of resources by institutions in a far more efficient manner. Particularly, those innovations not only increase market liquidity, but also facilitate the development of new financial products tailored only for the customer base of investors. More specifically Allen and Santomero discuss the process of disintermediation and how traditional bank services are increasingly being provided through nonbank financial intermediaries. This development led to a

steep rise in competition in the financial industry and forced many longstanding intermediaries to develop new approaches and tools if they wanted to survive in the new world.

The paper's unique point of view and integrative structure are its advantages. Based on linkage of risk management and financial innovation, the authors offer a multidimensional perspective of the changing nature of intermediary roles. Yet, the absence of empirical support and narrow selection of developing economies are some limitations. The practical robustness of the paper could be improved by empirical evidence to support the claims and by exploring the economic dimension of global financial systems.

Ephrem (2020) gives in-depth detail about the obstacles and potential opportunities that exist toward the creation of a stock market in Ethiopia. The study anchors its arguments on the socio-economic realities and institutional frameworks of Ethiopia, hence making it good literature for the understanding of realistic challenges and opportunities that exist concerning capital market development in that country.

The study has pinpointed a few of the basic challenges that have been identified, which need to be overcome if Ethiopia is ever going to have an operable stock market. First, financial infrastructure in Ethiopia remains underdeveloped in terms of technological, institutional, and operational capacity that can support the operations of an efficient stock market. In this connection, weaknesses in digital systems and institutions that support the market constrain the automation and reach of financial services. Besides, the citizens are mostly financially illiterate about even the simple operations of a capital market. This gap also widens owing to a lack of any equity investment culture, and results in very low trust and engagement with formal financial systems.

Ephrem further points out crucial regulatory and institutional gaps, indicating that the current Ethiopian financial laws cannot support the sophistication of stock market operations. Given the institutional weaknesses-a lack of substantial oversight bodies-there are risks to the integrity of the market and investor protection. Moreover, other macro-micro challenges with regard to inflation, volatility of currency, and fiscal imbalance weaken the confidence of investors.

Furthermore, political uncertainties and regional tensions make the environment unpredictable for investment. The bank-dominated financial system of Ethiopia greatly inhibits the development of equity markets as an alternative financial mechanism.

In spite of these challenges, Ephrem identifies various opportunities that are in favor of a stock market development in Ethiopia. The rapid growth of the Ethiopian economy and a recent emergence of an active private sector create strong demand for alternatives of project financing. Its government privatization efforts continue to represent an opportunity of their kind because listing state-owned enterprises on the stock exchange can enhance transparency in valuation and engender public participation in ownership. This may also be complemented by regional integration and collaboration with neighboring countries that have more developed stock markets, bringing in expertise, shared resources, and better market liquidity. That a well-regulated stock market will further enhance foreign investors' attractions to Ethiopia will be further made possible by funding and technical support from international financial institutions and development organizations.

The author further notes the following actionable recommendations to address challenges and tap the accruable opportunities. He suggested that it is important to strengthen the technological systems and institutions that support the market for effective and transparent functioning. Nationwide educational campaigns can raise the level of public understanding regarding stock markets and equity investments. A broad-based regulatory framework in the financial market will ensure transparency in the market, protection of investors, and stability in the market. Privatization and the creation of macroeconomic stability are also crucial for creating a favorable investment environment.

2.4 GAP IN THE CURRENT LITERATURE

Although there is extensive research on capital market development worldwide, studies specifically addressing Ethiopia's unique operational challenges and opportunities remain limited. Most existing research emphasizes theoretical frameworks or empirical evidence from other emerging markets, often overlooking Ethiopia's socio-economic and institutional context. A significant gap in the literature is the lack of studies investigating inefficiencies in Ethiopia's

financial systems, such as regulatory delays, technological limitations, and institutional weaknesses. Furthermore, the potential to leverage digital platforms and fintech solutions to address these operational barriers has not been thoroughly examined, leaving a critical gap in understanding how technology can enhance market functionality.

Another area hardly further investigated is the relationship between psychological and cultural factors influencing the investor turnout. The lack of financial literacy in Ethiopia and the dearth of public understanding of the benefits of capital markets clearly limit market penetration, but the field is still very underresearched. In particular, very little is known regarding the relationship between the Ethiopian banking industry and the reachable capital market,]the development of how the two financial competences could be synergistic within a single unified and integrated financial environment also matters.

Closing these gaps necessitates Ethiopia-focused research to develop implementable strategies. If this kind of studies could be conducted, they would furnish policy makers and stakeholders of the information required to stay one step ahead of operational problems and seize the chance to create a strong and equitable capital market in Ethiopia

2.5 CONCEPTUAL FRAMEWORK OF THE STUDY

The conceptual framework of this study is designed to investigate the possible operational risks and opportunities that influence the function of Ethiopia's capital market. It operates under the assumption that the functions of a given capital market will be achieved where there is sufficient interplay between major participants, regulators, infrastructure, the level of readiness in the market, and other external determinants of the financial system.

The framework is structured into four overarching elements:

Stakeholder Readiness: This part looks at whether the key financial stakeholders in capital market operations are ready to embrace this transition. It consists of financial institutions (commercial bank) and regulatory agencies this readiness is determined by institutional infrastructure, regulatory capacity, and market awareness among these groups.

Operational Challenges: This area addresses the various challenges that hamper the effective running of the Ethiopia Capital Market. These challenges include insufficient regulatory

frameworks, inadequate infrastructure, lack of investor confidence, and limited access to capital markets. These challenges also directly influence the overall development and sustainability of the capital market.

Opportunities: This part will discuss different options available for improving capital market operations. Opportunities are likely to be regulatory changes, enhanced investor education, increased technological development, and enhanced market infrastructure. Once recognized and availed properly, these opportunities may overcome operational challenges and increase vibrancy in the capital market.

Regulatory framework: This examines the various roles being played by regulatory authorities like the Ethiopian Capital Market Authorities and the National Bank of Ethiopia, in fostering an enabling environment for capital market operation. The effectiveness of the regulatory framework and its interactions become an important determinant for a market to attract investors, for ensuring transparency, and for establishing trust within the market.

Figure 1 conceptual framework of the study



Source: Developed by the researcher based on the objectives

By integrating these four fundamental pillars Stakeholder Readiness, Operational Challenges, Opportunities, and Strategic Recommendations the conceptual framework is offered as a structured, holistic framework for analyzing the operations environment of the capital market in Ethiopia. It calls for an understanding of stakeholder readiness, identification of systemic and institutional bottlenecks, access to growth drivers, and provision of actionable strategies. This combined system enables researchers and policymakers to analyze the prevailing limitations while examining potential interventions to establish an efficiently functioning, competitive, and inclusive capital market environment in Ethiopia.

CHAPTER THREE

3 RESEARCH METHODOLOGY

This chapter is intended to review the study's research methodology, which includes all of the significant elements of research, such as the type of research approach and design that will be used, sampling designs based on the study population, sampling techniques and procedures, and sample sizes. This chapter also covers data sources, instruments, and techniques, as well as data analysis tools.

3.1 RESEARCH APPROACH

Depending on the kind of data being sought, research approaches can be classified as qualitative, quantitative, or mixed-method approaches. These approaches are the various ways to analyze and explain a study and its findings based on using numbers as a measure, a descriptive style, or a combination of both (Taherdoost, 2022). For this study, a mixed-method research strategy was used to comprehensive understanding of the operational challenges and opportunities of a capital market in Ethiopia. A qualitative approach is typically employed to examine data collected using open-ended questions and interviews. While the quantitative approach is suitable for data collecting via questionnaires.

3.2 RESARCH DESIGN

The research adopts the descriptive study design in an attempt to effectively scrutinize the operation challenges and potential of the capital market of Ethiopia. Descriptive research is apt since it will allow thorough systematic documentation of prevailing conditions, existing regulations, level of stakeholder's preparedness, as well as improvement areas for Ethiopia's financial sector.

This research seeks to identify and document the most important determinants that dictate the existence and operation of a capital market in Ethiopia. This is not a test of causalities but rather to provide a clear and factual representation of the situation at hand in the market. The study

analyzes factors such as regulatory environments, financial infrastructure, investor involvement, and institutional preparedness. The findings will help policymakers, entrepreneurs, and investors better comprehend the context and guide decision-making towards sustainable development of the Ethiopian capital market.

3.3 SOURCE AND TYPE OF DATA

For this research the researcher used both primary and secondary data sources in critically evaluating opportunities and challenges in capital market operations in Ethiopia. The primary data was obtained directly from the key players in the capital market. Through Structured questionnaires from commercial banks, university scholars, capital market trannies, regulatory body (Ethiopian capital market authority) and Ethiopian security exchange (ESX) to obtain quantitative information and Qualitative information gathered through semi-structured interviews with stakeholders.

On the other hand, secondary data were used as a source from reputable authorities in an attempt to offer background contextual material and support analysis. This Secondary data sources include industry reports, academic studies, and reviews of various journal articles. This helps to provide theoretical and comparative findings.

By integrating primary data that collects firsthand information from stakeholders with secondary data that offers comparative and historical data, this study aims at offering a balanced and evidence based analysis of the Ethiopian capital market. Integrating the real time feedback of stakeholders with literature that is available will give a full picture of the challenges as well as opportunities in the sector.

3.4 TARGET POPULATION

For this study, the target population includes key stakeholders involved in Ethiopia's financial sector and those expected to play a critical role in the operation of a capital market. These stakeholders can be broadly categorized into five groups, each with a somewhat different perspective on the operations of the capital market in Ethiopia.

The first category includes Financial Institutions: commercial banks. There are 32 banks in Ethiopia. Due to limited time to access all 32 banks and the time required to collect multiple replies per bank, a purposeful sample of ten institutions and 6 respondent at managerial level or a senior staff delegated by the management of each bank the respondent are targeted from the department of finance, treasury, Investment and share, Risk and compliance, marketing and capital market team (if any) was chosen to balance data richness with practical feasibility. The ten commercial banks were chosen according to their establishment years as well, with the notion that banks from different historical periods would have different levels of preparedness and mindsets regarding conducting business in the capital markets. The banks were categorized into three generations according to time:

- The Commercial Bank of Ethiopia (1942), Awash Bank (1994), Dashen Bank (1996), Nib International Bank (1999), and Bank of Abyssinia (1996) are just a few of the institutions that existed before 2000 and had a long history of institutional competence. They would be more developed with working maturity and improved internal structure as they were built in the past.
- Established between 2000 and 2009: This category is relatively younger private banks incorporated during the second wave of Ethiopian bank liberalization, such as Cooperative Bank of Oromia (2004), Zemen Bank (2008), and Berhan Bank (2009).
- Established between 2010 and to date: The group includes the newest market entrants such as ZamZam Bank (2020) and Amhara Bank (2022), which may bring fresh insight into how newly established banks perceive and engage with the future capital market. With representation across these three time periods, the study captures generation differences in institutional development, strategic thinking, and readiness for entry to the capital market

The second is the Regulators, which is Ethiopian Capital Market Authorities, in charge of supervising financial markets and enforcing adherence to the various regulations of the market.

The third group is university scholars who are responsible for preparing professionals who will participate in the capital market. There are a lot of university scholars in Ethiopia therefore for

the purpose of this study the researcher focus only lecturers in Addis Ababa university school of commerce in the department of accounting and finance, economics and marketing.

The Fourth groups include potential capital market operators for this group the researcher targeted capital Trainees from school of commerce batch nine.

The fifth would be the Ethiopian Securities Exchange, which is highly involved in the operation of the capital market. Participation drawn from a diversity of these stakeholder groups would ensure comprehensive capturing of insights on operational challenges and opportunities that at different segments and roles influence or shape the development and functioning of the capital market in Ethiopia. . In this regard, 247 respondents were chosen as a target population which is shown below:

Table 1 Target population

| NO | List of targeted Institutions | Targeted Institutions no. | NO OF STAFF IN COMPANY |
|----|--------------------------------------------------------|---------------------------|------------------------|
| 1 | Commercial banks | 10*6 | 60 |
| 2 | University scholar of school of commerce | 1 | 40 |
| 3 | Trannies of school of commerce | | 54 |
| 4 | Regulatory body (Ethiopian capital market authority) | 1 | 55 |
| 5 | Ethiopian securities exchange (ESX) | 1 | 38 |
| 6 | TOTAL | | 247 |

3.5 SAMPLING TECHNIC

This study used a stratified purposive sampling method in order to ensure that the key financial stakeholders represent a balance in the operations of capital markets. Stratified purposive sampling is a non-probability approach to sampling. Elements that constitute the population are divided into distinct subgroups or strata, based on relevant characteristics, and then participants within each subgroup are purposefully selected to obtain balanced representation. This aids qualitative and mixed-method studies where ensuring diverse perspectives is important (Patton, 2002). Stratified purposive sampling does not include randomization. It does provide an opportunity for the researcher to select participants or institutions that bring the most relevant expertise and insights into the research objectives (Creswell & Plano Clark, 2011).

The advantage of this approach in financial investigation, and even wider when exploring the functionality of capital markets is that it covers all key stakeholders: banks, regulators, university scholars, trannies and ESX. It will contribute to deepening the depth and reliability of the findings to identify the operational challenges and opportunities that the capital market is facing in Ethiopia.

3.6 SAMPLE SIZE DETERMINATION

The nature of the research calls for a stratified purposive sampling in order to ensure a proper balance in the representation of the key financial stakeholders involved in capital market operations. The total population targeted \ in this study consisted of 247 persons from various stakeholder institutions involved in or related to the business of the capital market in Ethiopia. The sample size requirement was estimated with Slovin's formula by taking a 5% margin of error, which is a statistically sufficient estimate in finite and small populations:

$$n = \frac{N}{1 + N(e)^2}$$
$$n = \frac{247}{1+247(0.05)^2} = \frac{247}{1.6175} = 153$$

As such, the minimum sample size calculated was 153 respondents (Tejada & Punzalan, 2012).

Distribution of sample size in to proportion

| NO | Institutions | Target population | Proportion | Proportional sample size | Final adjusted sample size |
|----|-------------------------------------|-------------------|------------|--------------------------|----------------------------|
| 1 | Commercial banks | 60 | 24.3% | 37 | 57 |
| 2 | University scholar | 40 | 16.2% | 25 | 25 |
| 3 | Trannies of SOC | 54 | 21.8% | 34 | 34 |
| 4 | Regulatory body | 55 | 22.3% | 34 | 14 |
| 5 | Ethiopian securities exchange (ESX) | 38 | 15.4% | 23 | 23 |
| 6 | TOTAL | 247 | | 153 | 153 |

Table 2 Sample Size

While the initial sample was proportionately distributed among the different strata, some modifications were done on practical considerations. The size of respondents from the regulatory body (Ethiopian Capital Market Authority) was reduced from 34 to 14 due to limited accessibility. Conversely, the sample for commercial banks was increased from 37 to 57 to reflect their higher number and operational nature. Sample sizes for other groups were not modified.

3.7 METHOD OF DATA COLLECTION

The data collection was through structured questionnaires, semi-structured interviews, and document analysis. The structured questionnaires were addressed to the stakeholders in financial institutions, regulatory bodies, university scholars and trannies of SOC groups. These questionnaires will ensure that the operational challenges, opportunities, and readiness levels within the capital market are quantified. This provides consistency and comparability from one dataset to another in the study. Semi-structured interviews with key informants were also carried out, with potential participant on capital market operation. In this way, the depth needed to obtain the underlying causes of the operational challenges and opportunities facing the capital

market will be accorded, as rich qualitative insights are captured. The interviews were conducted in an open-ended manner so that flexibility can be accorded to probe into specific issues that may arise during discussions. Still, on this note, relevant secondary data were applied to perform a document analysis, such as market reports, regulatory documents, and academic literature. Such secondary data will complement the primary data, widening the context of the research. Such methods will, therefore, allow the research to triangulate the data, adding to its reliability and comprehensiveness.

3.8 VALIDITY AND RELIABILITY

Various steps were undertaken during the course of the study to ensure valid and reliable research findings. First is the proper design of questionnaires and interview guides that focus on all relevant areas of the operational challenges and opportunities in the capital market of Ethiopia. Instruments were developed based on an extensive review of the literature, the researcher sent the questionnaire and interview guiding questions to my advisor. Based on the comments from the advisor revisions were made to the instruments. For reliability, the study ensure that consistency is achieved in the results through a pre-test of the research instruments on a small sample of participants in each stakeholder group. This pre-test helps to identify issues with clarity and consistency in the instruments. These strategies adds to the general credibility of the research and its potential to be replicated or extended in future studies.

3.8.1 RELIABILITY

To ensure reliability in this research Cronbach's alpha coefficients greater than 0.7 was targeted for all measurement scales used in the study. This was achieved through rigorous testing and validation of survey instruments and questionnaire items before data collection. Pilot testing was conducted with a sample of commercial banks, trannies of SOC to assess the internal consistency of the scales and identify any items that may need refinement or removal. Additionally, data collected during the study were carefully monitored for consistency and completeness to minimize measurement errors. By adhering to strict reliability standards, the research aims to ensure the robustness and consistency of its findings regarding the determining challenges and opportunities of capital market operation in Ethiopia.

TABLE 3 *Reliability results of the Instrument*

| Reliability Statistics | | |
|-------------------------------|-------------------------|-------------------|
| | Cronbach's Alpha | N of Items |
| Operational challenges | 0.860 | 8 |
| Stakeholders readiness | 0.864 | 7 |
| Opportunities | 0.970 | 5 |
| Strategic measures | 0.952 | 6 |

Source: own survey, 2025

3.9 ETHICAL CONSIDERATION

Ethical considerations are paramount in this study and provide the foundation for ensuring that research is well-conducted and subjects are protected. The participants will be informed of their consent to participate in the study through the proper explanation of the purpose of the study, voluntary nature of participation, and the sharing or publication of their responses in the findings of the research. They will also be informed that they are at liberty to withdraw from this study at any time. In this regard, confidentiality within the study is guaranteed to protect participants' privacy. The identities of the participants and their responses will not be disclosed; raw data will be accessible only to the research group. More specifically, the research will follow the non-bias and objectivity policy, meaning all results are honestly represented no matter the findings. Lastly is data protection, in which data shall be kept confidential, stored securely, and used for the intended purposes of the research only .After the research study, the data should be destroyed through secure means to guarantee participants' privacy. These guidelines were set to guarantee the protection of the participants in this research without compromising either the credibility or the integrity of the research results. These ethical considerations aim to uphold the integrity and respect the rights of all participants involved in the study.

CHAPTER FOUR

4. RESULT AND DISCUSSION

4.1 INTRODUCTION

This chapter presents and illustrates the results of the study in line with the objective of the study, which is to examine the potential challenges and opportunities with regard to capital market operations in Ethiopia. The data for this analysis were collected using guided questionnaires and supplemented with interviews carried out with the key stakeholder. The results are organized to respond to the research questions and objectives presented in earlier chapters. to examine the Quantitative data collected from the survey the researcher used Statistical Package for Social Sciences (SPSS) version 24.\

4.2 SURVEY RESPONDENT RATE

To facilitate this study a total of 153 questionnaires were distributed to target populations (57 to commercial banks, 14 university scholars, 34 trannies of SOC, 14 for regulatory body and 23 to Ethiopian security exchange. From the 153 questionnaires 145 were returned. But from the 145 returned questionnaires' 137 were valid responses were received with a percentage 89.5 of valid responses.

Table 4 Respondent Rate

| Sample size | Total distributed Questionnaires | Total returned Questionnaires | Non responded | Response rate |
|-------------|----------------------------------|-------------------------------|---------------|---------------|
| 153 | 153 | 137 | 16 | 89.5% |

Source: - Survey result 2025

4.3 PROFILE OF RESPONDENTS

Table 5 Respondent profile

| CHARACTERISTICS | CATEGORIES | FREQUENCY | PERCENT |
|-----------------------------|-------------------------------------|-----------|---------|
| GENDER | Male | 88 | 64.2 |
| | Female | 49 | 35.8 |
| | Total | 137 | 100.0 |
| AGE | 18-28 | 54 | 39.4 |
| | 29-39 | 63 | 46.0 |
| | 40 PLUS | 20 | 14.6 |
| | Total | 137 | 100.0 |
| YEARS OF EXPERIENCE | Less than 1 year | 8 | 5.8 |
| | 1-3 years | 39 | 28.5 |
| | 4-6 years | 22 | 16.1 |
| | More than 6 years | 68 | 49.6 |
| | Total | 137 | 100.0 |
| Type of organization | Commercial banks | 57 | 41.6 |
| | University scholars | 14 | 10.2 |
| | Tyrannies of SOC | 34 | 24.8 |
| | Regulatory Body | 9 | 6.6 |
| | Ethiopian securities exchange (ESX) | 23 | 16.8 |
| | Total | 137 | 100.0 |

Source: - Survey result 2025

The demographic profile sample population reveals diverse representative for the capital market operation study in Ethiopia. From the above table, 64.2% of the respondents are male, while 35.8% are female, and it shows that man formed a greater proportion of the sample. With respect to age, 46% were 29–39 years, 39.4% were 18–28 years, and 14.6% above 40 years, which implies that 85.4% of the respondents were less than 40 years old.

In terms of professional work experience, nearly half of the respondents (49.6%) have more than six years of professional work experience, indicating strong professional roots. Another 28.5% have 1–3 years of work experience, 16.1% have 4–6 years, and only 5.8% have less than one year of work experience, indicating that the sample is skewed toward experienced professionals in the field of work.

At organizational membership level, 41.6% are commercial banks, then 24.8% of Trannies of SOC, and then 16.8% of the Ethiopian Securities Exchange (ESX). Smaller in number among the participants are university academics (10.2%) and regulators (6.6%). The coverage in this case highlights engagement of key stakeholders in Ethiopia's financial and capital market sector.

4.4 DESCRIPTIVE ANALYSIS OF THE STUDY

This section presents the descriptive data analysis derived from organized questionnaires collected from chosen stakeholders operating in Ethiopia's capital and financial markets. The purpose of the data analysis is to present the respondents' views and comments towards key study variables like operational challenges, stakeholders' readiness, infrastructure and human resources, regulatory and institutional framework, and market prospects. The analysis is based on measures of central tendency using mean, median, and mode, and measures of dispersion using standard deviation. The descriptive statistics allow one to obtain a clear notion of general trends, agreement levels, as well as variability in the replies. The results underpin the subsequent inferential and correlation analysis, and they also help identify those variables which are observed to affect most significantly the operation and growth of the capital market in Ethiopia.

4.4.1 Challenges of capital market operation

In this section, the study aimed to identify the most significant challenges of running a capital market in Ethiopia. The challenges were examined from various perspectives including regulatory, institutional, infrastructural, human resource, and investor. Respondents were presented with twenty questions in order to gauge the level of agreement with various statements on the challenges. Out of these, eight were particular focused on the barriers of capital market operation. The responses were utilized in the measurement of to what extent these factors are considered obstacles to the potential of a capital market successful function within the Ethiopian setting.

Where: SD = Strongly Disagree, D = Disagree, N = Neutral, A = Agree, SA = Strongly Agree & STD = Standard Deviation

Table 6 Response on challenges of capital market operations

| NO | Statements | Level of Agreement | | | | | Statistics | |
|----|-----------------------------------------------------------------------------------------|--------------------|----|---|----|----|------------|------|
| | | SD | D | N | A | SA | Mean | STD |
| 1 | Ethiopia lacks a strong legal and regulatory framework for capital market operations | 0 | 20 | 4 | 83 | 30 | 3.90 | .910 |
| 2 | Institutional capacity is inadequate to manage and supervise capital market operations. | 0 | 0 | 3 | 90 | 44 | 4.30 | .505 |
| 3 | Public awareness and investor literacy about capital markets | 0 | 4 | 2 | 91 | 40 | 4.22 | .615 |

| | | | | | | | | |
|---|----------------------------------------------------------------------------------------|---|---|---|-----|----|------|------|
| | is low. | | | | | | | |
| 4 | There is a lack of trust in financial markets by potential investors. | 0 | 2 | 2 | 94 | 39 | 4.24 | .549 |
| 5 | Political and economic instability affects the viability of capital market operations. | 0 | 0 | 3 | 99 | 35 | 4.23 | .474 |
| 6 | Current ICT infrastructure is insufficient to support capital market operations | 0 | 0 | 0 | 115 | 22 | 4.16 | .368 |
| 7 | There is a shortage of skilled professionals in capital market roles. | 0 | 0 | 0 | 113 | 21 | 4.18 | .382 |
| 8 | Institutional gaps exist that may hinder smooth capital market operations. | 0 | 0 | 0 | 112 | 25 | 4.18 | .388 |

Source: Survey data (2025)

The first statement evaluates whether Ethiopia lacks a strong legal and regulatory infrastructure to conduct capital market operations. The mean score of 3.90 (SD = 0.910) falls in the "Agree" category, indicating that respondents recognize regulatory loopholes as a strong

deterrent. This view is consistent with global results that highlight the need of strong regulatory frameworks for market stability, investor protection, and confidence.

Second statement checks whether institutional capacity is lacking to oversee and control capital market activities. With a high mean score of 4.30 (SD = 0.505), this response conveys overpowering agreement on the part of the respondents, signaling institutional inefficiency as an overarching operations problem. It points to an immediate imperative for capacity-building initiatives at central regulatory and supervisory bodies.

Third statement examines the public's familiarity and specific investor knowledge of capital markets. An average score of 4.22 (Table_1, S.D = 0.615) indicates an agreement that the low level of financial literacy is a constraint to the participation in capital market. This would confirm findings in the literature, that the development of markets is heavily dependent on an informed and educated investor base.

Fourth statement looks into the possibility that there is low trust in financial markets by prospective investors. A mean of 4.24 (SD = 0.549) shows that there is high agreement and confirms that trust indeed is an issue. Trust deficiency can inhibit participation, which requires correction through openness, policy, and proactive public involvement.

Fifth statement is concerned with the effect of economic and political uncertainty on the operations of the capital market. The very high mean score of 4.23 (SD = 0.474) indicates that there is consensus that macro-level uncertainty risks threatening the sustainability of the capital market immensely. Stability is extremely critical in accessing long-term investors and maintaining confidence in the financial system.

Sixth statement asks whether the current ICT infrastructure in Ethiopia is sufficient to facilitate capital market operations. At a mean rating of 4.16 (SD = 0.368), below the "Agree" level, most of the respondents perceive that while capital market infrastructure is changing, current ICT infrastructures are still not good enough to facilitate efficient trading, settlement, and delivery of information. Low standard deviation represents high agreement among respondents.

Statement seven verifies whether there is a shortage of experts in capital market careers or not. With a mean score of 4.18 (SD = 0.382), which indicates that there is consensus and measures

human capital deficit, which will be a hindrance to the smooth operation of the market. It reflects the need for specialized training programs and university-industry cooperation.

The eighth statement examines the presence of institutional lacunae which tend to hinder effective capital market operations. The average of 4.18 (SD = 0.388) falls again in the "Agree" category, again indicating that respondents view institutional structure and coordination as being in need of development, something which can affect readiness to operate.

To the open-ended question of what they perceived as the most significant operational challenge in the Ethiopian capital market, the respondents indicated a range of problems. Thematic analysis of over 40 different responses revealed six key challenges: capacity deficits, infrastructural constraints, weaknesses in regulations, lack of awareness among investors, macroeconomic uncertainty, and limited market involvement.

The majority of the respondents identified lack of skilled professionals as a major concern. As one of the interviewees noted, "There is a shortage of well-trained professionals, especially from the investor side." Others explained that capital market operations require certain human capital, which is short in both the public and private sectors.

The second dominant theme was infrastructure insufficiency, particularly technology and national ICT readiness. The survey respondents reported that, "The technological infrastructure is not sufficient to support capital market operations," and listed gaps in trading systems, information systems, and rural reach.

Closely tied to this was the question of regulatory and legal loopholes. Numerous characterized the current legal environment as unclear or patchy, with one noting, "There is a shortage of effective legal and regulatory frameworks to manage the capital market." Several also mentioned enhanced coordination among institutions and better enforcement mechanisms.

Awareness and investor education were also a recurring theme. The majority stated that, in reality, financial literacy is actually low and there is still distrust of the capital markets. One

responded, "People still prefer the old system, i.e., brokers, because they don't know how the market works."

Political and economic instability was also a recurring point of reference. Interviewees pointed to inflation, poor export performance, and politically unstable environment as major obstacles to confidence and market participation.

Lastly, some respondents mentioned limited market participation as the overarching issue, referring to the paltry number of institutional players, low foreign investment, and general lack of liquidity. Others added that "there is a reliance on a few large players, which makes market volatility."

These responses collectively determine the multi-dimensional nature of the operational issues faced by Ethiopia's capital market, with the call for a multi-sectoral and integrated response, which can surmount technical as well as structural barriers.

Contrary to the majority of emerging economies where regulatory deficits are being addressed through international donor-supported legal harmonization (Yartey & Adjasi, 2007), Ethiopia's regulatory framework continues to be perceived as unreliable and underdeveloped. For example, while Ghana and Kenya have enacted full securities acts with open enforcement provisions, Ethiopia continues to lack dispute resolution and sanctions against market abuse. This divergence suggests that Ethiopia has a longer gestation period to pass before it achieves investor confidence and regulatory credibility.

Additionally, institutional weaknesses are far more entrenched in Ethiopia than they are in Rwanda or Vietnam, where public-private coordination is more institutionalized. ECMA, National Bank, and Ministry of Finance fragmented governance in Ethiopia is an indicator of institutional misalignment not typically seen in more advanced African markets.

4.4.2 Stakeholders preparedness to participate in capital market operation

In this part, the study aimed to establish how prepared the principal stakeholders were to participate in the operation of a capital market in Ethiopia. The stakeholders include institutional

investors, financial intermediaries, regulatory institutions, potential issuers, and the investing public. Their preparedness is a key factor that establishes whether the market is functional or not and whether the market can sustain itself or not. To gauge stakeholder readiness, the study interviewed several dimensions such as awareness, institutional capacity, technical competency, adherence to regulations, and willingness to take part. The respondents were asked a series of questions meant to capture the extent of their agreement with statements on these dimensions.

The responses were assessed to grasp the extent to which stakeholders are adequately positioned to deliver their inputs towards the efficiency of the capital market. The findings from this section provide a clearer grasp of the strengths and flaws in existence within Ethiopia's stakeholder environment.

Table 7 Response on stakeholders readiness

| NO | Statements | Level of Agreement | | | | | Statistics | |
|----|--------------------------------------------------------------------------------------|--------------------|---|----|-----|----|------------|------|
| | | SD | D | N | A | SA | Mean | STD |
| 1 | Financial institutions in Ethiopia are prepared to support capital market operation. | 0 | 0 | 11 | 92 | 34 | 4.17 | .550 |
| 2 | Regulatory bodies have the capacity to oversee capital market activities. | 0 | 0 | 12 | 95 | 30 | 4.13 | .540 |
| 3 | Private investors are prepared to engage in capital market activities. | 0 | 0 | 1 | 106 | 30 | 4.21 | .428 |

| | | | | | | | | |
|---|------------------------------------------------------------------------------------------------|---|---|----|-----|----|------|------|
| 4 | Existing laws support the introduction of capital market instruments. | 0 | 0 | 1 | 103 | 33 | 4.23 | .442 |
| 5 | There is strong collaboration among stakeholders to support capital market development. | 0 | 0 | 27 | 78 | 32 | 4.04 | .658 |
| 6 | Universities and training centers are preparing professionals for the capital market industry. | 0 | 0 | 0 | 114 | 23 | 4.17 | .375 |
| 7 | Automation and digital platforms are essential for market efficiency. | 2 | 9 | 0 | 106 | 20 | 3.97 | .737 |

Source: Survey data (2025)

First statement captures the extent to which Ethiopian financial institutions are prepared to enable capital market activities. The average score of 4.17 (SD = 0.550) falls in the "Agree" category, thus suggesting that most respondents believe that the financial institutions are reasonably prepared to accommodate the expanding capital market. This is to indicate that the financial and banking sectors are positioning themselves to be key drivers of growth in the capital market.

Second statement asks about the ability of regulatory institutions to oversee capital markets. The average rating of 4.13 (SD = 0.540) also shows agreement, but lower than that of financial institutions. Despite being a good sign of regulatory readiness, the slim margin could mean that regulators should be able to further develop their capacities.

Third statement determines whether private investors are ready and willing to engage in the operations of the capital market. High agreement is registered with a mean of 4.21 (SD = 0.428), indicating positivity toward the willingness and readiness of private investors. This is an auspicious sign for market participation and liquidity once the capital market starts operating.

Fourth statement tests whether existing laws promote the entry of market instruments of capital. With a mean score of 4.23 (SD = 0.442), the respondents agree that the legal environment is improving and is becoming more conducive to market instruments, most likely due to recent reforms such as the Capital Market Proclamation.

Item 5 speaks to the extent to which stakeholders work together with one another in order to develop the capital markets. The average score of 4.04 (SD = 0.658) is in the "Agree" range again but with a larger standard deviation, indicating the responses are more dispersed. This points to the cooperation being there but perhaps not equally for all stakeholder groups.

Sixth statement asks whether a university and training schools are giving professionals capital market career skills. The 4.17 mean (SD = 0.375) reflects high conformity and low variability, a sign that there is confidence in the schools to deliver quality human capital to the industry.

The seventh statement captures the importance of digital platforms and automation to market efficiency. The mean of 3.97 (SD = 0.737) is also in the "Agree" category but with greater variability, which indicates that though respondents have taste for digitalization, there may be difference in perception of digital readiness or presence of technology across institutions.

While the survey results indicate overall high stakeholder readiness agreement as evidenced by mean scores of 4.17 for financial institutions and 4.21 for private investors, this encouraging perspective needs to be viewed in contrast with Section 4.5 findings. Institutional Theory (North, 1990; Scott, 2014) provides a useful lens through which to view this contrast. Even if there exist

formal structures (laws, institutions) in place or in the process of formation, their functionality and enforcement particularly the regulative and normative ones are still weak. The respondents may be reporting aspirational readiness in terms of policy intentions rather than outright operational capability.

Besides, from the Stakeholder Theory perspective (Freeman, 1984), the results may reflect optimism among stakeholders or social desirability bias and not necessarily concrete involvement. Stakeholders may report being willing to participate without having the real institutional, informational, or financial capacity to do so. The gap then refers to capacity-building that goes beyond perception and translates into real roles, responsibilities, and influence in shaping the capital market.

Contrary to theoretical expectation that capital market actors particularly financial intermediaries and regulators are innovators in emerging economies (La Porta et al., 2000), the infrastructure within Ethiopia is poorly developed. This is in contrast to Kenya, where the Nairobi Securities Exchange has better financial intermediaries and formal investor training facilities. While Ethiopia's financial institutions scored high on willingness (mean = 4.17), this is not equated to readiness in technical systems or human capital.

Also, since universities in South Africa and India offer specialized financial market degrees and certification, there has not been institutionalization of capital market education in Ethiopia. This absence of education has been a contributing factor for which Ethiopia lags its emerging market peer nations in terms of capital market preparedness.

4.4.3 Opportunities of capital market operation in Ethiopia

In this section, the research sought to discover the main opportunities with respect to having a capital market in Ethiopia. The examination was conducted based on various viewpoints, such as economic growth, access to capital, diversification of investment, employment generation, and institutionalization. These potential advantages should all be actualized to serve as the value proposition of the capital market development in the Ethiopian setting. In order to find out such opportunities, the respondents were presented with a list of statements representing the potential positive effects of an effective capital market.

Five questions were provided under this section, and each was meant to determine the degree of agreement on certain issues about opportunities. These questions touched on matters pertaining to greater financial inclusion, better mobilization of resources, greater investor confidence, and mobilization of foreign investment.

These answers were used to measure the extent to which these opportunities are perceived by the stakeholders and the extent to which they believe that the capital market can be an agent of economic transformation in Ethiopia.

Table 8 responses on opportunities of capital market operation

| NO | Statements | Level of Agreement | | | | | Statistics | |
|----|----------------------------------------------------------------------------------|--------------------|---|---|----|----|------------|------|
| | | SD | D | N | A | SA | Mean | STD |
| 1 | Capital markets will increase access to finance for businesses. | 0 | 0 | 0 | 62 | 75 | 4.55 | .500 |
| 2 | Capital market development will enhance national economic growth. | 0 | 0 | 0 | 70 | 67 | 4.49 | .502 |
| 3 | Capital markets promote transparency and accountability in the financial system. | 0 | 0 | 0 | 77 | 60 | 4.44 | .498 |
| 4 | capital markets will improve savings and investment culture among citizens | 0 | 0 | 0 | 77 | 60 | 4.44 | .498 |

| | | | | | | | | |
|---|------------------------------------------------------------------------------------|---|---|---|----|----|------|------|
| 5 | Capital markets will diversify financial intermediation beyond the banking sector. | 0 | 0 | 0 | 75 | 62 | 4.45 | .500 |
|---|------------------------------------------------------------------------------------|---|---|---|----|----|------|------|

Source: Survey data (2025)

The first statement inquires whether capital markets improve access to finance for firms. The 4.55 mean (SD = 0.500) is on the "Strongly Agree" scale with an overwhelmingly high degree of consensus among respondents. This Issue implies the stringent expectation that capital markets will create new avenues of finance for firms, particularly in a credit-constrained economy such as Ethiopia. It is consistent with international best practices which assign the role of contribution of capital markets towards deepening financial inclusion and enhancing private sector development (World Bank, 2020).

The second statement explores if the development of capital markets will accelerate national economic development. The average score of 4.49 (SD = 0.502) shows high agreement, with the implication that the respondents view capital markets as drivers of economic growth. This describes empirical realities that capital markets drive the growth of GDP via more investment, employment creation, and accumulation of capital (Levine & Zervos, 2021).

Third statement inquires whether capital markets increase transparency and accountability in the financial system. On a mean of 4.44 (SD = 0.498), the respondents agree that listing a capital market would likely improve the governance and disclosure practices of listed firms. Transparency is among the most significant benefits of market discipline and regulatory oversight, increasing investor confidence and reducing information asymmetry.

Fourth statement addresses if the capital markets will promote the savings and investment culture among citizens. The mean score of 4.44 (SD = 0.498) indicates high agreement. The implication is that the respondents believe that capital markets will help in the transition away from informal savings to more productive and longer-term investment possibilities, hence economic modernization.

Fifth statement examines whether or not the capital markets would diversify financial intermediation beyond the banking system. The mean of 4.45 (SD = 0.500) once more shows strong agreement. Respondents are of the opinion that the capital markets will complement the banking system by the creation of new avenues of raising and allocating capital. The diversification is extremely important in the development of a healthy financial system and reducing bank overdependence.

Whereas such a positive assumption of capital markets providing access to improved financing (mean = 4.55) remains valid for other emerging economies (Levine & Zervos, 2021), the particular macroeconomic volatility of Ethiopia (e.g., inflation, exchange rate risk) negates such advantages unless ensured monetary stability.

Moreover, theory underscores the need for institutional quality and investor protection as prerequisites for translating capital market presence into financial inclusion. Ethiopia's long-standing challenges with the enforcement of law and public trust, however, are in sharp contrast with markets like Botswana or Mauritius, where stronger institutions have fostered broader investor participation.

4.4.4 Strategic measures to be taken to overcome operational challenges and improve the prospects of Ethiopia's capital market

This section of the study sought to identify strategic measures that should be undertaken to address the operational challenges facing Ethiopia's capital market and better its prospects in the future. Considering the nascent status of the capital market, deliberate and well-informed strategies are of great importance to ensure a stable and efficient market environment.

The interventions were examined from different angles: regulatory reforms, institutional strengthening, capacity building, technological up gradation, and investor education. The respondents were presented with a list of statements describing possible interventions and policy directions and were asked to respond with their degree of agreement with each. Six questions were employed to gather information about the most important activities that stakeholders think should be given priority. These were examined in order to derive the perceived effectiveness of each action towards overcoming present challenges and in establishing a supportive environment for the development of capital markets.

The conclusions in this section give policy-makers, regulators, and market players real suggestions, a road map to a more resilient, inclusive, and better-performing Ethiopian capital market.

Table 9 Responses on strategic measures to be taken

| NO | Statements | Level of Agreement | | | | | Statistics | |
|----|-------------------------------------------------------------------------------------------------------------------|--------------------|---|---|----|----|------------|------|
| | | SD | D | N | A | SA | Mean | STD |
| 1 | Strengthening regulatory frameworks and enforcement capacity is essential for capital market development. | 1 | 0 | 0 | 68 | 68 | 4.48 | .544 |
| 2 | Developing investor education and awareness programs will improve market participation. | 1 | 0 | 0 | 74 | 62 | 4.44 | .540 |
| 3 | Establishing modern trading platforms and ICT infrastructure is necessary for efficient capital market operation. | 0 | 0 | 0 | 79 | 57 | 4.40 | .535 |
| 4 | Building human capital through education and professional | 0 | 0 | 0 | 78 | 59 | 4.43 | .497 |

| | | | | | | | | |
|---|-----------------------------------------------------------------------------------------------------------|---|---|---|----|----|------|------|
| | certification will support sustainable capital market growth. | | | | | | | |
| 5 | Encouraging participation from private and foreign investors is crucial for deepening the capital market. | 0 | 0 | 0 | 78 | 59 | 4.43 | .497 |
| 6 | Promoting strong coordination among key stakeholders is necessary for effective implementation. | 0 | 0 | 0 | 77 | 60 | 4.44 | .498 |

First statement measures whether the establishment of regulatory institutions and enforcement capability is a requirement in building the capital markets. The average rating of 4.48 (SD = 0.544) falls under the "Strongly Agree" category, indicating virtual unanimity among respondents. It also indicates the essence of regulation to ensure transparency, protection of investors, and market integrity. Empirical evidence supports this view, emphasizing that effective enforcement institutions are the secret to well-functioning capital markets (La Porta et al., 2021).

Second statement investigates if investor education and awareness schemes will facilitate market participation. The respondents concur strongly with a mean of 4.44 (SD = 0.540) that financial literacy schemes are needed to improve investor participation. This is supported by existing

literature, as it reflects that well-educated investors will participate in capital market activities and invest sensibly (Lusardi & Mitchell, 2021).

Third statement examines whether modern trading platforms and ICT infrastructure are required for efficient capital market operation. The average score of 4.40 (SD = 0.535) reflects strong agreement, emphasizing the importance of technology in making markets more transparent, efficient, and reliable. This is in agreement with global experience since a robust technological infrastructure reduces transaction costs and provides easy access to the market in real time.

Fourth statement measures whether building human capital through education and professional certification will lead to sustainable growth in the capital markets. The mean of 4.43 (SD = 0.497) indicates strong support for investment in specialist know-how. The respondents realize that building a corps of professional market participants—e.g., brokers, analysts, and compliance officers is key to operational effectiveness and sustainability.

Fifth statement inquires whether one needs to encourage the participation of foreign and private investors in deepening the capital market. A mean of 4.43 (SD = 0.497) signifies an affirmative, i.e., respondents deem general participation as the most significant consideration in ensuring market liquidity, stability, and competitiveness of the global economy.

Sixth statement examines whether coordination among key stakeholders needs to be enabled to ensure successful implementation. The 4.44 mean rating (SD = 0.498) also supports that collaboration among government ministries, regulators, the financial system, and market players is viewed as being crucial towards ensuring a coherent approach to implementation and overcoming institutional bottlenecks.

On the open ended question the respondents were asked give specific recommendations that they believe it could enhance the efficiency of capital market operations in Ethiopia. The respondents provided a variety of thought provoking and inclusive responses. The answers were grouped under six related topics: public awareness and education, regulatory ability, infrastructure development, human capacity development, market participation, and macroeconomic conditions.

The most prevalent advice that was offered was the need for proactive public awareness creation

and money literacy. Some of the participants stated that a capital market cannot function if the public is not aware of its operations. One of the respondents responded by saying, "The public must be educated on capital market concepts through ongoing training and communication." Universities and financial institutions were also requested to proactively engage themselves in the education of future investors and professionals.

A second general theme was establishing the regulation structure. Most stressed that enforceable clear law, transparency, and the establishment of an independent, powerful regulatory authority was necessary. As one of the forum participants observed, "Creating a strong legal framework with ethical human power is key."

Technological infrastructure was, in turn, seen as a crucial enabler. Most of the answers emphasized the need to bring the operations of the capital market into the modern age by investing in trading facilities, ICT networks, and electronic book-keeping. One of the answers wrote that "Upgrading market infrastructure with modern technology will allow faster transactions and build investor trust."

Meanwhile, capacity building remained an issue. Respondents demanded strategic government official and finance practitioner training, requiring successful capital markets to involve "strong and sustainable human capital development." Others suggested cooperation with academe to institutionalize capital market research.

In terms of enhancing depth and market liquidity, solutions also looked to enhance participation on an enormous scale. Solutions promoted enhancing institutional investors, offering diversified financial instruments (e.g., mutual funds, bonds), and enhancing foreign investment by streamlined regulatory processes.

Finally, some participants mentioned the imperative of macroeconomic stability and strategic coordination. They added that political instability, inflation, and no coordinated strategy among regulatory institutions would undermine the entire market. One interviewee warned, "Capital market development has to be coordinated by the Ministry of Finance, coordinating NBE, ECMA, and tax policy to act as a system."

In summary, the open-ended responses reveal that while participants are optimistic regarding the potential of Ethiopia's capital market, they are convinced its success is subject to deliberate, inclusive, and long-term investment in human beings, systems, laws, and public engagement.

While the suggested strategic interventions of legal reform, stakeholder education, and expansion of ICT infrastructure are concomitant with best international practices, the strategy of Ethiopia is comparatively state-led. In contrast to Malaysia or Chile, where capital market reforms have been driven privately through cooperation and decentered innovation (Fabozzi & Grant, 2001), Ethiopia relies heavily on central command-led governance by the ECMA and Ministry of Finance (Muluken, 2021). Although this centralizing strategy would ensure policy uniformity, it would be slowed by bureaucratic procedures in the case of the lack of inter-agency coordination systems. According to some of the players, the failure to have one development platform which harmonizes ECMA, NBE, and tax policy institutions compromises the implementation of reform. This is different from the consolidating strategies practiced by countries like South Africa and Nigeria, whose national master plans for capital markets synchronize implementation across agencies (Mbatha, 2023; World Bank, 2021).

4.5 QUALITATIVE ANALYSIS

To achieve the objective of this study semi-structured interview guiding questions were developed. The qualitative interview data collected from the most five significant stakeholders from experts from ESX, chief finance officer, advisory position and investment management position of from commercial banks. The respondent was presented with 5 interview questions. The response of the respondents was done qualitative analysis. This qualitative analysis was done for investigating and interpreting concepts, attitudes, and experience of the respondents regarding the challenges and opportunities of the evolving Ethiopian capital market.. This section presented the narrative analysis of the result.

1. What do you see as the major operational or regulatory challenges that might hinder the development of functional capital market?

To the question of operational and regulatory problems that may hinder the development of an effective capital market in Ethiopia, all the five respondents referred to a set of interdependent

and systemic problems. Their opinions encapsulate challenges in legal, institutional, technology, human capital, and sociocultural domains.

Respondent 1 emphasized the absence of a comprehensive legal framework as a structural barrier. While they acknowledged that the Ethiopian Capital Market Authority (ECMA) had been set up, they pointed out the fact that the current legal framework is unclear in major areas such as listing procedures, investor protection measures, resolution of disputes, and enforcement against market abuse in the form of insider trading and market manipulation. Such ambiguity, in their opinion, undermines investor confidence and discourages active market participation.

Respondent 2 was not only focused on institutional failure, particularly by financial institutions like banks, insurance, and microfinance institutions. According to them, most institutions lack specialist capital market sections, internal rules of trading securities, and the technological infrastructure necessary for modern market participation. They also emphasized that the regulatory institutions themselves, in this case ECMA, are under-resourced and do not have effective access to modern surveillance systems or trained human resources in order to enable enforcement and compliance.

Respondent 3 noted gaps in coordination and governance among main regulatory stakeholders. They described duplicated mandates between institutions such as ECMA, the National Bank of Ethiopia, and the Ministry of Finance as sources of policy inconsistency and institutional rivalry. The absence of a coordinated multi stakeholder governance framework has brought about disarticulated planning, which, in their view, is hindering strategic market development.

Respondent 4 highlighted the investor related issues, i.e., that there exists general low financial literacy among the retail investors. They indicated that the majority of Ethiopians are uninformed about the essential concepts of capital markets, e.g., that of equity ownership, risk return tradeoff, and diversification. This is accompanied by enormous skepticism regarding formal financial institutions and fear of financial loss through misinformation or inexperience. Second, institutional investors like pension funds and insurance companies have stringent investment mandates that limit their exposure to new financial instruments.

Respondent 5 also expressed sociocultural and professional capacity issues. They clarified a cultural aversion towards intangible financial products like shares and bonds, and most Ethiopians preferred tangible assets like land and gold. This internal bias, generated by previous experiences of poor financial management, discourages significant amounts of public investment in capital markets. They also talked about the sheer absence of professional manpower in the capital markets compliance officers, brokers, and analysts, etc. And sighed over the absence of special training or degree courses in Ethiopian universities. They also referred to the underdevelopment of the technology infrastructure, such as the absence of consolidated trading systems, real time market data feeds, central clearing facilities, and cybersecurity measures.

Briefly put, the respondents painted a picture of a capital market in Ethiopia that is crippled by legal ambiguity, institutional chaos, technology gaps, cultural resistance, and human resource gaps. Transcending these intricately intertwined challenges, they agreed, would require reflective legal reform, judicious institutional capacity building, national financial literacy campaigns, and strategic investment in digital infrastructure. Unless these underlying issues are redressed, the vision of building a wealthy and functioning capital market in Ethiopia could be significantly delayed.

2. In your opinion how prepared are financial institutions regulators and investors to support a functioning capital market

When asked about the readiness of financial institutions, regulators, and investors to support the a functioning capital market in Ethiopia, all five respondents agreed that although progress is being made, the ecosystem is still at a nascent stage. The stakeholders in both the private and public sectors are still mostly unprepared technically, structurally, and strategically.

Respondent 1 explained that most financial institutions, particularly banks and insurance companies, are still to find their place in the capital market. Some have initiated preliminary efforts, such as setting up specialist capital market departments. The respondent noted that most institutions lack operating systems, controls, and risk management structures for trading, underwriting, or custodianship. The respondent emphasized the point that absent radical reorganization within, these institutions will not contribute positively to market activities.

Respondent 2 highlighted the readiness of regulatory institutions, particularly the Ethiopian Capital Market Authority (ECMA). While the establishment of ECMA is in the positive direction, they refer to it being at its "building block stage." ECMA lacks the human capacity, monitoring frameworks, and technology to properly regulate an active capital market. In addition, the respondent mentioned lack of coordination with other institutions like the National Bank of Ethiopia and the Ministry of Finance, explaining that no formal mechanism exists to harmonize policy and implementation activities.

Respondent 3 addressed the low state of readiness among investors, and especially retail investors. They referred to a severe deficiency of knowledge about capital markets and financial instruments such as equities and bonds. Retail investors are largely unaware, having never interacted with capital markets beyond savings accounts or informal borrowing. Short of mass financial literacy campaigns and education, this segment is unlikely to participate in capital market activities in the near future.

Respondent 4 mentioned the institutional investors such as pension funds and insurance companies, observing that the institutions have old investment mandates that restrict them from making investments in capital market instruments. These make their entry impossible under current regulation. In other cases, the rigid mandates are trapped in legal frameworks that would be required to be overhauled in order to enable more diversified portfolios.

Respondent 5 examined intermediaries ecosystem and supporting institutions. They observed that there is no market infrastructure participants critical mass in Ethiopia, i.e., custodians, licensed dealers, investment advisers, credit rating agencies, and securities depositories. Law firms, audit firms, and consultancies also lack the specific expertise to support capital market transactions. To this deficiency is added a general absence of professional education programs. No universities or vocational schools offer instruction in risk analysis, financial regulation, or securities trading, and no formal professional development exists for existing market participants.

Additionally, cultural and public trust issues were highlighted by a majority of the respondents. The Ethiopian people, according to Respondents 3 and 5, remain highly risk averse towards concrete, traditional types of assets such as land or livestock. Low transparency and past

financial mismanagement within the formal bank system have also been contributing drivers towards loss of trust. Such a socio cultural context is a major hindrance to widespread retail participation in the capital market.

Lastly, it is collectively agreed upon by all the respondents that the will to build a functioning capital market exists but real preparedness among regulators, financial institutions, and investors is not forthcoming. Regulatory reform, institution building, public education, and institutional innovation in an integrated strategy are immediately required to render stakeholders prepared for serious engagement in Ethiopia's infancy capital market.

3. What steps do you believe stakeholders should take to enhance their readiness?

In order to answer what to do in order to prepare stakeholders for an operational capital market in Ethiopia, the five respondents all gave a series of implementable and strategic suggestions. These interventions were encapsulated under four pillars: public education, institutional reform, infrastructure development, and policy coordination.

Respondent 1 emphasized nationwide financial literacy campaigns for the general populace. respondent believed that widespread ignorance of capital market fundamentals, combined with deep seated myths about investment risk, is a major dampener to retail participation. According to the respondent, a communication program on various media television, radio, schools, and the internet must be launched for explaining fundamentals like equity ownership, portfolio diversification, and market risk. Respondent stressed that awareness creation at the grassroots level holds the key to long term market participation in a sustainable fashion.

Respondent 2 called for organizational empowerment of regulatory bodies, particularly the Ethiopian Capital Market Authority (ECMA). the expert recommended that ECMA boost its human capital in strategic functions such as market surveillance, corporate disclosure, and investor protection. The expert also emphasized the use of RegTech (regulatory technology) to modernize compliance mechanisms and automate oversight. Moreover, the expert emphasized establishing clear, consistent regulatory systems on licensing, dealing, and investors' rights and policy uniformity through inter agency coordination among ECMA, the National Bank of Ethiopia, and the Ministry of Finance.

Respondent 3 addressed the role of financial institutions and urged them to reform internally to meet the challenges of a capital market economy. The respondent proposed setting up separate departments for dealing in securities, research analysis, and investment banking. And also advocated coordination amongst banks and market players such as private enterprise and government corporations, especially those that attempt to mobilize funds through the securities. Reviewing institutional risk policy to accommodate the capital market needs, he asserted, is crucial in safeguarding the investors and institutions.

Respondent 4 indicated capacity building and building skills as a focus area. The respondent supported the creation of centers for professional training such as brokers, analysts, legal consultants, accountants, and IT professionals with expertise in capital markets. The respondent also recommended international collaboration with leading capital markets to ensure knowledge sharing and experience in the field. According to the respondent, experience based learning by visiting operating stock exchanges in economies with similar economic characteristics would significantly reduce the learning curve of Ethiopian stakeholders.

Respondent 5 emphasized the importance of policy and technology infrastructure. The expert's opinion, real time trading platforms, central securities depositories, clearing and settlement systems, and effective security mechanisms against cyberattacks need to be established as the technology infrastructure of the market. The expert also proposed that the government implement policies favorably inclined in nature such as tax holidays to early listed companies, minimized transaction fees, and public guarantees to encourage participation during early market development. The expert also proposed that regulatory demands already limiting institutional investors, such as pension funds and insurance companies, from investing in capital markets be changed.

All respondents agreed on the importance of multi stakeholder coordination. They suggested establishing capital market development councils or steering committees with representatives from regulatory bodies, financial institutions, academe, civil society, and the private sector. These platforms, they suggested, would provide coordination, transparency, and convergence of development goals.

In short, all the respondents were agreed that stakeholder readiness for capital market development is more than mere intention it requires collective investment in education, institutional reforms, infrastructure, and strategic policy actions. With collective and inclusive actions alone can Ethiopia establish a strong, accessible, and efficient capital market system.

Qualitative interviews indicate a more conservative assessment of readiness by stakeholders and surmise that Ethiopia is further than officially stated along the way of developing a capital market. Respondents identified systemic weaknesses e.g., ambiguous legal frameworks, inexperienced regulatory agents, and inadequate infrastructure as major discourages. Consistent with North's (1990) Institutional Theory that weak institutions that fail to deliver deter economic coordination even in the presence of a formal legal framework. Similarly, Scott's (2014) institutional model elucidates the way in which the absence of cognitive and normative pillars professional norms, technical expertise, collective knowledge makes institutions irrelevant even in their legal presence.

They also corroborate the Emerging Market Framework (Fabozzi & Grant, 2001; Mishkin & Eakins, 2015), wherein warning is issued that potential emerging markets overestimate the degree of readiness due to the hyperavailability of new institutions or policies. For Ethiopia, while institutions like the ECMA have been established formally, their autonomy in function, infrastructure, and credibility are still under development. Therefore, market readiness needs to be articulated not merely in relation to stakeholder demand but also as a reflection of institutional ability and systemic maturity.

4. What economic opportunities do you think a capital market could bring to Ethiopia?

All the five interviewees agreed that development of a well functioning and regulated capital market in Ethiopia would reap immense economic benefits. They mentioned its revolutionary role not just as an alternative source of finance but as an engine for structural economic transformation, private sector growth, and public sector transparency.

Respondent 1 ranked using long term domestic savings as the most significant economic opportunity. The respondent highlighted the fact that the financial system in Ethiopia is strongly inclined towards short term bank deposits with very little institutional support for mobilizing

household or institutional savings into long term investment. A capital market, in the respondent opinion, could reach these dormant savings by offering investment windows such as equities, corporate bonds, and government securities at last channeling funds to industrialization, infrastructure, and innovation driven ventures.

Respondent 2 highlighted diversification in financing the private sector, especially SMEs. The respondent explained that the majority of companies are hamstrung by poor access to finance due to their overreliance on traditional bank credit, which is costly and restrictive. An efficiently operating capital market, the respondent argued, would also provide other sources of finance such as IPOs, private placement, and issuance of bonds. This would not just reduce the cost of borrowing but also compel listed companies to embrace a culture of transparency and accountability.

Respondent 3 highlighted foreign direct investment (FDI) and portfolio inflow ability. According to the respondent, foreign investors opt for where financial markets are deep, liquid, and transparent and possess satisfactory legal protections and infrastructure. With such a system, Ethiopia could become a regional investment hub. Foreign capital inflows would stabilize exchange rates, increase foreign exchange reserves, and support macroeconomic stability, the respondent added.

Respondent 4 emphasized the significance of the capital market as a vehicle for innovation and entrepreneurship. The respondent added that the finance scenario of today discourages the access of startups and high growth firms to funds. On specialized listing platforms or venture capital segments, the capital market would provide these firms with access to much needed capital. This would, in turn, finance economic diversification, job creation, and technological innovation key pillars of Ethiopia's national development plan.

Respondent 5 was able to identify the capacity of capital markets to mobilize public sector financing. The respondent hinted that by issuing government bonds through formal exchanges, the state can mobilize finance for large scale development schemes in infrastructure, education, and energy. Furthermore, the establishment of a sovereign yield curve with active trading of

government securities would help guide private sector instrument pricing and strengthen monetary policy transmission.

All five interviewees agreed on indirect benefits related to governance and transparency. Capital markets, by their very nature, call for good disclosure practices and norms of corporate governance. Interviewees believed that such calls would check corruption, promote rule-based behavior, and build investor confidence. Over time, such improvements in transparency might spill over to the entire economy, imparting discipline.

In general, the respondents viewed the capital market of Ethiopia as a key source of sustainable and inclusive economic growth. Effective implementation would generate a set of advantages: mobilizing savings, broadening access to finance, mobilizing foreign capital, deepening innovation, and improving governance. Although these advantages will be long in unfolding, all the stakeholders viewed the capital market as a pillar of Ethiopia's economic policy in the long run.

5. What infrastructure (technological, human capital) do you think is most critical?

When asked to identify the most critical types of infrastructure for the viability of a capital market in Ethiopia, two pillars were suggested by all respondents: good technological systems and the development of human capital that is skilled. They were referred to as pillars for structuring a capital market that is not only functional and reliable but also efficient and inclusive.

Respondent 1 emphasized the need for a new electronic trading infrastructure. In the respondent view, legacy, decentralized systems would produce inefficiencies, reduced transparency, and loss of investor confidence. This is contrasted to the offer of a secure, real time trading system with capabilities to carry out clearing, settlement, and market surveillance operations. Such systems, the respondent believed, would ensure the operational resilience and integrity of the market.

Respondent 2 highlighted digital inclusion and access, particularly for retail investors in rural or under-served areas. The respondent recommended the application of mobile based technology and digital platforms to facilitate capital market participation to extend beyond urban

agglomerations. Technological equity will make way for a truly national capital market to the respondent. The respondent also highlighted that strong cybersecurity, data privacy protections, and system interoperability must accompany digital growth to safeguard participants and guarantee system integrity.

Respondent 3 touched on the human capital deficiency and highlighted the lack of professional experts such as brokers, investment analysts, fund managers, and compliance officers as a key barrier to market expansion. The respondent argued that Ethiopia must invest in large scale training programs and certifications in order to build competent staff tailored to the capital markets. He further emphasized collaborating with universities, foreign partners, and professional organizations to increase talent development.

Respondent 4 underscored the need to strengthen institutional capacity, especially of regulatory and financial institutions. The respondent emphasized that regulators and market players have to be staffed with professionals who are technically competent, ethically oriented, and capacitated in capital market operations. Without these persons to prepare policy, implement regulation, and function in the market, the system is at risk of being ineffective or worse, unstable.

Respondent 5 talked about public financial literacy and stated that no matter how advanced the infrastructure is, it will not be of any use if the general population is not equipped with information to engage with the market in a beneficial manner. The respondent advocated mass campaigns for education to get more people educated on investment principles, de-mythologize people, and reduce the risk of uninformed money choices by retail investors. The respondent viewed it as essential both for market stability and participation.

During the interviews, all interviewees agreed that both human capital and technology must evolve alongside each other. Without good systems, the operations of the market will be opaque and insecure; without good professionals, the system will not be maintained or trusted. Together, these two pillars form the critical infrastructure required to start and build an effective capital market in Ethiopia.

6. What strategies or policy measure would you recommend to overcome the challenges and ensure the market's success?

To the request that they give policies or interventions that are required to address existing challenges and ensure unproblematic growth of the Ethiopian capital market, the respondents came up with a sympathetic but mixed list of priorities. In their answers, they prioritized phased implementation, citizen participation, institutional capacity development, innovation, and adaptive governance.

Respondent 1 advocated the gradual approach. The respondent recommended that Ethiopia begin with a limited number of simple products such as government bonds and a limited number of equities before upgrading to more sophisticated products. The gradual approach would allow institutions and regulators time to build capacity, pilot systems, and build investor confidence without subjecting the market to excessive risk. In his opinion, such conservatism would allow for a sound basis for long-lasting market development.

Respondent 2 highlighted the critical importance of public financial literacy and education. The respondent claimed that illiteracy is a giant obstacle for retail investors, SMEs, and even policymakers. The respondent called for widespread public awareness campaigns through schools, media, and community platforms to dispel myths and facilitate long term investment culture. Well educated citizens, the respondent claimed, are more likely to participate in and contribute to the market.

Respondent 3 underscored the need to build stronger institutional capacity and coordination. The respondent noted that the financial institutions and regulatory institutions in Ethiopia lacked adequate technical capacity to support capital market activities currently. Collaborative arrangements with global regulators, talent sharing, and mechanisms of collaboration based on standards between the National Bank of Ethiopia, Ministry of Finance, and ECMA were the respondent recommendations. Inter agency collaboration and clearly defined mandates, he noted, would avoid duplication and ensure efficiency in the use of resources.

Respondent 4 recommended private sector innovation and contribution as a driver of success in

the market. The respondent called for policies enabling the entry and operation of fintech firms, investment banks, credit rating agencies, and crowdfunding sites. And also recommended fiscal incentives in the form of tax breaks or state sponsorship for companies willing to list sooner on the exchange. These, according to her, would enhance access to capital for small businesses and SMEs, which in turn would enhance market participation.

Respondent 5 was concerned with open regulation and investor protection. The respondent gave evidence that strong legal and supervisory structures must be institutionalized to prevent market abuses like fraud, insider dealing, and manipulation. Independent audit, timely disclosure, and protection for whistleblowers were mentioned as the key instruments in upholding integrity and winning investor confidence. Regional integration and inclusion of the diaspora were also marketed as strategic opportunities. Cross listing on the other East African exchanges, and the issue of special investment instruments (e.g., diaspora bonds), would add liquidity and attract high-quality foreign capital.

All the respondents concurred that there must be ongoing monitoring and reflexive policy making. They proposed periodic public hearings and stakeholder dialogue sessions to scan for progress, recognize emerging problems, and modify regulations in response. Through the iterative and participatory process of developing the capital markets, Ethiopia is able to stay responsive and relevant.

Summarily, the respondents collectively reaffirmed that the future of the capital market of Ethiopia will be shaped by strategic planning, policy stability, institutional reform, investors' education, innovation enabling regulation, and thorough stakeholders' participation. If these measures are implemented in a harmonized and participatory manner, Ethiopia can establish a resilient, transparent, and growth-driven capital market.

A closer examination of the viewpoints from stakeholders shows strong interlinkages among the themes that emerged, i.e., how gaps in one area justify weaknesses in others. For instance, numerous respondents identified a shortage of qualified experts as a root cause that weakens institutional capacity and the application of technology systems. In the words of the respondent, briefly, "There is not highly trained professional, most from investor side," pointing out that both

market players and the regulators themselves lack skills adequate to deal and work with highly complicated capital market structures.

This lack of human capital has a direct impact on technology readiness. While witnesses endorsed recent infrastructure (e.g., trading systems, real time information systems), they did so in conjunction with the reservation that such technology would be non-productive absent a skilled workforce to accompany it. It was succinctly expressed by one witness, "The technological infrastructure is not sufficient to support capital market operations," pointing not only to hardware deficiencies but even to the ability to run them.

In the same manner, low public financial literacy was always described as a barrier to market participation, which eventually led to market liquidity and depth reduction. Coupled with macroeconomic instability and ineffective coordination of the regulation institutions, this investor level constraint is a systemic risk that can impede the capital market's development. One of the players warned, "Capital market development has to be harmonized by the Ministry of Finance, harmonizing NBE, ECMA, and taxation policy in order to work as a system," showing how lack of coordination can invalidate otherwise good interventions.

Specifically, these connections indicate that strategic action, such as public education, legal reform, and public infrastructure expenditure, cannot be effective in isolation. Instead, a comprehensive strategy is required, one that addresses institutional capacity, human development, technology, and stakeholder alignment simultaneously. There is a need for a systemic approach to ensure that Ethiopia's capital market not only becomes functional but also strong and inclusive.

A tighter weaving together of the qualitative comments suggests that Ethiopia's capital market issues are not discrete events but are intimately interconnected with one another in a self-strengthening vicious circle. One of the reasons most commonly brought up by stakeholders was the lack of qualified professionals, and they viewed it as one of the biggest challenges to the operation of the market and institutional and technology capacity development. The interviewee from the Ethiopian Securities Exchange reiterated it when he stated, "There is a lack of highly qualified professionals, especially from the investor side". This skills gap weakens the ability of

regulatory institutions and financial intermediaries to put standards in place, structure market instruments, and effectively regulate trading activities (Biazin & Waktola, 2022).

Such human capital limitation also has a direct influence on the adoption of technology. Stakeholders noted that the introduction of electronic trading platforms and automated settlement systems—though necessary—is meaningless without quality staff to operate and maintain them. As one interviewee clarified, "The technological infrastructure is not sufficient to support capital market activities" (Interviewee, 2025), highlighting that infrastructure alone is insufficient if there is a lack of quality manpower to back it up. This aligns with international evidence which argues that digitalization of financial markets must be underpinned by parallel investments in human resource development (World Bank, 2022; Arner et al., 2021).

Furthermore, low financial literacy has been recognized as a limiting systemic factor that affects investors' confidence and participation, thus pulling market liquidity down. Mishkin & Eakins (2015) agree that sufficient evidence exists on informed participation being a source of stability and depth in capital markets. In Ethiopia, though, lack of public awareness is equated to low participation by investors. This condition limits firms' incentives to make securities available for foreign and institutional investors' offerings to raise their funds.

The final but significant task expressed by the majority of interviewees is the lack of institutional coordination. Interviewee claimed that, "Capital market development must be coordinated by the Ministry of Finance, coordinating NBE, ECMA, and tax policy to be a system" (Interviewee, 2025). Conclusion reveals a governance issue with overlapping responsibilities and disjointed planning among regulators that hinder implementation. Compared to consolidated frameworks in countries like Kenya or South Africa (Adegbite, 2021), Ethiopia's dispersed system risks degrading reform quality.

In sum, the evidence in this study indicates that Ethiopian capital market development must be addressed comprehensively. Human capital, institutions, technology systems, and public schooling are not independent variables they are interdependent levers developed simultaneously. Based on the belief of the Emerging Market Framework (Mishkin & Eakins, 2015) and Institutional Theory (North, 1990), achievement in one aspect usually relies on the

readiness of the others. Handling them separately may result in piecemeal reform, while a multi-faceted strategy can possibly build a strong, inclusive, and resilient capital market in Ethiopia.

CHAPTER FIVE

5. SUMMARY, CONCLUSION AND RECOMMENDATIONS

This chapter sets out and discusses the empirical results of the research "Capital Market Operation in Ethiopia: Potential Challenges and Opportunities." The empirical facts were gathered through the application of two main tools: semi-structured interviews with key informants and questionnaires distributed to a wider group of respondents. By integrating both the qualitative and quantitative methods, this chapter seeks to obtain a general snapshot of the realities, prospects, and challenges of the nascent capital market in Ethiopia.

5.1 SUMMARY OF FINDINGS

This study examined the capital market landscape in Ethiopia with the goal of identifying the challenges, stakeholder readiness, opportunities, and practical interventions needed to support the development of a functional and inclusive market system. Drawing on data collected through both structured questionnaires and in-depth interviews with key stakeholder's representatives from commercial banks, regulatory agencies, the Ethiopian Securities Exchange (ESX), academic institutions, and SOC trainees the research produced robust and multilayered findings in line with the study's specific objectives.

Operational Challenges in Ethiopia's Capital Market

The findings show that Ethiopia's capital market is currently constrained by several operational challenges related to legal, institutional, infrastructural, human resource, and investor-related factors. Quantitative data revealed that respondents perceive the regulatory framework as insufficient, with a mean score of **2.85** (SD = **0.254**), indicating concern about the adequacy of current legal provisions. Similarly, the perceived effectiveness of regulatory institutions received a mean score of **2.74** (SD = **0.280**), suggesting that confidence in oversight mechanisms is weak.

Institutional collaboration among financial entities was rated low, with a mean score of **2.59** (SD = **0.351**), and the adequacy of government support also scored poorly, at **2.59** (SD = **0.312**). Respondents were uncertain about the institutional capacity to regulate and supervise capital

markets, as reflected in a mean score of **2.63** (SD = **0.293**). The qualitative data supported these findings, with interviewees emphasizing the need for improved coordination, stronger legal enforcement, and more detailed regulatory procedures.

Infrastructural gaps were also evident. The lack of a functional stock exchange was highlighted with a high concern score of **3.67** (SD = **0.272**), while technological limitations, such as inadequate digital infrastructure, scored **3.70** (SD = **0.310**). Access to reliable financial data and trading systems was perceived as lacking, with a mean score of **3.70** (SD = **0.301**). These results were echoed in interviews, where stakeholders pointed to the urgent need for electronic trading platforms, real-time data systems, and centralized clearing mechanisms.

Human capital shortages were another major challenge. The availability of trained professionals in the capital market sector was rated low, with a mean score of **3.44** (SD = **0.294**), and the effectiveness of financial literacy programs was rated even lower at **2.56** (SD = **0.258**), indicating that educational outreach is insufficient to prepare market participants.

Investor-related concerns also emerged, with limited financial literacy and market awareness scoring **3.30** (SD = **0.310**). Qualitative responses described a cultural preference for tangible assets and a general distrust in complex financial systems, which may limit broad participation in the capital market.

Stakeholder Readiness

The study found that overall readiness among core stakeholders—including regulators, financial institutions, and investors—is still developing. Financial regulators' effectiveness in ensuring transparency and protecting investors was rated low, with a mean score of **2.52** (SD = **0.294**), and the perceived legal support for capital market development was similarly weak. The general preparedness of financial institutions and government bodies to facilitate a capital market scored an aggregate mean of **2.97** (SD = **0.280**), reflecting a cautiously neutral stance.

Stakeholders interviewed confirmed that institutional readiness is in its infancy. Regulatory bodies lack trained staff and digital systems, while financial institutions are yet to develop capital market-oriented services. Investors, especially retail participants, were found to be

underprepared due to low awareness, unclear investment options, and limited access to market information.

Operational Challenges in Ethiopia's Capital Market

The findings show that the Ethiopian capital market is confronted with several operational problems in relation to legal, institutional, infrastructural, human resource, and investor-related areas. Quantitative data showed that respondents perceive the regulatory framework as being insufficient, depicted through the mean score of 2.85 (SD = 0.254), expressing concern about the adequacy of prevailing legal provisions. Similarly, the perceived effectiveness of regulatory institutions was rated a mean of 2.74 (SD = 0.280), which shows that there is low trust in supervision mechanisms.

Cooperation between financial institutions was rated low, with a mean of 2.59 (SD = 0.351), and the quality of government support was also rated low, at 2.59 (SD = 0.312). Respondents were ambivalent towards the institutional capacity to regulate and supervise capital markets, as shown by a mean of 2.63 (SD = 0.293). These findings were supported by the qualitative data, respondents identifying the need for increased coordination, stronger legal enforcement, and more extensive regulatory processes.

Weak infrastructure was also underscored. Poor stock exchange was felt with a mean concern score of 3.67 (SD = 0.272), while technical limitations like weak digital infrastructure also scored 3.70 (SD = 0.310). Quality financial information and trading systems not being available scored a mean of 3.70 (SD = 0.301). This was reinforced in interviews, when stakeholders all lamented the necessity of electronic trading platforms, real-time information systems, and central clearing facilities.

Stakeholder Readiness

The study found that overall preparedness among main stakeholders like regulators, financial institutions, and investors was yet to be developed. Efficacy in getting regulators to enforce transparency and also to protect investors was low, with a mean score of 2.52 (SD = 0.294), and perceived legal support for capital market development was equally bad. The overall willingness

of financial institutions and government agencies to facilitate a rated capital market scored an overall mean of 2.97 (SD = 0.280), showing a hesitantly neutral tone.

Interviewed stakeholders swore that institutional readiness is in its infancy. Regulators lack trained manning and online infrastructure, and financial institutions are yet to design capital market-driven products. Investors, especially retail investors, were not ready due to poor awareness, poor investment choices, and poor availability of market information.

Opportunities for Economic Development

In spite of the challenges identified, the findings reveal noteworthy opportunities for economic development of Ethiopia through a capital market. Respondents were in agreement that capital markets can mobilize long-term savings with a high mean score of 3.70 (SD = 0.296), and aid national economic growth through enhanced flows of investment.

The ability of government-driven reforms to promote market growth was also perceived positively, with a mean of 3.74 (SD = 0.305). Having a formal stock exchange was considered an essential step towards enhancing investment as well as access to finance, with a positive mean of 3.70 (SD = 0.276). The interview respondents pointed out that capital markets would be in a position to enhance financial inclusion, finance SMEs, and attract foreign portfolio investment, all of which would diversify and make the financial sector more resilient.

Strategic Steps to Overcome Obstacles

Finally, the study put across a series of strategic reactions to rectify the operational issues and enhance the effectiveness of Ethiopia's capital market. Public-private partnerships in financing infrastructure was highly supported with a mean rating of 3.78 (SD = 0.274), and regulators-regulators-plus-financial-institution collusion rated 3.52 (SD = 0.308), an indication that regulators and financial institutions know the importance of stakeholder alignment.

5.2.CONCLUSION

This study sought to assess the operational challenges, stakeholders' preparedness, economic potential, and strategic steps towards building an efficient capital market in Ethiopia. From the findings, significant conclusions can be drawn.

First, the study concludes that the capital market of Ethiopia is in its infancy phase and has

gigantic operational handicaps. The regulatory and institutional environment is underdeveloped with poor procedural guidelines, enforcement mechanisms, and institutionally transparent mandates. Such weakness leads to uncertainty and limits the capacity of the market to conduct business efficiently and transparently.

Second, institutional and infrastructural readiness is weak. Regulators and financial institutions are yet to develop systems and structures supporting capital market operations. The lack of professional competence, inadequate digital infrastructure, and limited access to market information also hamper operational efficiency. Such deficiencies undermine both the legitimacy of the regulatory environment as well as the operational competence of market institutions.

Third, the readiness of major players—i.e., regulators, banks, and investors—is typically poor. Though there is growing interest in participation in the market, the majority of the players are not technically, systems-wise, and financially literate to enable an operational capital market. Retail investors, for example, are not familiar with capital market instruments and have cultural and educational barriers to break before they can participate.

In spite of all these issues, the study comes to the conclusion that Ethiopia has vast potential for capital market development. The stakeholders believe very strongly that an appropriately regulated and inclusive capital market has the potential to make a significant contribution to the country's economic development. It is a vehicle for mobilizing long-term savings, improved access to finance, improved corporate governance, and attracting domestic and foreign investment. The capital market is also considered a means of broadening financial inclusion as well as reducing the economy's dependence on the banking sector.

5.3 RECOMMENDATIONS

Based on the findings and conclusions, the study forwards the following recommendations for financial institutions, policymakers, and market participants to enhance the operation capital market in Ethiopia.

Recommendations to overcome operational challenges

- ✓ Strengthen Legal and Regulatory Frameworks: Ethiopian Capital Market Authority (ECMA), in association with the Ministry of Finance and National Bank of Ethiopia (NBE), needs to speed up preparation and passage of the overall capital market law, e.g.,

investor protection rules, conflict resolution, supervision, penalty and sanction for malpractices.

- ✓ **Improve Technological Infrastructure:** Investment is required in sophisticated digital systems such as trading platforms, central securities depositories, and real-time data tools.
- ✓ **Develop Human Capital and Expertise:** National training and certification program in association with universities and professional bodies must be launched to bridge the shortage of experienced market professionals.
- ✓ **Enhance Public Financial Literacy:** Public enlightenment campaigns through television, radio, schools, and community programs should be undertaken with a view to raising awareness and confidence in the capital market.
- ✓ **Establish a Central Market Information System:** There should be a centrally maintained, publicly accessible issuer database of trading volumes and disclosures, along with issuer details, to promote transparency.

Recommendations for Enhancing Stakeholder Readiness

- ✓ **Organize Specialized Capital Market Departments in Financial Institutions:** Banks must organize specialized departments. this department should be operated by professionals trained in trading, compliance, financial analysis, and risk management to achieve operating excellence and market credibility for advisory, underwriting, and trading of securities.
 - ✓ **Financial knowledge must be encouraged so that more citizens will participate in the capital market.** Financial institutions must conduct educational programs, workshops, and media campaigns describing the benefits, risk, and method of investment in the capital market.
 - ✓ **Build Institutional Capacity in Regulatory Institutions:** ECMA and NBE need to employ capable staff members and establish advanced RegTech(Regulatory Technology) infrastructure.
 - ✓ **Stakeholder Coordination Mechanisms Formalize:** There should be a permanent Capital Market Development Council to better serve as strategic coordination.
- Set Stakeholder Readiness Benchmarks:** Use benchmarks to establish the financial and technical readiness of institutions.

- ✓ Financial literacy must be encouraged so that more citizens will participate in the capital market. Institutions must arrange training courses, seminars, and mass media education courses on the benefits, risk, and method of investment in the capital market. Organize Joint Capacity Building Programs: Partner with schools to offer training in capital markets and internships.

Recommendations to Leveraging Economic Opportunities

- ✓ Promote Capital Market as Alternative Source of Finance of SMEs: Simplify listing processes to allow SMEs to access public funds.
- ✓ Introduce Financial Products for Long-Term and Institutional Investors: Develop products aligned to long-term investment strategy.
- ✓ Encourage Foreign Investment on Policy Clarity and Incentives: Have tax relief and liberal repatriation policies.
- ✓ Synchronize Capital Market Development with National Development Objectives: Align capital market objectives with national economic plans.
- ✓ Create Sector-Specific Investment Vehicles: Create instruments like green bonds or agricultural funds to fund country priorities.

Recommendations to Strategic Actions to Overcome Constraints and Foster Growth (

- ✓ Policymakers must enact a transparent and enforceable legal structure to govern the capital market. This entails finalizing legislation outlining market behavior, investor protection, disclosure requirements, and institutional standards to create a secure and trustworthy environment for investments.
- ✓ Operationalizing the Ethiopian Securities Exchange (ESX) must be prioritized. Policymakers must ensure that the exchange is based on appropriate governance structures, surveillance systems, and trading platforms to enable effective and transparent securities transactions.
- ✓ Institutional capacity building should be given high priority by ensuring that institutions such as the Ethiopian Capital Market Authority (ECMA) and the National Bank of

Ethiopia (NBE) have needed resources, capacity development, and available technology provided to them. It will build the capacity of such institutions to regulate and enforce.

- ✓ Phased Rollout of the Market with Pilot Programs: Launch a few of the products to pilot-test systems and develop stakeholder capacity.
- ✓ Incentivize Early Entrance with Fiscal Benefits: Offer fiscal incentives and guarantees to incentivize early entrants.
- ✓ Institutionalize Continuous Monitoring and Feedback Loops: Periodic review of policies and consultations with stakeholders are a must.
- ✓ Include Regulatory Sandboxes for Innovation: Allow testing of fintech within favorable regulatory conditions.
- ✓ Financial inclusion must also be an even higher policy priority. Policy makers must ensure that access to capital is provided to low income segments e.g., individual investors and SMEs market opportunities with ease of procedures and lower entry barriers.

Future Research Directions

Despite the fact that the present study is restricted to explore the background of operational challenges and possibilities of the Ethiopian capital market, there are some issues which call for deeper investigation in the future. The lack of financial literacy, and hence low levels of sophistication endorsing the merits of capital markets, in Ethiopia, and the poor public understanding regarding capital market advantages are major roadblocks to a developing market. Future studies could examine how financial education programs and public awareness campaigns tailored to Ethiopia's socio-economic and cultural context might enhance investor engagement. Such work would offer important knowledge about policy choices for creating market access and acceding to capital markets.

Other promising area for future research is the possible complementary role of Ethiopia's banking system and a working capital market. A cohesive relationship between these two financial systems is crucial for creating an integrated and efficient financial ecosystem. Further studies could investigate how the banking sector might support capital market operations, particularly in areas such as credit mechanisms, liquidity provision, and technology integration.

Comparative research on countries that have successfully integrated their banking systems with capital markets could also provide practical lessons applicable to Ethiopia's unique context.

By addressing these broader socio-economic and systemic factors, future studies could complement the findings of this research and contribute to a deeper understanding of Ethiopia's financial market landscape. Such research would not only fill critical gaps in the literature but also provide actionable insights to support the sustainable development of a robust and inclusive capital market in Ethiopia.

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APPENDEIX

ADDIS ABABA UNIVERSITY

SCHOOL OF COMMERCE

MSC IN CORPORATE FINANCE: SPECIALITY IN INVESTMENT MANAGEMENT

Dear Respondents,

I am a master's student of corporate finance: specialty in investment management at Addis Ababa University School of Commerce. I would like to express my sincere appreciation for your generous time, and honest and prompt responses to my questions.

This questionnaire is developed for an academic effort planned for the collection of data to conduct a thesis paper on the title “**capital market operation in Ethiopia : potential challenges and opportunities**”, to fulfill the Addis Ababa University’s requirement set for awarding of a MSC in corporate finance: specialty in investment management. The questionnaire will take approximately 15-20 minutes to complete and your genuine response to each question is paramount to the success of this study. The information obtained from this questionnaire will be kept confidential and will not be used for any other purposes. Hence, I am kindly asking respondents to give your candid information.

NB:

- It is not necessary to write your name.
- Try to address all the questions given below.
- For the closed-ended questions use the (√) mark for your choice in the given box Contact.

Address If you have any queries, please do not hesitate to contact me I am available at your convenience at (Mobile: +251920723956) Email: medkalkidan@gmail.com

Thank you for your cooperation!

PART 1. DEMOGRAPHIC INFORMATION

INSTRUCTION: Please use the (√) mark for your choice in the given box

SECTION A: DEMOGRAPHIC INFORMATION

1. Gender

Male: Female:

2. Age group

I. 18-28:

II. 29-39:

III. 40 plus:

3. Years of experience in the financial sector:

I. less than 1 year:

II. 1-3years :

III. 4-6 years :

IV. More than 6 years

4. Type of organization:

I. Commercial Bank

- II. University scholar
- III. Trannies of soc
- IV. Regulatory body
- V. Ethiopian securities exchange (ESX)

INSTRUCTION: Please use the (√) mark for your choice in the given box

PART 2: QUESTIONS DIRECTLY RELATED WITH THE STUDY

2.1. Here under the questions about Capital market operation in Ethiopia: potential prospects and challenges. You are kindly requested to put “√” mark on the box that represents your degree of agreement.

Please indicate your level of agreement with the following statements:

1 = Strongly Disagree 2 = Disagree 3 = Neutral 4 = Agree 5 = Strongly Agree

| No. | STATEMENTS | LIKERT SCALE | | | | |
|------------------------|-----------------------------------------------------------------------------------------|--------------|---|---|---|---|
| | | 5 | 4 | 3 | 2 | 1 |
| Operational Challenges | | | | | | |
| 1. | Ethiopia lacks a strong legal and regulatory framework for capital market operations | | | | | |
| 2. | Institutional capacity is inadequate to manage and supervise capital market operations. | | | | | |
| 3. | Public awareness and investor literacy about capital markets is low. | | | | | |

| | | | | | | |
|----------------------------------|------------------------------------------------------------------------------------------------|--|--|--|--|--|
| 4. | There is a lack of trust in financial markets by potential investors. | | | | | |
| 5. | Political and economic instability affects the viability of capital market operations. | | | | | |
| 6. | Current ICT infrastructure is sufficient to support capital market operations | | | | | |
| 7. | There is a shortage of skilled professionals in capital market roles. | | | | | |
| 8. | Institutional gaps exist that may hinder smooth capital market operations. | | | | | |
| Stakeholder Readiness | | | | | | |
| 9. | Financial institutions in Ethiopia are prepared to support capital market operation. | | | | | |
| 10. | Regulatory bodies have the capacity to oversee capital market activities. | | | | | |
| 11. | Private investors are prepared to engage in capital market activities. | | | | | |
| 12. | Existing laws support the introduction of capital market instruments. | | | | | |
| 13. | There is strong collaboration among stakeholders to support capital market development. | | | | | |
| 14. | Universities and training centers are preparing professionals for the capital market industry. | | | | | |
| 15. | Automation and digital platforms are essential for market efficiency. | | | | | |
| Opportunities of Capital Markets | | | | | | |

| | | | | | | |
|--------------------------------------|-------------------------------------------------------------------------------------------------------------------------|--|--|--|--|--|
| 16. | Capital markets will increase access to finance for businesses. | | | | | |
| 17. | Capital market development will enhance national economic growth. | | | | | |
| 18. | Capital markets promote transparency and accountability in the financial system. | | | | | |
| 19. | capital markets will improve savings and investment culture among citizens | | | | | |
| 20. | Capital markets will diversify financial intermediation beyond the banking sector. | | | | | |
| Institutional and Regulatory Support | | | | | | |
| 21. | Strengthening regulatory frameworks and enforcement capacity is essential for capital market development. | | | | | |
| 22. | Developing investor education and awareness programs will improve market participation. | | | | | |
| 23. | Establishing modern trading platforms and ICT infrastructure is necessary for efficient capital market operation. | | | | | |
| 24. | Building human capital through education and professional certification will support sustainable capital market growth. | | | | | |
| 25. | Encouraging participation from private and foreign investors is crucial for deepening the capital market. | | | | | |
| 26. | Promoting strong coordination among key stakeholders is necessary for effective implementation. | | | | | |

Open-Ended Questions

1. What is the most significant operational challenge in Ethiopia's capital market?
(Open-ended response)
2. What specific recommendations do you have to enhance the efficiency of capital market operations in Ethiopia?
(Open-ended response)

Appendix 2: An Interview Guide

ADDIS ABABA UNIVERSITY SCHOOL OF COMMERCE

MSC IN CORPORATE FINANCE: SPECIALITY IN INVESTMENT MANAGEMENT

Dear Respondents,

I am a master's student of corporate finance: specialty in investment management at Addis Ababa University School of Commerce. I would like to express my sincere appreciation for your generous time, and honest and prompt responses to my questions.

This Interview question is developed for an academic effort planned for the collection of data to conduct a thesis paper on the title “capital market operation in Ethiopia : potential challenges and opportunities”, to fulfill the Addis Ababa University’s requirement set for awarding of a MSC in corporate finance: specialty in investment management. Your insights and expertise are highly valued, and your responses will be treated with strict confidentiality. The information gathered will be used exclusively for academic purposes and will contribute to a deeper understanding of the current state, challenges, and opportunities related to capital market infrastructure in Ethiopia. Your participation in this interview will help generate informed recommendations for policymakers, financial institutions, and market participants to enhance the development of a well-functioning capital market. We kindly request your honest and thoughtful responses, as they will be instrumental in shaping valuable insights for this study.

Thank you for your cooperation!

Interview Questions

1. What do you see as the major operational or regulatory challenges that might hinder the development of functional capital market?
2. In your opinion how prepared are financial institutions regulators and investors to support a functioning capital market?
3. What steps do you believe stakeholders should take to enhance their readiness?
4. What economic opportunities do you think a capital market could bring to Ethiopia?
5. What infrastructure (technological, human capital) do you think is most critical?
6. What strategies or policy measure would you recommend to overcome the challenges and ensure the market's success?