

COLLEGE OF BUSINESS AND ECONOMICS

DEPARTMENT MANAGEMENT

POST-LAUNCH CHALLENGES AND EMERGING PROSPECTS IN ETHIOPIA'S CAPITAL MARKETS

BY:

MERON BERHANU

ADVISOR:

HABTAMU ENDRIS(PhD)

JUNE, 2026

ADDIS ABABA, ETHIOPIA



COLLEGE OF BUSINESS AND ECONOMICS

DEPARTMENT OF MANAGEMENT

POST-LAUNCH CHALLENGES AND EMERGING PROSPECTS IN ETHIOPIA'S CAPITAL MARKETS

A THESIS SUBMITTED TO ADDIS ABABA UNIVERSITY, COLLEGE OF BUSINESS AND ECONOMICS, DEPARTMENT OF MANAGEMENT, FOR THE PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE DEGREE OF MASTER OF ARTS IN INTERNATIONAL BUSINESS

BY: MERON BERHANU

ADVISOR: HABTAMU ENDRIS (PhD)

JUNE, 2026

ADDIS ABABA, ETHIOPIA

DECLARATION

This thesis entitled "Post-Launch Challenges and Emerging Prospects in Ethiopia's Capital Markets" has been prepared by me and presented to the University of Addis Ababa as the requirement for obtaining a Master of Arts in International Business Degree. The research has been conducted independently, guided by my supervisor, Dr. Habtamu. All sources of information consulted have been appropriately cited. This work is being presented for the first time as a requirement for this award.

Name: Meron Berhanu

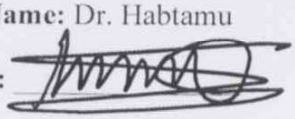
Signature: _____

Date: June, 2026

CERTIFICATE

I hereby certify that the thesis entitled "Post-Launch Challenges and Emerging Prospects in Ethiopia's Capital Markets" presented by Meron Berhanu to the Department of Management at the College of Business and Economics, Addis Ababa University, is an authentic piece of research performed by her under my supervision. This thesis is of adequate scope and standard to fulfill partially the requirements of the Master of Arts in International Business degree program.

Advisor Name: Dr. Habtamu

Signature: 

Date: June, 2026

CERTIFICATE OF APPROVAL

This thesis, titled **"Post-Launch Challenges and Emerging Prospects in Ethiopia's Capital Markets"** by Meron Berhanu, has been approved by the examining board for the partial fulfillment of the requirements for the degree of Master of Arts in International Business.

Examination Board Signatures:

Asmamaw Argeta, PhD		21/06/2026
External examiner	Signature	Date
Degene T.		23/6/2026
Internal examiner	Signature	Date
Dean SGS	Signature	Date

ACKNOWLEDGEMENT

I would like to sincerely thank Almighty God for providing me with the necessary strength, knowledge, and determination throughout the process of researching.

I extend my profound appreciation to my supervisor, Dr. Habtamu, for the critical role he played by offering me constructive criticism, consistent motivation, and valuable insights in the course of this study.

I am truly thankful to all the participants in the study from regulatory bodies, market intermediaries, institutional investors, academic experts, and consultant companies.

My sincere appreciation goes to the Ethiopian Capital Market Authority (ECMA) and the Ethiopian Securities Exchange (ESX) for granting me access and information needed. The Department of Management of Addis Ababa University is thanked for their academic assistance.

My sincere gratitude goes out to my family members for their continued support and encouragement towards me. They are my pillar of strength.

Lastly, I thank all my friends and co-workers for their moral support and intellectual discussion.

Meron Berhanu

June, 2026

Addis Ababa, Ethiopia

TABLE OF CONTENTS

DECLARATION iii
CERTIFICATE iv
CERTIFICATE OF APPROVAL v
ACKNOWLEDGEMENT vi
LIST OF TABLES xi
ABBREVIATIONS & ACRONYMS xii
Abstract xiii
CHAPTER ONE 1
INTRODUCTION 1
1.1. Background of the Study 1
1.2. Statement of the Problem 3
1.3. Research Questions 8
1.4. Objectives of the Study 8
1.4.1. General Objective 8
1.4.2. Specific Objectives 8
1.5. Scope of the Study 9
1.6. Significance of the Study 10
1.7. Organization of the Study 11
CHAPTER TWO 11
REVIEW OF RELATED LITERATURE 11
2.1. Introduction 12
2.2. Theoretical Framework 12
2.2.1. Efficient Market Hypothesis (EMH) 12
2.2.2. Capital Asset Pricing Model (CAPM) 13
2.2.3. Interest Rate Parity (IRP) 13
2.2.4. Institutional Theory 14
2.2.5. Financial Development Theory 15
2.3. Challenges Affecting Capital Market Efficiency 16
2.3.1. Regulatory and Institutional Challenges 16
2.3.2. Infrastructural and Technological Deficiencies 17
2.3.3. Market Awareness and Investor Participation 18
2.3.4. Macroeconomic and Political Factors 19

2.4. Overview of African Capital Markets 20
2.4.1. Historical Development and Current Landscape 20
2.4.2. Comparative Country Experiences 20
2.4.3. Synthesized Lessons from African Capital Markets for Ethiopia 23
2.5. Empirical Insights on Capital Market Development 24
2.5.1. Market Integration and Segmentation 24
2.5.2. Capital Flows and Economic Growth 25
2.5.3. Financial Crises and Capital Market Behavior 25
2.5.4. Empirical Studies on Capital Markets in Frontier African Economies 26
CHAPTER THREE 27
RESEARCH METHODOLOGY 27
3.1 Introduction 27
3.2 Research Philosophy 28
3.3 Research Approach 28
3.4 Research Design 29
3.5. Target Population, Sample Size, and Sampling Procedure 29
3.5.1. Target Population 29
3.5.2. Sample Size Determination 29
3.5.3. Sampling Techniques 30
3.5.4. Sampling Proportions 31
3.6Sources of Data 32
3.7. Data Collection Procedures 32
3.8 Validity and Reliability 33
3.8.1 Validity 33
3.8.2 Reliability 33
3.8.3 Trustworthiness 34
3.9 Method of Analysis 34
3.10 Ethical Consideration 35
CHAPTER FOUR 36
PRESENTATION, ANALYSIS, AND INTERPRETATION OF FINDINGS 36
4.1 Introduction 36
4.2 Demographic Profile of Survey Respondents 37
4.3 Regulatory Environment and Governance 38

4.3.1 Regulatory Clarity and Enforcement Capacity 39
4.3.2 Minority Shareholder Protection 40
4.3.3 Cross-Regulatory Coordination 41
4.3.4 Policy Consistency and Foreign Investor Confidence 43
4.3.5 Synthesis of Regulatory Challenges 44
4.4 Market Operations and Infrastructure 45
4.4.1 Trading Platform Reliability 45
4.4.2 Clearing and Settlement Deficiencies 47
4.4.3 Liquidity and Information Availability 48
4.4.4 Synthesis of Infrastructure Challenges 50
4.5 Market Participants and Capacity 51
4.5.1 The Financial Literacy Paradox 51
4.5.2 Institutional Investor Caution 53
4.5.3 Intermediary Capacity and Company Readiness 54
4.5.4 Informal Savings Mechanisms 55
4.5.5 Synthesis of Participation and Capacity Challenges 56
4.6 Macroeconomic and External Environment 57
4.6.1 Macroeconomic Conditions as Binding Constraint 58
4.6.2 Currency Risk and Foreign Investment 59
4.6.3 Policy Support and Political Stability 60
4.6.4 Synthesis of Macroeconomic Findings 60
4.7 Prospects and Opportunities 61
4.7.1 SOE Privatization as Market Catalyst 62
4.7.2 Diaspora Finance as Low-Hanging Opportunity 63
4.7.3 Product Innovation: Islamic and Green Finance 64
4.7.4 Regional Integration 65
4.7.5 Synthesis of Opportunities 66
4.8 Integration of Qualitative and Quantitative Findings 66
CHAPTER FIVE 70
SUMMARY, CONCLUSIONS, AND RECOMMENDATIONS 70
5.1 Introduction 70
5.2 Summary of the Study 70
5.3 Conclusions 71

5.4 Recommendations 72
5.5 Limitations and Future Research Directions 73
References 75
Appendix I: Questionnaire 83
Appendix II: Interview Guide 86

LIST OF TABLES

Table 1: Comparative Summary of Selected African Capital Markets 22
Table 2: Sampling Proportions (n = 258) 31
Table 3: Cronbach's Alpha Reliability Coefficients 33
Table 4: Demographic Characteristics of Survey Respondents (N = 233) 37
Table 5: Regulatory Environment and Governance (N = 233) 38
Table 6: Market Operations and Infrastructure (N = 233) 45
Table 7: Market Participants and Capacity (N = 233) 51
Table 8: Macroeconomic and External Environment (N = 233) 57
Table 9: Prospects and Opportunities (N = 233) 61
Table 10: Integration Matrix: Qualitative and Quantitative Convergence 67

ABBREVIATIONS & ACRONYMS

AfDB - African Development Bank

CAPM - Capital Asset Pricing Model

ECMA - Ethiopian Capital Market Authority

EMH - Efficient Market Hypothesis

ESX - Ethiopian Securities Exchange

FGD - Focus Group Discussion

FPI - Foreign Portfolio Investment

IMF - International Monetary Fund

IOSCO - International Organization of Securities Commissions

IRP - Interest Rate Parity

KII - Key Informant Interview

NBE - National Bank of Ethiopia

NSE - Nairobi Securities Exchange

RQ - Research Question

SD - Standard Deviation

SME - Small and Medium Enterprise

SOE - State-Owned Enterprise

UNECA - United Nations Economic Commission for Africa

Abstract

The current study has examined the challenges that have been facing Ethiopia's capital market after its establishment, focusing particularly on the ESX. Mixed method research design, which had a qualitative perspective, was used whereby data collection involved 233 questionnaire surveys, 14 in-depth interviews, and 4 focus group discussions. It was found out that the main problems in this industry emanating from macroeconomic factors included an inflation rate of around 25 percent, unstable exchange rates, and foreign currency shortages. With regard to regulatory issues, poor protection of minority shareholders according to the Commercial Code of 1960, absence of secondary legislative measures, and inadequate coordination between ECMA and NBE were identified. Other difficulties identified in relation to infrastructure problems included inefficiencies in clearing and settlement operations as well as disruptions in trading operations. There was also a contradiction with regard to the level of financial literacy among the respondents since professional respondents indicated a high awareness of the public, but the actual finding was that less than 15 percent of adults in Ethiopia were financially literate. However, the study highlights several opportunities, such as privatization, investment by Diasporas, Islamic financing, and green bonds. According to these results, the study recommends that efforts be made to stabilize the economy in order to achieve single-digit inflation, updating the 1960 Commercial Code in favor of minority shareholders, passing all subsidiary legislation within six months, improving clearing and settlement facilities in order to avoid disrupting trading activities, initiating a financial literacy campaign throughout the nation using informal savings mechanisms such as iddir and iqub, and developing Diaspora investment products.

Keywords: *Ethiopian Securities Exchange, capital market development, frontier markets, macroeconomic instability, regulatory capacity, Diaspora finance, Islamic finance, Ethiopia*

CHAPTER ONE

INTRODUCTION

In this chapter, the basic assumptions regarding the study on the problems and future prospects of the capital markets of Ethiopia are discussed. First of all, the background of the capital market in Ethiopia is described. In particular, the notion of financial markets and their contribution to economic growth will be discussed. The problem statement is provided next where the discrepancy between the advantages of having a capital market established and the issues associated with the functioning of the market since the introduction of the ESX is revealed. Further, the research questions and objectives of the study (both general and specific) are introduced. Then, the scope and limitations of the study are defined. Finally, the significance of the study is outlined.

1.1. Background of the Study

The capital markets constitute one of the most crucial elements within the structure of financial systems and contribute significantly to economic development. These markets facilitate capital accumulation and allocation, allow for risk sharing, and provide financial services to governments, firms, and individuals (Madura, 2014). Stock markets came about during Europe's First Industrial Revolution and are currently regarded as key institutions for conducting securities transactions and allocating savings for productive purposes (Guiso & Jappelli, 2005).

In terms of history, the capital market of Ethiopia has always been bank-dominated, thus making it hard for capital intensive sectors, such as the manufacture, infrastructure, and technology sectors, to access long term capital financing (World Bank, 2022; Abebe, 2021; IMF, 2023; African Development Bank, 2021). The recent formation of the Ethiopian Securities Exchange (ESX) and Ethiopian Capital Market Authority (ECMA) marks an important transformation into market-based capital financing. Empirical evidence shows that effective capital markets lead to improved capital allocation efficiency, financial deepening, innovations, and higher productivity (Levine & Zervos, 1998; Beck & Levine, 2004; Yartey & Adjasi, 2007). Also, effective stock markets improve corporate governance by ensuring transparency and higher monitoring efforts (World Bank, 2022).

The development of capital markets in Ethiopia occurs within a certain set of characteristics that are part of the economic, social and political environment of Ethiopia. They include, inter alia, a

history of state-led growth; a tiny under-developed banking sector; significant levels of informality within the economy; and political/security instability. New developments to liberalize the economy by means of partial privatization of public companies, along with integration of the country's financial institutions with international financial markets, open up new possibilities for the creation of a stock exchange (FDRE, 2021; World Bank, 2022). A study across countries shows that better-quality institutions help increase private credit and total factor productivity in moving from bank-based to market-based financial systems (IMF, 2023).

However, Ethiopia is still in the early stages of establishing its capital markets. Difficulties often encountered in the process of building up nascent securities exchanges include poor infrastructure, unclear regulatory signals, weak enforcement, and insufficient public awareness of securities exchanges (Abebe, 2021; Esayas Ephrem, 2022). All these difficulties are typical of other emerging countries in their initial period (Kunt et al., 2015). As seen in experience of other countries, such as Rwanda and Kenya, carefully-designed securities exchange plays an important role in economic transformation (UNECA, 2023).

Instability in the macreconomic environment, which is characterized by excessive and highly volatile inflation, exchange rate pressures, and limited foreign exchange reserves, makes market development difficult through higher cost of capital and discouraging investments (IMF, 2023). In addition, low financial inclusion, alongside poor understanding of investments, limits the number of retail investors since over 60 percent of Ethiopians lack access to banking services, and there have been minimal financial literacy campaigns (African Development Bank, 2021; Biazin & Waktola, 2021). Insufficient clearing and settlement mechanisms and trading platforms pose additional challenges.

However, despite the above challenges, the ESX has the following benefits: mobilization of savings in Ethiopia, including informal savings such as iddir and iqub, mobilization of long-term funds for SMEs and infrastructural developments, and attracting foreign capital, which would bring better practices and know-how (Levine & Zervos, 1998; Beck & Levine, 2004; Allen et al., 2011). Achieving success will be determined by building up the regulatory framework, upgrading market infrastructure, ensuring macreconomic stability, and educating investors on financial markets.

The study analyzed the expectations and experiences of Ethiopia's emerging capital market since the launch of the ESX. The primary concern is to analyze the challenges faced and opportunities identified by the stakeholders so as to provide informed recommendations. An attempt has been made to ensure that all the references cited within this paper include the most recent findings related to the subject under discussion.

1.2. Statement of the Problem

The establishment of the Ethiopian Securities Exchange (ESX) in January 2024 marked a watershed moment in Ethiopia's financial sector development, transitioning from a bank-dominated system to a market-based financing framework (World Bank, 2022). This institutional innovation was intended to address critical financing gaps that have long constrained Ethiopia's economic transformation, particularly in capital-intensive sectors such as manufacturing, infrastructure, and technology (Abebe, 2021; IMF, 2023). Theoretically, Financial Development Theory (Levine & Zervos, 1998; Beck & Levine, 2004) posits that well-functioning capital markets contribute to economic growth through efficient capital allocation, risk diversification, and enhanced corporate governance. However, the successful realization of these benefits depends critically on the presence of enabling institutional, regulatory, and macroeconomic conditions conditions that empirical research suggests are often deficient in frontier African markets (Yartey & Adjasi, 2007; Allen et al., 2011).

Despite the strategic importance of Ethiopia's capital market development, the ESX faces a complex array of post-launch challenges that threaten to undermine its potential contributions. These challenges operate at multiple interconnected levels and manifest in ways that are particularly acute in the Ethiopian context.

First, regulatory and institutional deficits pose significant barriers to market integrity and investor confidence. While Proclamation No. 1248/2021 established the Ethiopian Capital Market Authority (ECMA) as an independent regulator, empirical evidence suggests that enforcement capacity remains weak (Adonay, 2021). The Commercial Code of 1960, which governs corporate governance and shareholder rights, predates modern financial market requirements and provides inadequate protection for minority shareholders a critical concern given that International Organization of Securities Commissions (IOSCO, 2017) principles identify investor protection as foundational to market development. Secondary legislation, particularly regarding foreign

portfolio investment, has not been finalized, creating regulatory uncertainty that discourages international participation (IMF, 2025a). Furthermore, coordination gaps between ECMA and the National Bank of Ethiopia (NBE) have delayed implementation of institutional investment mandates, constraining participation by pension funds and insurance companies that are legally authorized but practically unable to invest (World Bank, 2024).

This regulatory fragmentation is consistent with patterns observed in other frontier markets where unclear separation of responsibilities between central banks and securities regulators limits institutional participation (World Bank, 2024; IMF, 2025b). The absence of clear regulatory guidance on borderless transactions and novel instruments further compounds the problem, creating an environment where potential investors face significant uncertainty about the legal and operational framework governing their investments (El Wassal, 2013).

Second, infrastructural and operational weaknesses compromise market efficiency and reliability. Although the ESX trading platform has been launched, it has experienced at least three unplanned trading halts due to technical failures in its first year of operation (ESX, 2026). Clearing and settlement processes remain underdeveloped, and the ecosystem of complementary institutions custodian banks, research analysts, and investment banks that are essential for market functioning is virtually absent (Esayas Ephrem, 2022). The problem is compounded by a "chicken and egg" dilemma: custodians and analysts will only invest in infrastructure when trading volumes justify the investment, but trading volumes remain low precisely because the necessary infrastructure is absent (Allen et al., 2011).

This infrastructure deficiency directly affects market accessibility and operational efficiency, creating barriers for both domestic and foreign investors. According to the Committee on Payments and Market Infrastructures and IOSCO (2012), efficient clearing, settlement, and custody arrangements are prerequisites for financial market stability, and their absence in Ethiopia represents a significant operational risk that could undermine investor confidence (World Bank, 2024). The lack of reliable market data and research analysis further compounds these challenges, as investors cannot make informed decisions without accurate and timely information.

Third, limited market participation reflects broader patterns of financial exclusion and low financial literacy. The African Development Bank (2021) estimates that over 60% of Ethiopians lack access to formal financial services, while Biazin and Waktola (2021) found that more than

70% of Addis Ababa residents lack basic capital market knowledge. The reliance on informal savings mechanisms such as iddir and iqub, while reflecting strong social capital and trust networks, channels funds away from formal capital markets (Allen et al., 2011; Biazin & Waktola, 2023). This is particularly problematic given that Guiso and Jappelli (2005) demonstrated that financial awareness defined as knowledge that a stock market exists and understanding how to participate is a significant predictor of actual market participation.

In communities where financial literacy is low, many households remain unaware of capital market opportunities, reinforcing informal savings systems and perpetuating financial exclusion. Institutional investors exhibit a "wait-and-watch" approach, allocating less than 1% of their portfolios to ESX-listed securities despite regulatory allowances of up to 5% (ECMA, 2026b). This cautious stance reflects both fiduciary responsibilities and uncertainty about market viability, creating a coordination problem that reinforces low liquidity and limits price discovery (Beck & Levine, 2004).

Fourth, and perhaps most critically, macroeconomic instability serves as a binding constraint that fundamentally undermines the economic logic of equity investment. Ethiopia's inflation rate, which has exceeded 20% for several consecutive years, effectively eliminates positive real returns from equity investments (IMF, 2025a). Simultaneously, government treasury bills offer risk-adjusted returns of 18%, providing an attractive risk-free alternative that diverts potential capital away from the ESX (World Bank, 2025b). According to the Capital Asset Pricing Model (CAPM) (Sharpe, 1964; Lintner, 1965), investors require compensation for systematic risk; however, when macroeconomic risk eliminates the risk premium, rational investors withdraw from equity markets. This is precisely what is occurring in Ethiopia, where the negative real returns on equity investments make participation economically irrational (IMF, 2025a).

The exchange rate float in late 2024, while necessary for macroeconomic adjustment, introduced significant currency volatility that foreign investors cannot hedge due to the absence of forward currency markets (IMF, 2025a). Foreign exchange shortages continue to constrain the repatriation of profits and dividends, creating additional risks for international portfolio investors (U.S. Department of State, 2025). According to Interest Rate Parity (IRP) Theory (Keynes, 1923; Hodrick, 1987), deviations from covered interest parity are greater and more erratic in emerging markets, exposing international investors to unhedged currency risk (Du & Schreger, 2024).

In Ethiopia's segmented foreign exchange market, where no forward markets exist, these deviations are particularly pronounced, forcing foreign investors to either accept significant currency risk or simply avoid the market altogether (Froot & Thaler, 1990). The combination of high inflation, exchange rate uncertainty, and foreign exchange shortages creates a macroeconomic environment that fundamentally contradicts the conditions necessary for capital market development (IMF, 2025a; World Bank, 2025b). This macroeconomic instability not only deters foreign investment but also undermines domestic investor confidence, as the erosion of purchasing power through inflation makes long-term equity investment unattractive compared to short-term government securities.

Despite the significance of these challenges and the strategic importance of Ethiopia's capital market development, there exists a substantial gap in empirical research. Existing studies have identified potential challenges through theoretical analysis or pre-launch assessments (Adonay, 2021; Esayas Ephrem, 2022; Biazin & Waktola, 2021), but no comprehensive empirical study has systematically examined post-launch challenges and emerging prospects since the ESX became operational. This gap is particularly problematic because the dynamics of capital market development are context-specific.

Experiences from South Africa, Nigeria, Kenya, and Morocco offer generalizable lessons, but the specific institutional, political, and economic configuration in Ethiopia creates unique challenges that cannot be assumed from other contexts (Yartey & Adjasi, 2007; UNECA, 2023). Moreover, the post-launch period is critical for market legitimacy, as the first twenty-four to thirty-six months of an exchange's operation are decisive in establishing investor confidence, regulatory credibility, and market viability. Empirical evidence is urgently needed to inform timely interventions (World Bank, 2022).

Policy decisions require evidence that current research does not provide. Decisions about SOE privatization sequencing, regulatory reforms, diaspora investment products, and financial literacy campaigns require systematic stakeholder analysis (IMF, 2025a). Furthermore, theoretical refinement is needed, as the applicability of Western financial theories including the Efficient Market Hypothesis, Capital Asset Pricing Model, and Interest Rate Parity to frontier African markets with distinctive institutional characteristics requires empirical testing that has not been conducted (Bekaert & Harvey, 1995; El Wassal, 2013).

This research gap has significant implications for multiple stakeholders. Policymakers and regulators including ECMA, the National Bank of Ethiopia, and the Ministry of Finance require evidence on regulatory effectiveness to guide reform priorities and sequencing decisions. Without systematic empirical analysis, policy decisions risk being based on anecdotal evidence or untested assumptions (World Bank, 2024). Market participants such as brokers, institutional investors, and potential issuers need clarity on risks and opportunities to inform investment decisions and business planning.

The current information asymmetry between market participants and regulators undermines efficient market functioning (Adonay, 2021). Potential foreign investors lack independent assessment of market readiness, making it difficult to evaluate the risk-return profile of Ethiopian investments. This information gap perpetuates the "wait-and-watch" attitude observed among institutional investors (IMF, 2025a). Academic researchers need empirical evidence to develop theories appropriate to African frontier markets, as the current reliance on theories developed in Western contexts limits the explanatory power of research on African financial development (Yartey & Adjasi, 2007; El Wassal, 2013).

Finally, the Ethiopian public requires evidence to inform financial decision-making and assess potential benefits of market participation. Without credible information, informal savings mechanisms will continue to dominate, perpetuating financial exclusion (African Development Bank, 2021).

This study addresses the identified gap by providing a systematic, empirically-grounded analysis of post-launch challenges and emerging prospects in Ethiopia's capital markets. Through a qualitatively-dominant mixed methods approach involving surveys, key informant interviews, and focus group discussions, the research documents and analyzes the specific challenges that have emerged since ESX operations commenced across regulatory, infrastructural, human capital, and macroeconomic dimensions. The study examines the interrelationships among these challenges and their implications for market functioning, while also identifying emerging opportunities for market development, including diaspora finance, SOE privatization, Islamic finance, and green bonds.

By providing evidence-based recommendations for policymakers, regulators, and market participants, the study contributes to theoretical understanding of capital market development in

frontier African economies. The research responds to the practical urgency of these issues while contributing to academic knowledge about the dynamics of capital market development in low-income countries transitioning from bank-based to market-based financial systems. Through addressing the research gap, this study provides the empirical foundation needed to inform policy decisions, guide investment strategies, and advance theoretical understanding of frontier capital market development.

1.3. Research Questions

1. What specific regulatory and institutional challenges have emerged in Ethiopia's capital market?
2. How do technology and infrastructure conditions influence operational efficiency and market accessibility?
3. To what extent does financial literacy affect capital market participation?
4. How does macroeconomic instability (inflation, exchange rate volatility, and foreign exchange shortages) affect market performance and attractiveness?
5. How do political factors influence the development and stability of Ethiopia's emerging stock market?
6. What opportunities exist for domestic savings mobilization, SME financing, and global financial integration?

1.4. Objectives of the Study

1.4.1. General Objective

To explore the challenges and prospects that has emerged after the launch of Ethiopia’s capital markets.

1.4.2. Specific Objectives

1. To identify and analyze regulatory and institutional challenges including regulatory effectiveness, enforcement capacity, coordination mechanisms, minority shareholder protection, and gaps in secondary legislation.

2. To assess the influence of technology and infrastructure on operational efficiency and market accessibility including trading platform reliability, clearing and settlement efficiency, and stakeholder satisfaction.
3. To determine the extent to which financial literacy affects capital market participation including investor awareness, literacy-participation relationships, and barriers to retail involvement.
4. To evaluate the impact of macroeconomic instability on market performance and attractiveness including inflation effects on real returns, exchange rate volatility influence on foreign investment, and foreign exchange shortages impact on investor confidence.
5. To investigate the influence of political factors on capital market development and stability including policy consistency, political transition impacts, and stakeholder perspectives on political risk.
6. To explore opportunities for domestic savings mobilization, SME financing, and global integration including SOE privatization potential, diaspora finance feasibility, Islamic finance and green bond opportunities, and regional integration prospects.

1.5. Scope of the Study

The scope of this study is defined by its geographical, temporal, thematic, stakeholder, and content boundaries.

Geographically, the study was conducted in Addis Ababa, Ethiopia, where the Ethiopian Securities Exchange (ESX) and Ethiopian Capital Market Authority (ECMA) are headquartered, and where the majority of financial institutions and market intermediaries are located. While the findings may have relevance to other regions, the study does not include perspectives from other Ethiopian cities.

Temporally, the study focused on the post-launch period of Ethiopia's capital market, specifically from the operational launch of the ESX in January 2024 through the data collection period in April-June 2026 (approximately 27 months post-launch). This timeframe captures the critical early development stage of the market but does not provide a longitudinal perspective.

Thematically, the study examined challenges and prospects across five dimensions: regulatory and institutional environment, market operations and infrastructure, market participants and human capacity, macroeconomic and external environment, and opportunities for market development.

Stakeholder-wise, the study included perspectives from six categories: regulators (ECMA), market operators (ESX), financial market intermediaries (brokerage firms), institutional investors (pension funds, insurance companies, commercial banks), academic and research experts, and consulting and advisory firms.

Content-wise, the study specifically addresses capital market issues related to equity securities listing and trading. It does not address other financial market segments including over-the-counter (OTC) markets, government securities markets (treasury bills, bonds), money markets, foreign exchange markets, or alternative financial products (derivatives, structured products).

The study investigates the perspectives of stakeholders on post-launch challenges and prospects using a qualitatively-dominant mixed methods approach. It does not attempt to establish causal relationships through econometric modeling or predict future market performance through quantitative forecasting.

1.6. Significance of the Study

The importance of this study was multi-fold, as it impacted academic research, policymaking, market operations, and future research.

Academic Significance: The study added to the small body of empirical research related to frontier capital markets, particularly within the context of Ethiopia. Using well-known financial theories (EMH, CAPM, Institutional Theory), the study examined whether Western-based financial theories applied to frontier capital markets. In addition, the study provided empirical information about the behavior of the market after launching it. This information helped fill an important void highlighted by the literature review.

Policymaker Significance: The results of this study could be useful for the Capital Market Authority of Ethiopia (CMAP) and the Ministry of Finance when designing policies that promoted capital market development. It was necessary to understand the situation of the market to know how the gap between the intended and actual outcome could be narrowed.

Practical Significance: For market participants including potential issuers, institutional investors, brokers, and retail investors, this study offered a clear assessment of the risks and opportunities associated with participating in the ESX. For financial intermediaries, the findings highlighted areas requiring capacity building. For potential foreign investors, the study provided an independent evaluation of the market's readiness for portfolio investment.

Social Significance: By examining the potential of the capital market to mobilize domestic savings (including through informal mechanisms like iddir and iqub) and finance SMEs, this study addressed issues of financial inclusion and economic empowerment. The findings informed strategies to broaden access to capital market benefits beyond traditional elite investors.

Methodological Significance: The mixed-methods design employed in this study combining a stakeholder survey with in-depth interviews offered a replicable framework for studying other frontier capital markets in Africa and beyond. Future researchers could adapt the instruments and analytical approach developed in this study.

Finally, based on the integrated analysis of challenges and prospects, this study concluded with actionable recommendations for policymakers, regulators, and market participants to strengthen Ethiopia's capital market in its critical early years of operation.

1.7. Organization of the Study

This research study is organized into five chapters. The first chapter includes an introduction containing the background of the study, statement of the problem, research questions, objectives of the study, significance of the study, scope of the study, and organization of the study. The second chapter includes a review of existing literature on the topic of capital market theory, the development of financial theories, and empirical studies related to emerging markets that shared similar characteristics with Ethiopia. The third chapter includes information on research methodology which includes research design, data source, sampling techniques, and data collection and analysis methods. The fourth chapter focuses on data analysis and results. The fifth chapter summarizes the study and provides recommendations.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

2.1. Introduction

In this chapter, relevant theory and research studies were reviewed to understand the post-launch problems and potential opportunities associated with capital markets in developing nations, considering the specific situation of the Ethiopian market. This chapter was structured in several parts. First, important finance theories were discussed: the Efficient Market Hypothesis (EMH), Capital Asset Pricing Model (CAPM), Interest Rate Parity (IRP), Institutional Theory, and Financial Development Theory. These theories provided a useful perspective to understand the workings of capital markets. Second, a literature review was conducted on problems related to capital market efficiency across four dimensions: regulatory and institutional factors, infrastructural and technological constraints, market awareness and investor involvement, and macroeconomic/political conditions. Third, the evolution and current state of African capital markets were considered in comparative light of South Africa, Morocco, Egypt, Nigeria, and Kenya. Finally, this chapter ended by summarizing areas for further research.

2.2. Theoretical Framework

2.2.1. Efficient Market Hypothesis (EMH)

The efficient Market Hypothesis was developed by Fama (1970). According to EMH, all information regarding market transactions is reflected in prices of assets, and there cannot be any investor who makes abnormal profits without increasing the risk levels. Fama classified market efficiency into three categories: weak market efficiency, in which case previous prices do not contain enough information about future prices; semi-strong market efficiency, in which case all publicly available information, like annual reports and press releases, is reflected in the price of stocks; and finally strong market efficiency, in which case prices also reflect private and insider information. As per the theory developed by Fama, in an efficient market environment, there is no way to outperform the market through either technical or fundamental analysis.

EMH provides an essential tool with which to gauge whether the ESX exhibits efficient information processing. From empirical research carried out in emerging economies, it is clear that there is almost no evidence of the weak form of efficiency in the first few years of development due to low liquidity, high costs of transactions, asymmetric information, and lack of institutions (Bekaert & Harvey, 1995; Lo & MacKinlay, 1988). In such markets, past trends may predict future trends, and new information can be incorporated with some lags. For Ethiopia, it would be fair to

say that during the first few years of the establishment of the ESX, inefficient trends will prevail. This would be demonstrated by predictable trends and delayed incorporation of new information. However, there is evidence of inefficiencies due toincreased volatility and mispricing. It is therefore crucial for policymakers to understand that market inefficiencies should not be surprising and can be dealt with using appropriate policy measures (Bekaert & Harvey, 1995; World Bank, 2023).

2.2.2. Capital Asset Pricing Model (CAPM)

The Capital Asset Pricing Model was independently created by Sharpe (1964) and Lintner (1965). It is based on the assumption that there exists a linear association between expected returns and systematic risk in terms of the beta coefficient. According to the theory behind the model, investors get paid for assuming any undiversifiable risk associated with the market, but not for diversifiable company-specific risk. This is because diversification is the solution to minimizing such risks across a broad range of assets. The International Capital Asset Pricing Model adds more risk factors by considering currency risk, political risk, and taxation issues, among others.

The CAPM model is especially useful for evaluating how investors will price securities in the Ethiopian stock market. During the first years of operation in the stock exchange, systematic risk is bound to be high due to factors such as high inflation rates, an unstable exchange rate, political uncertainties during the transition period, and a lack of proper institutional mechanisms (IMF, 2023; World Bank, 2023). Foreign investors who follow the International CAPM model would be expected to earn high returns since they would need to receive a high risk premium for bearing currency inconvertibility and restrictions on the repatriation of profits, alongside weak legal protection for minority investors. Domestic investors, on the other hand, will not have enough asset types from which to choose for diversification purposes, making firm-specific risks un-diversifiable and thus a deviation from the CAPM assumptions. Therefore, the returns expected on securities in the Ethiopian Stock Exchange may have to be high compared to those in developed stock exchanges in order to draw both local and foreign investors (Beck & Levine, 2004; Fama & French, 1992).

2.2.3. Interest Rate Parity (IRP)

Interest Rate Parity theory sets forth the connection between interest rate differences and anticipated exchange rate movements in terms of two currencies. The Covered Interest Rate Parity

applies to forward contracts to preclude arbitrage activities, implying that the interest rate difference between two nations is matched with the forward premium or discount. The Uncovered Interest Rate Parity employs the expected spot exchange rates and also considers risk premiums. In the latter case, risk premiums denote the amount investors receive as a reward for the risk assumed due to exchange rates (Keynes, 1923; Hodrick, 1987; Froot & Thaler, 1990).

The principle of interest rate parity has vital implications for foreign portfolio investments in securities issued by firms in Ethiopia and traded in the ESX. Considering the historical presence of exchange rate management policies, occasional foreign currency shortages, and a premium in the parallel foreign exchange market in the country, the preconditions for the validity of IRP are unlikely to exist in the short term. The deviation from IRP creates risks for foreign investors as well as opportunities for arbitrage. The inability of foreign investors to hedge their currency risk effectively will make investment in the ESX more risky, particularly for equity securities with a long maturity. On the other hand, the government of Ethiopia needs to align the official foreign exchange rate with the parallel foreign exchange rate, make sufficient foreign currencies available, and develop forward currency markets to attract large inflows of foreign portfolio investments into Ethiopia (IMF, 2023; Ho & Odhiambo, 2021).

2.2.4. Institutional Theory

In addition to asset pricing theory, Institutional Theory, as developed by North (1990), stresses that the institutions, which include both the formal rules like laws, regulations, and agreements and the informal restrictions like norms, conventions, and societal knowledge, have a significant impact on economic transactions and market outcomes. From this point of view, institutional development affects the level of transaction costs, contract enforcement, property rights protection, and consequently, the performance of financial markets. Good institutions create certainty and improve cooperation in the market, whereas poor institutions generate rents and create information asymmetries leading to market failures.

The Institutional Theory is perhaps the most relevant theory in addressing the issues facing Ethiopia post launch in its capital markets. The Ethiopian Securities Exchange does not function on an island; it is affected directly by the wider institutional context within which it operates. Some of the key institutional determinants affecting the ESX include the legislation governing the capital market, which is provided for in the Capital Market Proclamation No. 1248/2021; the ability of

the judiciary to enforce contract agreements and safeguard shareholders' rights; the regulatory ability of the Ethiopian Capital Market Authority (ECMA) to oversee the intermediaries and impose sanctions; the accounting and auditing systems applied by the listed firms; and the social norm regarding transparency of operations within Ethiopian businesses. Any weakness in these institutional determinants would adversely affect the development of capital markets and make investment in the markets risky. In contrast, institutional progress in terms of ensuring that ECMA adheres to the International Organization of Securities Commission (IOSCO) principles, judicial independence, and improved financial reporting quality would spur development (IOSCO, 2017; North, 1990).

2.2.5. Financial Development Theory

The theory of financial development was introduced by Levine & Zervos (1998), Beck & Levine (2004), and others. This theory claims that well-functioning financial systems consisting of banks and capital markets contribute to economic growth via capital allocation to the most efficient investment projects, risk diversification, saving generation, and firm governance. According to financial development literature, stock market liquidity or ease of buying and selling stocks without having to significantly impact stock prices becomes an even stronger predictor of economic growth compared to the mere size of stock markets because it stimulates participation and reduces the cost of capital (Levine & Zervos, 1998). Moreover, the higher the financial depth, the more likely risky and high-payoff investments are to be financed.

Financial Development Theory constitutes the underlying rationale for setting up the Ethiopian Securities Exchange. According to this theory, once the ESX becomes functional, it will play a significant role in the economic transformation of Ethiopia by ensuring the availability of long-term sources of financing other than bank credits to capital-intensive industries like manufacturing, construction, and technology; enhancing corporate governance within the listed firms by increasing transparency and monitoring by the shareholders; channeling household savings saved in traditional modes like iddir and iqub or in less productive uses like land and precious metals; and securing foreign portfolio investments that bring not only financial resources but also financial skills into the country. But at the same time, the theory is aware of the limitations of premature securities market opening and thus warns that these advantages will accrue only when institutions supporting financial development are adequately established. Otherwise, market instability,

misappropriation, and the collapse of investors' confidence will ensue, as is evident in some developing countries where the process of financial development was pursued too hastily without proper institutional development (Beck & Levine, 2004; World Bank, 2022; IMF, 2023).

2.3. Challenges Affecting Capital Market Efficiency

Using the various theoretical lenses highlighted in the foregoing discussion, this paper highlights key insights from the empirical studies conducted regarding the issues affecting the efficiency of capital markets, especially focusing on developing and frontier economies.

2.3.1. Regulatory and Institutional Challenges

One of the prerequisites for capital markets' effective functioning is seen to be setting proper regulations and organizational frameworks. This matter was mentioned by the International Organization of Securities Commissions (IOSCO) and the International Monetary Fund (IMF), alongside some other standard-setting organizations, which outlined the general principles of market regulation, including such aspects as combating information asymmetries between issuers and investors, maintaining market integrity and protecting the investors, and ensuring the proper functioning of trade, clearance, and settlement systems (IOSCO, 2017; IMF, 2021; CPMI IOSCO, 2012; Financial Stability Board, 2022). The idea of sound market regulation is multi-faceted and involves various aspects, among which are supervision over intermediary organizations, such as brokers and investment advisers, conduct rule enforcement, and prudence measures.

Regulatory indicators proposed by IFC include information disclosure requirements, accounting methods, shareholder protection measures, and rules concerning foreign investments and dividenddistribution (IFC, n.d.). It is a perpetual challenge in designing effective regulations to achieve an appropriate balance between overregulation and underregulation. As El Wassal (2013) shows, overregulation may hinder the development of the market by making compliance too costly and preventing innovation, whereas underregulation exposes the market to fraudulent activity, manipulation, and extreme volatility. Four different types of regulatory systems have been delineated along a continuum from government-led regulation, limited SROs, strong SROs, to member-based SROs, each representing an appropriate framework depending on the level of institutional infrastructure, market size, and developmental status of a country.

For Ethiopia, the creation of the Ethiopian Capital Market Authority (ECMA), which operates as an autonomous regulator, is a proper institutional setup in accordance with international standards. Nevertheless, key challenges exist with regard to regulatory capacity. According to Adonay (2021), regulators' capacity to monitor violations of law, conduct investigations into such cases, and administer appropriate sanctions is usually low. Moreover, ambiguity in the regulations concerning certain types of market operations and the lack of clear guidance on borderless transactions and novel instruments, like cryptocurrencies, may hinder investment and trading. Another important issue that still needs to be addressed by the Ethiopian authorities is the protection of minority shareholders, as no litigation or arbitration related to ESX-listed enterprises has been recorded to date, according to World Bank evaluations (World Bank, 2023).

2.3.2. Infrastructural and Technological Deficiencies

A technological infrastructure is necessary for the proper functioning of capital markets in terms of trading, clearing, settling, and distributing information. The lack of such an infrastructure will lead to inefficiencies in capital market operations, high costs, and unavailability. Samuel Teklu (2022) mentions shortcomings in trading technologies, inefficiency in clearing and settling, and difficulties in managing market information as major technological problems for the Ethiopian Securities Exchange (ESX). Shortcomings in infrastructure can take many forms: traders may be unable to trade because of problems with their trading platform; delays and long processes associated with clearing and settling may increase risks; or traders may not have access to market information in a timely manner.

Technology-based solutions may provide ways around these problems. According to Meron Desta (2023), blockchain technology may increase transparency and cut down settlement time and costs by creating secure, immutable records of ownership and transactions for securities. AI systems may help monitor the market, recognize manipulative practices, and educate investors individually. Yet all these sophisticated solutions require certain minimum development of the ICT framework, including availability of internet connection, cybersecurity measures, data centers, and identification systems, which is currently uneven in Ethiopia (Tekle haimanot, 2014). Other African exchanges may offer lessons learned.

In this case, the Nigerian Exchange (NGX) was able to upgrade itself from a manual, under-regulated stock exchange to an advanced one via investing in modern trading infrastructure,

securities depositories, and online trading platforms through the reforming of the regulatory environment (NGX Group, 2020; PwC, 2023). Likewise, the Nairobi Securities Exchange adopted technology adoption, demutualization, and integration of central depository systems although such a process faced difficulties due to inefficiency (Omuchesi et al., 2014; Muchiri, 2015). The lesson learned here is that technology adoption is necessary but not sufficient for enhancing market efficiency since other investments such as in human resources and cybersecurity must also be made to complement the former.

2.3.3. Market Awareness and Investor Participation

Financial literacy and awareness are key determinants for the viability of the capital market, especially among retail investors. According to Guiso & Jappelli (2005), social learning has an important role in augmenting the informational signal value in the investment process. They indicate that the awareness which is defined as knowledge that there is a stock market as well as awareness about the basics of how to participate in the stock market plays a significant part in predicting participation. In communities where financial literacy is low, there are many households which are not even aware how the capital market works or what the advantages and disadvantages of participating in the capital market are. As stated by El Wassal (2013), the more financial literacy that exists in society, the more analysts, advisers, and portfolio managers are produced who will support the development of institutions and intermediated services in the market. The lack of financial literacy, however, reinforces informal savings systems such as iddir and iqub in Ethiopia, real estate investments, or even savings in banks.

Financial literacy levels in Ethiopia remain low compared to other countries. According to the African Development Bank (2021), more than 60 percent of Ethiopians do not have access to any financial service. However, the actual level of financial illiteracy in the country is much higher since people who have opened accounts in banks do not necessarily know the risks associated with investing in various products and how to balance the risks and returns. As found by Biazin & Waktola (2021), very few systematic initiatives aimed at educating potential investors about the market have been introduced. Consequently, many potential retail investors are unaware of basic concepts, such as diversification, liquidity, and market regulation. Low financial literacy leads not only to an insufficient number of participants in capital markets but also results in the absence of

a sufficient number of retail investors. This situation makes the market volatile and vulnerable to manipulation since liquidity is high only with a few institutions involved in trading.

2.3.4. Macroeconomic and Political Factors

Both inflation and its uncertain nature have negative impacts on capital markets through several mechanisms. To start with, high levels of inflation decrease the real gains from the nominal fixed income investment and make them less appealing to potential investors. Second, an increase in inflation usually implies higher interest rates set by the central bank and, hence, a higher discount rate for equities, which causes lower equity prices. Finally, uncertain inflation makes companies' earnings forecasts and planning more difficult and makes long-term investments unattractive. According to Tweneboah (2011), even changes in discount rates or risk-free rates caused by higher levels of inflation negatively impact equity prices. In this respect, the economy of Ethiopia faces major challenges because of continuous high inflation (IMF, 2023).

Economic growth positively impacts the capital markets through increased profitability of firms, improved investor confidence and higher saving rates available for investments (Ben Omri, Hkiri, & Ftiti, 2020; Ho & Odhiambo, 2021). This is a two-way relation since the development of capital markets, where effective, can encourage growth leading to a positive feedback cycle. Breaking out of this cycle, however, becomes difficult starting from an equilibrium of underdevelopment where the poor markets fail to draw adequate savings and investments, limiting growth. Political instability has an additional effect on equity investments since equities are characterized by the long-term nature of their value being based on the future income streams of businesses. Political instability through the likelihood of elections, civil unrest, policy changes and changes in political leadership create risks in the form of a longer commitment period for investments. Salisu and Vo (2020) have shown how, in cases of political instability, households and institutional investors invest more in short-term assets like bonds and real assets such as property, gold and commodities. According to Cepni et al. (2020), the impact of political instability on markets is felt both indirectly as lower economic growth and directly through increased risks.

Political factors in particular stand out as very important for Ethiopia. Ethiopia has seen a lot of political transition, ethnicity-based conflicts, and uncertainty regarding its policies in recent times. Though the present government has adopted certain economic reforms, such as privatizing certain firms and liberalizing its financial sector, it still seems uncertain whether these policies will last

long or whether there will be any inconsistencies in them from the investors' point of view (World Bank, 2023). Thus, the peaceful solution to the political disputes and commitment to consistent policy reform are very important for establishing investor confidence.

2.4. Overview of African Capital Markets

2.4.1. Historical Development and Current Landscape

The development of the capital markets in Africa has been influenced by the history of colonialism, independence economics, and attempts to integrate the region. In colonial times, economic activities in Africa were mainly focused on extracting and exporting raw materials, and the financial system was aimed at serving colonial needs rather than helping local capital markets grow (African Development Bank, 2005). This is why after achieving their independence, most African states did not have any developed capital markets that could accumulate their domestic capital for productive investments. The first exchange in Africa to be established dates back to 1887 and is called the Johannesburg Stock Exchange (JSE). It was founded to raise money for the mining sector of South Africa (JSE Limited, 2023). Later other exchanges emerged: in 1954 – Nairobi Securities Exchange; in 1961 – Nigerian Exchange; in 1929 – Casablanca Stock Exchange; in 1883 – Egyptian Exchange, which is the oldest exchange in Africa and one of the oldest in the world (ASEA, 2023). Currently, there are about 30 African stock exchanges that operate in 39 markets in Africa (ASEA, 2023).

However, even though there have been developments for decades in these markets, African capital markets still remain rather underdeveloped compared to other parts of the world. The market capitalization of all the exchanges of Africa is smaller than that of an individual European or American stock exchange. Also, illiquidity problems prevail here since the trading activity of many exchanges is rather insignificant compared to GDP. Nevertheless, considerable variation persists within the continent where the major share of activities takes place on the exchanges of South Africa, Egypt, Morocco, and Nigeria. This difference can be attributed to various factors affecting the level of development of capital markets in these countries (World Bank, 2022; IMF, 2023).

2.4.2. Comparative Country Experiences

Learning from peers becomes necessary when it comes to Ethiopia because there is much knowledge that can be gained from other countries' experiences regarding what works, what to

avoid, and what circumstances play a role in shaping the outcomes. A comparative analysis of selected African capital markets, which is shown in Table 1, will help identify the key lessons learned about the further development of the Ethiopian Securities Exchange after its launch. Despite some difficulties that South Africa still encounters today – such as economic inequality, inadequate financial inclusion, and vulnerability to investment cycles driven by foreign investors (SARB, 2023b; IMF, 2023) – the country's capital market remains one of the most advanced in the continent. The reason for this is that the Johannesburg Stock Exchange has successfully addressed the issue of economic isolation left over from apartheid times by opening up trade relations, embracing the Twin Peaks approach to financial regulation, and creating specific stock exchange segments for SMEs (Absa & OMFIF, 2023; SARB, 2023a; Raubenheimer, 2019).

The high level of regulations and sustainability is one of the main features of the Casablanca Stock Exchange, or the stock exchange of Morocco. Due to strict reporting practices imposed by the AMMC (Moroccan Capital Market Authority), the level of transparency is raised significantly. At the same time, the country leads the way in sustainable finance in the region as regards green bond issuance and Shariah-compliant investments (Climate Bonds Initiative, 2023; AMMC, 2022). Given that a considerable proportion of the Ethiopian population practices Islam and the country is increasingly requiring finances for environmentally-friendly projects, issuing Shariah-compliant securities or green bonds is one of its competitive advantages.

As for the Egyptian Exchange (EGX), which issues stocks and other securities for long-term financing in accordance with the provisions of the Capital Market Law No. 95 of 1992, economic instability, non-transparent operations, and controversial taxation, especially capital gains, have led to negative effects on the attitude towards investment in the stock market. Recently, management activities have included currency exchange rate regulation, investment-related legislative changes, and stakeholders' consultations in order to improve the taxation environment for investments (Mondaq, 2024; U.S. Department of State, 2024). Therefore, Ethiopia should provide stable taxation of capital markets activities.

There have been remarkable developments in the transition of the NGX from a paper-based system to a modern demutualized one that incorporates sophisticated technology. The key stakeholders behind these changes are the SEC, CSCS, and electronic trading platforms, who work hand in hand to reduce any possible risks in their activities (NGX Group, 2020). However, the current challenges

facing the NGX include liquidity crises, exchange rate fluctuations, and uncertainty in relation to digital assets (PwC, 2023; Financial Times, 2024). For the Ethiopian context, the Nigerian example provides a good learning lesson on how innovative technology can be incorporated within a decade of sustained efforts, yet not solve liquidity and macroeconomic issues.

The Nairobi Stock Exchange (NSE), the biggest stock exchange in East Africa, trades equity securities, debt securities, and derivative contracts (Muiruri & Maina, 2021). However, despite the modernization of trading by introducing automation, demutualization, and a CDS, the Nairobi Stock Exchange still faces problems with delayed introduction and efficiency in general (Omuchesi et al., 2014; Muchiri, 2015). Specifically, there is a lack of liquidity, withdrawal of foreign investments, cyber security risks, and low awareness of investors. Potential solutions to these challenges may include the development of new products, such as REITs and derivatives, providing listing incentives, and effective CRM (Muiruri & Maina, 2021; Muiruri, 2023). As for the stock exchange to compare to in the context of Ethiopia, it would be the Nairobi Stock Exchange (NSE) because of similar geography, economy, and membership of both countries in the EAC.

Table 1: Comparative Summary of Selected African Capital Markets

Country (Exchange)	**Market Size (Relative)**	**Key Strengths**	**Major Challenges Overcome**	**Persistent Challenges**	**Relevant Lessons for Ethiopia**
South Africa (JSE)	Largest in Africa	High liquidity; product diversity; international connectivity	Economic isolation (apartheid); fragmented regulation	Economic inequality; financial exclusion; sensitivity to external cycles	Adopt Twin Peaks regulatory model; develop SME listing platforms; prioritize

					international integration
Morocco (CSE)	Medium-large	Strong regulation; green/Islamic finance leadership	Weak investor confidence; low transparency	Sustaining innovation; expanding retail participation	Leverage green bonds and ESG products; develop Islamic finance; strengthen AMMC's role
Egypt (EGX)	Medium-large	High liquidity; diverse product range	Economic instability; controversial taxation	Currency volatility; transparency deficits	Implement predictable tax policies; maintain exchange rate reforms; engage stakeholders on contentious laws
Nigeria (NGX)	Largest in West Africa	Technological transformation; product innovation	Manual trading; poor regulation; weak infrastructure	Low liquidity; FX volatility; digital asset regulation	Invest systematically in trading platforms; demutualize; ensure cybersecurity
Kenya (NSE)	Largest in East Africa	Green bonds; sustainable finance; derivatives	Automation gaps; demutualization challenges	Low liquidity; foreign capital flight; cybersecurity	Develop REITs and derivatives; provide listing incentives; prioritize investor education

Source: *Compiled by the author from ASEA (2023), World Bank (2022), IMF country reports (2022-2023), and individual exchange annual reports.*

2.4.3. Synthesized Lessons from African Capital Markets for Ethiopia

The key lessons from the comparative study of the above-mentioned countries for Ethiopia's capital market development are the following:

Lesson 1: Importance of orderly reform sequencing. The example of South Africa demonstrates that sequencing is important because one has to start with the establishment of good domestic institutions before embarking on international integration. This lesson implies that Ethiopia should not rush into market liberalization.

Lesson 2: Priority to regulatory system effectiveness. Moroccan example proves that high regulatory capacity of a nation is capable of creating a favorable investment environment even for

small markets. In other words, the enforcement capacity of Ethiopia's ECMA is more important than creation of market tools.

Lesson 3: Macro stability is essential. Egypt's recurring problems with currency instability and Nigeria's problems with foreign exchange shortage have repeatedly caused problems for investors irrespective of the quality of exchange facilities. Ethiopia has to resolve its problems with foreign exchange and inflation as a necessary pre-condition for capital market take-off.

Lesson 4: Adoption of technology has to be planned. The Nigerian Stock Exchange transformation was successful since it involved technology and regulation together. However, implementation of reforms at the Nairobi Stock Exchange was delayed owing to the fact that technology had been adopted before regulation. Ethiopia has to adopt a coordinated approach to technology.

Lesson 5: Product innovation can create initial momentum. Kenya introduced green bonds while Morocco introduced products compliant with Shariah requirements. Ethiopia can capitalize on its diaspora communities and Shariah-based finance to introduce innovative products.

Lesson 6: Investor education is imperative. The persistent issues that Kenya continues to experience in regards to the awareness of retail investors after years of market operations show that Ethiopia needs to start with the development of a system of investor education prior to any market growth.

2.5. Empirical Insights on Capital Market Development

2.5.1. Market Integration and Segmentation

A lot of empirical research has been done and it suggests that a high level of financial market integration exists in developed nations in terms of the relationship between assets which have common characteristics in relation to the riskiness and thus their returns should be equivalent in both locations. However, emerging markets tend to face segmentations due to capital controls, transaction cost, information asymmetry, and poor institutional quality (Bekaert & Harvey, 1995; Stulz, 1999). In order to reduce the issue of market segmentation, it is important for governments to conduct financial reforms through which the restrictions to cross-border movements of money can be removed. This strategy may prove useful in integrating emerging economies' capital markets into global capital markets but makes them prone to contagion effects (Reinhart & Rogoff, 2009; Radelet & Sachs, 1998).

In the case of Ethiopia, a cautious strategy would be encouraged in the liberalization process. Full and fast liberalization, if done without adequate regulatory capacity, would make Ethiopia vulnerable to capital movements and contagion risks. However, if the country remains too protectionist, then it will suffer from inefficient market segmentation.

2.5.2. Capital Flows and Economic Growth

While foreign investment inflows are good for boosting economic growth, there is concern over what types of capital are flowing in. Contrary to FPI, which is usually disruptive, FDI can be said to be beneficial because it brings business management know-how along with technology. This is the reason why FDI is regarded positively since it comprises capital, technology, and management expertise needed for economic development (Prasad et al., 2007; Alfaro et al., 2008).

Thus, with regard to Ethiopia, the ESX must concentrate on FDI and FPI, meaning that it must attract foreign institutions to invest in the securities that will be traded through its exchange or buy stocks of Ethiopian firms. The policymaker must also realize that FPI is, by nature, risky and can give rise to financial bubbles and cause financial crises due to foreign pressure on the national currency (Prasad et al., 2007; Alfaro et al., 2008).

2.5.3. Financial Crises and Capital Market Behavior

Financial crises such as the one that took place in East Asia in 1997, the Russia financial crisis of 1998, global financial crisis of 2008/2009, and European debt crisis of 2010-2012 have been great sources of information about how capital markets behave in these situations. Among the common problems that may arise in such situations include sudden stop, contagion, and excess leverage. The sudden stop implies the reversal of capital flows whereas contagion denotes financial crises spreading to other financial markets. Excess leverage implies that the use of leverage worsened the situation (IMF, 2017; Acharya & Richardson, 2009; Reinhart & Rogoff, 2009). In such instances, investor sentiment will be negative, asset prices will fall, and liquidity will be hard to come by.

The reforms which have been made after the occurrence of the financial crisis have pointed out the importance of having more capital and liquidity ratios and also the significance of risk management within financial institutions (BIS, 2022; Borio, 2003). In this context, the aim of the regulatory reforms can be seen as taking necessary actions to ensure that there will be no crisis in

the future by taking measures such as capitalizing adequately with respect to risk exposure. Given the above-discussed context, it would appear that the country can take advantage of setting up its capital market according to modern standards as it is being done after a financial crisis. However, care must be taken to ensure that these reforms do not impose undue burdens on the participants who refrain from participating in the market at the Ethiopian Securities Exchange (IMF, 2017; World Bank, 2023).

Moreover, such events highlight the significance of implementing prudent policy measures on a macro scale and instilling investor confidence. Capital outflows and stock index drops in emerging markets happen during times when there is an element of risk either on a macroeconomic or political level, making it crucial for a nation to have effective communication channels, a regulatory framework that works effectively, and proper institutions to cope with any shock without undermining the integrity of the financial sector (Acharya & Richardson, 2009; IMF, 2017). The experience of such nations should be taken into account while formulating ECMA's regulatory framework for the country.

2.5.4. Empirical Studies on Capital Markets in Frontier African Economies

There have been many empirical studies regarding the development of capital markets in frontier African countries, providing both methodological and contextual information to aid the case of Ethiopia.

The study by Yartey & Adjasi (2007) is one of the most thorough studies about the development of stock markets in Sub-Saharan Africa. They used panel data analysis from 14 countries in Africa between 1990 and 2004, identifying the significance of macroeconomic stability, institutional factors, and financial sector development in predicting stock market capitalization.

The study by El Wassal (2013) explored the effects of legal and regulatory framework on stock market development in 44 emerging and frontier economies, including some African nations. Through the use of multiple regression analysis, El Wassal discovered that regulations and accounting standard were more influential on market development than market size or per capita income. This information can be used to support Ethiopia's focus on the Capital Market Proclamation No. 1248/2021.

Some of the early and fundamental empirical researches done on emerging market integration include Bekaert and Harvey (1995, 2003). These researchers showed that partial market liberalization is more favorable for reducing the cost of capital and lowering contagion risks compared to complete liberalization.

An empirical review of financial systems in Africa was done by Allen et al. (2011). Although bank-based systems dominate, they observed that countries having operational stock exchanges, such as South Africa, Nigeria, and Kenya, have more private credit accessibility and affordable loans for big companies. The empirical study provides a strong basis for the Financial Development Theory in the African situation.

In a time series empirical analysis of the linkage between financial development and economic growth in selected African countries, Ho and Odhiambo (2021) found out the existence of bidirectional causation: financial development leads to growth, but growth also results in high demands for financial development. Therefore, it implies that Ethiopia cannot afford to wait until its economy is well developed to develop its capital market.

Ethiopian Domestic Empirical Studies: In the domestic front, an empirical study carried out by Adonay (2021) in Ethiopia using the qualitative research method identified weaknesses in enforcement ability and lack of clarity in the policies as major barriers. Another empirical study done by Esayas Ephrem (2022) through surveys revealed that inefficient clearing and settling systems hinder participation due to high costs involved in the process. Biazin and Waktola (2021) carried out an empirical investigation in Addis Ababa regarding the level of financial literacy among citizens and found out that more than 70 percent lacked information on capital markets.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter outlines the methodology that has been adopted for this study. The methodology includes aspects such as research design, research approach, the target population, the sample size, the sampling technique, the source of data, techniques of collecting data, validity and

trustworthiness, data analysis, and ethical issues. This chapter aims to present how the research has been carried out.

3.2 Research Philosophy

Research philosophy is concerned with the system of beliefs and assumptions that governed the process of research (Creswell & Creswell, 2018). The three principal research philosophies were positivism, interpretivism, and pragmatism. In positivist philosophy, there was one objective reality that could be quantified, while interpretivism believed that reality was social construction and required qualitative approach to understand (Saunders et al., 2019). Since this study used a mixed-methods approach wherein qualitative methods were dominant in the form of surveys, interviews, and focus group discussion, pragmatism was chosen as the underlying research philosophy. Pragmatism focused more on research questions than philosophical questions. Moreover, this research philosophy allowed the researcher to adopt a combination of quantitative and qualitative data in one study (Creswell & Plano Clark, 2018). As per the arguments made by Saunders et al. (2019), pragmatism involved asking "what works" to provide an answer to research questions, rather than being restricted to just one research philosophy. This position suited this research very well since what was needed here was not the debate on the reality but the formulation of practical recommendations regarding the functioning of capital market in Ethiopia.

3.3 Research Approach

Two types of research approaches were employed in the study – quantitative and qualitative. The use of the quantitative research approach helped to collect structured data from survey participants, while the qualitative research approach helped in the collection of data from key informant interviews and discussions in focus groups that helped better comprehend the problems facing the growth of the capital market.

Use of the two research approaches was dictated by the nature of the problem being investigated. Since the capital market in Ethiopia is very new, use of one approach to analyze the problems would limit the study. Use of two research approaches provided an opportunity to triangulate data gathered during the process, hence increasing its credibility. As Bryman (2016) observes, combining quantitative and qualitative research approaches helps in improving the interpretation of results and minimizes problems inherent in adopting only one approach.

3.4 Research Design

The study used an exploratory and descriptive research design. An exploratory descriptive research design was deemed appropriate for the study since the study focused on exploring the challenges and emerging opportunities for the capital market in Ethiopia after launch, as well as describing the existing scenario in relation to perceptions. The exploratory descriptive research design is suitable for research problems that are new or for which there is little information.

Furthermore, a mixed-methods research design, with a focus on qualitative research methods, was employed. The reason why a mixed-methods research design was used in this case is that the study was characterized by a need for quantitative and qualitative analysis. It is through the quantitative research approach that the extent of the challenges and opportunities experienced in the capital market will be measured, while the qualitative research design provided in-depth insight into the situation in question. As Creswell and Plano Clark (2018) put it, mixed methods are appropriate for research where breadth and depth of analysis are sought in the same study.

3.5. Target Population, Sample Size, and Sampling Procedure

3.5.1. Target Population

The target population of the study comprised of those individuals who were either directly or indirectly connected with the evolving capital market in Ethiopia. The target population comprised of people from various institutions such as Ethiopian Capital Market Authority, Ethiopian Securities Exchange, financial institutions, market intermediaries, institutional investors, academic experts, and consulting firms. These entities were chosen due to the fact that they possess the required information about the status of the capital market after launch.

Addis Ababa served as the primary location of the study due to the reason that the majority of the institutions mentioned above are located there. Kothari (2004) believes that the process of selecting a clearly identified target population is crucial for a study.

3.5.2. Sample Size Determination

To determine the required sample size for the quantitative component of the study, the Yamane (1967) formula for finite populations was employed. The formula is expressed as:

$$N = \frac{N}{(1 + N(e)^2)}$$

Where;

- n = sample size,
- N = total population size
- e = level of precision or margin of error

In this study, the total population was N=725N=725, and the margin of error was set at e=0.05e=0.05 at a 95% confidence level. Substituting these values into the formula gives:

$$N = \frac{725}{(1 + 725(0.05)^2)}$$

$$N = \frac{725}{(2.8125)}$$

$$\boldsymbol{N} \approx 258$$

Therefore, the required sample size for the quantitative part of the study was 258 respondents. However, 233 questionnaires were returned and found to be usable for analysis. The final analysis was therefore based on 233 valid responses.

3.5.3. Sampling Techniques

Mixed sampling technique was employed in this study for the purpose of matching the qualitative dominant methodology and the practicalities associated with respondent access in the nascent capital markets of Ethiopia. Purposive non-probability sampling was employed to identify key informant interviewees who had firsthand experiences of the Ethiopian Securities Exchange (ESX). Such key informants included senior members of the Ethiopian Capital Market Authority, management officials in ESX, experienced brokers, managers of institutional investors, capital market consultants, and academics. Purposive sampling was an ideal technique to employ in this regard due to its ability to allow for the selection of information-rich individuals that were relevant to the research.

Snowball sampling served as another technique that allowed other potential participants who may not have been readily accessible to be identified and interviewed. The use of snowball sampling

was necessary due to its ability to help in identifying underrepresented stakeholders of the capital markets in the country. Focus group discussions on the other hand were held among participants who shared common professional interests like brokers, institutional investors, and academics.

The qualitative part focused on conducting roughly 25 to 35 key informant interviews as well as 3 to 4 focus group discussions, where each discussion would involve 4 to 6 participants. The exact number of respondents for each method was established based on reaching thematic saturation, whereby the data collection process proceeded until no new themes or patterns were identified. This is the standard procedure followed in qualitative research, in which the primary goal is to achieve deeper insights regardless of the number of people surveyed.

As for the quantitative survey part, the pragmatic, sample-focused approach was taken. If a sampling frame had been fully accessible, as would have been the case for registers of licensed intermediaries, then a stratified simple random sampling method could be implemented. Unfortunately, due to practical limitations involved in conducting a probability sampling process, purposive and convenience sampling were employed as well in order to recruit certain predefined quotas from each of the key stakeholder categories.

Recruitment processes involved creating databases of contact details of organizations drawn from ECMA and ESX databases, professional bodies, university faculties, and industry directories. Selection of key informant interviewees involved criteria of relevance of role, experience, and information richness. As for survey respondents, recruitment involved monitoring of inclusion criteria, reasons for selection, and non-response, to ensure transparency, methodological rigour, and adherence to the qualitative approach to sampling.

3.5.4. Sampling Proportions

A total of 258 individuals were assigned to the sample sizes based on their ratios among the different groups of stakeholders, as illustrated in Table 2 below. The total sample size is derived by multiplying the total population of each stakeholder group with their corresponding ratios as depicted in Table 2 below.

Table 2: Sampling Proportions (n = 258)

No	Stakeholder Category	Total Population	Proportion	Sample Size

1	Regulators, ESX, and intermediaries	385	0.531	137
2	Institutional investors (banks, insurance, pension funds)	120	0.166	43
3	Academics and policy researchers	120	0.166	43
4	Consulting and audit firms (capital-market service providers)	100	0.137	35
	Total	**725**	**1.000**	**258**

Source: Developed by researcher (2025).

For the qualitative component: Approximately 20-25 key informants were selected purposively, distributed across the four stakeholder categories based on information richness rather than proportional representation.

3.6Sources of Data

Both primary and secondary sources of data were used in the research process. Data collection involved using questionnaires, key informants' interview and focus group discussion methods. The questionnaire method was used for collecting quantitative data while the two latter methods were used for collecting qualitative data.

The secondary sources of data included books, journal articles, policies, legal frameworks, and reports among others. This method was used to supplement the literature review as well as for contextualizing the findings of the study. According to Sekaran & Bougie (2016), a combination of primary and secondary data strengthens a research process.

3.7. Data Collection Procedures

Questionnaires were distributed and retrieved in hard copy form using physical visits to the work places of the respondents within Addis Ababa, and it took about 15 to 20 minutes to fill each questionnaire. Telephone interviews of fourteen key informants were held and in the process handwritten notes were taken by the researcher right after each interview; each interview session took about 45 to 60 minutes to finish. Four focus group discussions were conducted face-to-face, involving 4 to 6 people in each group according to their stakeholders. Notes were taken by the researcher with the help of two research assistants, taking about 60 to 90 minutes each discussion. To evaluate the comprehensiveness and efficacy of all the instruments used, a pilot study with five

professionals was undertaken, and the results were incorporated in revising the survey and guidelines before conducting the actual study. Document analysis was undertaken to support the qualitative data and included the use of information from the World Bank, IMF, AfDB, ASEA, ECMA, and ESX. All data gathered were safely stored in locked file cabinets; consent was given verbally for telephone interviews and written for FGDs; anonymity was ensured through coded responses.

3.8 Validity and Reliability

3.8.1 Validity

Validity was defined as the degree to which an instrument measured what it purported to measure (Yin, 2018). In the case of the quantitative section of the current study, the instrument was constructed taking into consideration the aims of the research as well as a comprehensive analysis of literature relevant to the post-launch issues and possibilities of the nascent capital markets of Ethiopia. Since no standardized instrument existed for measuring the particular case of the development of the capital markets of Ethiopia, a questionnaire was developed with questions designed with respect to the corresponding research aim. The content validity was established since every item was linked to one of the study aims, and the research instrument was validated with the research advisor. Construct validity was established through the use of Principal Component Analysis, which generated four components with eigenvalues of more than 1.0, accounting for 77.254% of variance with communalities between 0.526 and 0.918, exceeding the acceptable limit of 0.50 recommended by Hair et al. (2019), thus providing evidence of good construct validity for the questionnaire.

3.8.2 Reliability

Reliability meant the dependability of the research tool in giving out consistent and reliable findings. Internal consistency reliability was determined through calculating Cronbach's alpha coefficient for each construct. The results are presented in Table 3 below.

Table 3: Cronbach's Alpha Reliability Coefficients

Variable	Number of Items	Cronbach's Alpha
Regulatory Environment and Governance	5	0.736
Market Operations and Infrastructure	4	0.804

Market Participants and Capacity	5	0.762
Macroeconomic and External Environment	4	0.723
Prospects and Opportunities	5	0.755
Overall	**23**	**0.930**

Source: Survey data (2026)

All construct values exceeded the minimum acceptable threshold of 0.70 as indicated by Nunnally and Bernstein (1994). The overall Cronbach's alpha coefficient for the entire 23-item questionnaire was 0.930, indicating excellent internal consistency reliability.

3.8.3 Trustworthiness

The trustworthiness of the qualitative part of this research was assured using the four standards set forth by Lincoln and Guba (1985), namely, credibility, transferability, dependability, and confirmability. Credibility was attained using triangulation by cross-referencing data collected from questionnaires, interviews, and focus groups to validate major themes and reduce any bias on the part of the researchers. Transferability was enhanced by providing a thick description of the research setting, such as the unique features of the Ethiopian capital market and the background of the respondents. The standard of dependability was assured by documenting an audit trail of all research-related decisions regarding sampling, data gathering, and analysis. Confirmability was secured by keeping a continuous record of reflexive memos and engaging in investigator triangulation through consultation with the advisor.

3.9 Method of Analysis

Following data collection, the quantitative data were checked for completeness, coded, and entered into IBM SPSS Statistics for analysis. The qualitative data from interviews and focus group discussions were transcribed verbatim, organized using NVivo software, and anonymized by assigning participant codes. Both datasets were cleaned and prepared separately before integration.

For quantitative data, descriptive statistics including frequency, percentage, mean, and standard deviation were employed. Descriptive statistics were chosen because the research focused primarily on describing stakeholder perceptions rather than establishing causal relationships. For qualitative data, thematic analysis following the six phases proposed by Braun and Clarke (2006) was conducted: familiarization with the data, generating initial codes, searching for themes, reviewing themes, defining and naming themes, and producing the report. Responses with similar

meanings were categorized into themes based on common ideas presented in the data. Thematic analysis was used to understand the meanings behind responses and the reasons for quantitative findings. Qualitative and quantitative findings were integrated using a convergent parallel approach to obtain a comprehensive picture of the research problem.

Given the qualitatively-dominant exploratory nature of this study, no inferential statistical models (e.g., regression, structural equation modeling) were specified or tested. The study aimed to describe and interpret post-launch challenges and prospects of Ethiopia's capital market as perceived by stakeholders, not to predict or establish cause-and-effect relationships. Therefore, model specification was confined to the conceptual framework outlined in Chapter 2, which guided the thematic analysis and the interpretation of descriptive statistics.

3.10 Ethical Consideration

Everything concerning the research was done with regard to ethics as per the APA guide on doing ethical research based on the 7th edition of APA as well as the guide on conducting ethical research in an institution (American Psychological Association [APA], 2020; Creswell & Poth, 2018). Participants were provided with an information sheet that elaborated on what the research was all about and explained its potential advantages and drawbacks. In addition, informed consent was obtained from all participants: verbally for telephone interview participants and in writing for focus group discussion participants. All participants were assured of privacy and the freedom to withdraw from the study at any time without penalty. The tools utilized in data collection were not subjected to any form of misuse and could only be accessed by the researcher and the supervisor. Names of participants were not disclosed during data analysis.

CHAPTER FOUR

PRESENTATION, ANALYSIS, AND INTERPRETATION OF FINDINGS

4.1 Introduction

In this chapter, the results of the study on the challenges and opportunities that arise in the post-launch phase in the capital market of Ethiopia, particularly the Ethiopian Securities Exchange (ESX), have been reported. These results have been generated using an empirical database collected through a mixed-method approach, involving 233 questionnaire survey forms, 14 Key Informant Interviews (KIIs), and four Focus Group Discussions (FGDs). This chapter is arranged thematically as is standard in mixed-method studies (Creswell & Clark, 2017).

This analysis aimed at answering the six research questions outlined by the study related to: (1) regulatory challenges that arise after the introduction of new regulations on the capital market; (2) how technology and infrastructure affect operational efficiency and accessibility; (3) how financial illiteracy and lack of knowledge among investors affects market performance; (4) the implications

of macroeconomic instability on the capital market of Ethiopia; (5) the effect of political considerations in capital market development; and (6) future possibilities for savings mobilization, SME financing, and international integration.

The analysis adopts an organized methodology whereby the quantifiable results are first stated per theme, followed by qualitative information, and finally integration and interpretation of the results. This ensures that there is an extensive examination of all the research questions by considering more than one source of information. The interpretation of the results is based on the theories explained in Chapter Two, namely EMH, CAPM, IRP, Institutional theory, and Financial Development Theory.

The combination of the quantitative descriptive statistics of the survey was used together with the qualitative themes that emerged through thematic analysis of interview and discussion transcripts.

4.2 Demographic Profile of Survey Respondents

A total of 258 questionnaire forms were sent out to the target population, and 233 responses were gathered, which amounted to 90.3% of the total number of respondents. The demographic profile of the 233 survey respondents is shown in Table 4 below.

Table 4: Demographic Characteristics of Survey Respondents (N = 233)

Variable	Category	Frequency	Percent
Gender	Male	137	58.8
	Female	96	41.2
Education Level	Bachelor's degree	86	36.9
	Master's degree or above	99	42.5
	Diploma	42	18.0
	PhD	6	2.6
Position	Junior level	120	51.5
	Senior level	101	43.3
	Managerial/Head/Director	12	5.2
Experience	4–8 years	112	48.1
	9–12 years	80	34.3
	More than 13 years	41	17.6

Source: Own Survey,2026

This gender ratio of 58.8 percent male and 41.2 percent female is evidence of adequate participation of professional women in the Ethiopian emerging financial sector. Concerning the level of education of the respondents, 79.4 percent had master's degree and above, and thus it shows that a highly educated sample was used for the research, which was quite suitable for the study since the latter required knowledge on how capital markets operate. The high level of education is important because it means that the sample comprised people who were knowledgeable enough to give their informed perspectives on capital market operations. The drawback of the study was that the views of less educated individuals were not adequately represented.

Regarding the period of professional experience, 82.4% of the respondents had worked for four years and above in jobs relating to either finance or economics, with 17.6% having more than 13 years of professional experience. A larger portion of the respondents (51.5%) occupied junior positions, 43.3% senior positions, and 5.2% managerial/director-level positions. This indicated that a relatively representative group of professionals who were experienced enough in the ESX environment to provide feedback was obtained. This ensured the credibility of the data obtained quantitatively (Saunders, Lewis, & Thornhill, 2019). This also ensures balanced perspectives are provided by the respondents, with the junior staff giving operational perspectives and the senior and managerial staff providing strategic and policy perspectives.

4.3 Regulatory Environment and Governance

Question one provided the problems that emerged due to the emergence of regulation in the capital markets. It was important to generate a decision rule for interpreting mean scores based on Best & Kahn (2016). This was because the range of the Likert Scale, which is five (5 - 1 = 4), was divided by five to give an interval of 0.80. Therefore, mean scores ranging from 1.00 to 1.80 were categorized as Very Low, those ranging from 1.81 to 2.60 were Low, those ranging from 2.61 to 3.40 were Moderate, those ranging from 3.41 to 4.20 were High, and those ranging from 4.21 to 5.00 were Very High.

Table 5: Regulatory Environment and Governance (N = 233)

Statement	Mean	Std. Deviation

The current regulatory framework under the Ethiopian Capital Market Authority (ECMA) is clear and effective for market operations.	3.65	0.874
ECMA's enforcement capacity is sufficient to ensure market integrity and investor protection.	3.80	0.958
Existing accounting, auditing, and financial reporting standards in Ethiopia are adequate for listed companies on the ESX.	3.63	0.799
Current regulations sufficiently protect the rights of minority shareholders in listed companies.	3.00	1.209
There is sufficient regulatory guidance for institutional investors (e.g., pension funds) wishing to participate in the ESX.	3.59	1.010

Note: Scale: 1 = Strongly Disagree, 2 = Disagree, 3 = Neutral, 4 = Agree, 5 = Strongly Agree

Source: Survey data (2026)

4.3.1 Regulatory Clarity and Enforcement Capacity

Based on the decision rule stated in section 4.3 (Best & Kahn, 2016), in which values between 3.41 to 4.20 mean high, it is observed that there was high agreement among the respondents in terms of clarity and effectiveness of the regulatory framework employed by ECMA (M = 3.65, SD = 0.874). Similarly, high agreement exists concerning the enforcement capabilities of ECMA (M = 3.80, SD = 0.958), thus suggesting high agreement in terms of high enforcement capacities of ECMA. The accounting and financial reporting standards obtained high mean score too (M = 3.63, SD = 0.799). The relatively low standard deviations for these items indicate that respondents were generally consistent in their views, suggesting a degree of consensus on these regulatory aspects.

Notwithstanding these moderate mean ratings, the qualitative findings revealed deeper underlying issues. In particular, a senior regulator stated:

"...we have the legal mandate, but converting that into meaningful supervision requires numbers and skills we currently lack." (KII-REG-01, Senior Legal Officer, ECMA)

The finding corroborates the principles of institutional theory, according to which formal systems like laws and regulation are important; however, they cannot function without the ability to enforce them (North, 1990). The quotation makes an important point about the difference between having the right by law and having the operational ability to enforce that right. Such disparity between the regulatory ability and enforcement ability is a common problem in frontier markets. Lack of

enforcement ability despite having the regulatory ability is one of the classical problems in frontier African markets (Yartey & Adjasi, 2007).

The same regulatory body also pointed out that the secondary legislation was yet to be finalized:

"Secondary legislation on foreign portfolio investment is still at the draft stage after one year. This leads to uncertainty for international investors." (KII-REG-01, Senior Legal Officer, ECMA)

The delayed process of formulating secondary legislation is important since it results in the failure to operationalize the primary law framework. Without the implementation regulations, there is uncertainty in the law, which affects investor confidence and development of the market. This is what was indicated through research findings by El Wassal (2013), whereby he discovered that the regulatory framework was very important in defining the stock market and that ambiguous regulation leads to lack of investments regardless of the quality of primary legislation. The discovery is in line with Institutional Theory, where the enforcement of laws is as important as the formulation of the laws themselves.

4.3.2 Minority Shareholder Protection

Based on the decision rule defined in section 4.3 (Best & Kahn, 2016), mean values ranging from 2.61 to 3.40 were considered as Moderate, implying that minority shareholder protection had a mean value of 3.00 (SD = 1.209). The mean value of 3.00 is the lowest among all regulatory indicators; hence, the respondents did not strongly agree or disagree that there is protection for the minority shareholders. The highest value for standard deviation, being 1.209, suggests substantial disagreements among the respondents. This high standard deviation indicates considerable divergence in stakeholder perceptions, with some viewing minority protection as adequate while others perceive significant deficiencies. The large standard deviation shows that while some respondents felt that the minority shareholder protection is sufficient, others felt it is an important regulatory deficiency. The wide dispersion of responses suggests that this is a contested issue with genuine differences in stakeholder experience and expectation.

As it was expected, the qualitative information supported this hypothesis. One regulator stated:

"The weakest part is shareholder protection. Our Commercial Code is from 1960." (KII-REG-02, Director of Market Supervision, ECMA)

Such statement drew attention to an institutional problem which, according to IOSCO (2017), also had been recognized by that time: investor protection mechanisms such as shareholder rights, enforcement mechanisms, and corporate governance systems were the prerequisites for any financial market development. In fact, the Commercial Code of 1960 included very few provisions on protection of minority shareholders which became typical for further legislation (World Bank, 2022). Mentioning the Commercial Code of 1960 has a particular significance since it clearly illustrates how out-of-date legal institutions limit the development of modern financial markets. The Commercial Code was adopted more than six decades ago before the creation of the ESX.

The same participant commented further:

"There's a lot of information asymmetry. Individual investors know nothing." (KII-REG-02, Director of Market Supervision, ECMA)

The existence of information asymmetry in material terms in which the issuers possessed a significantly greater amount of information compared to the investors negatively impacted market efficiency and confidence (Fama, 1970). In an efficient market, the information becomes part of the price. When there was no dissemination or deliberate delay of information, there was informed investing and adverse selection on the part of the investors (Bekaert & Harvey, 1995). From the EMH view, the presence of information asymmetry fails to meet the conditions necessary for semi-strong market efficiency in that the information could not be fully reflected in the price because it was not disseminated.

Shareholder protection from qualitative research shows that there is a gap between law and implementation. Although the law is established through Proclamation No. 1248/2021, the absence of enforcement mechanisms and the old Commercial Law of 1960 indicate governance gaps which affect the protection of investors and market integrity. The study is consistent with Yartey & Adjasi (2007) who stated that legal and regulatory frameworks are a key constraint to stock market development in Sub-Saharan Africa.

4.3.3 Cross-Regulatory Coordination

Coordination issues between regulatory authorities were highlighted as one of the key barriers by institutional investors. A pension fund investment manager said:

"Our mandate says that we can invest up to 5% in equities. However, implementing regulations have not been updated." (KII-PEN-01, Head of Investments, Pension Fund)

On another occasion, an institutional investor said:

"This issue has been raised to both ECMA and NBE for eighteen months. It still remains pending." (KII-INV-02, Investment Manager, Pension Fund)

The delay of eighteen months to solve this problem is especially alarming because it shows an organizational problem of coordinating efforts of the regulators. In the case at hand, the NBE and the ECMA both regulate institutional investors; however, there is no coordination process in place to harmonize their regulations. This kind of regulatory overlap makes it impossible for institutional investors, which are officially licensed, to enter the market. The following were some signs of poor coordination of regulatory activities of the ECMA and the NBE, which regulate the capital market and banking institutions and pension funds, respectively.

Such instances are common even outside Ethiopia. Recent findings in other frontier and emerging economies reveal that fragmentation of regulatory responsibility usually results in delayed execution of investment mandates and institutional under-participation. In a 2024 report on capital markets development in developing countries, the World Bank highlighted unclear separation of responsibilities between the central bank and the securities regulator as one of the major factors limiting pension fund and insurance company participation in early-stage stock exchanges (World Bank, 2024). Likewise, the African Securities Exchanges Association (2023) noted the impact of cross-regulation coordination lags on limiting liquidity in at least six African frontier stock markets such as Uganda, Tanzania, and Ghana.

Regarding Ethiopia, for example, the implementation of the Capital Market Proclamation (Proclamation No. 1248/2021), which was passed in 2021, has enabled ECMA to be a key regulator, but it is noted that there are still some implementing regulations yet to be adopted, such as institutional investor rules. It has been stated by an IMF assessment done in 2025 that the failure by the regulators to harmonize their rule making process has left the pension schemes and insurance institutions authorized by law to operate but lacking implementation rules (International Monetary Fund, 2025). This has led to the situation described in section 4.5.2 whereby the institutional investors are investing less than one percent of their assets in the ESX listed securities.

This problem of cross-regulatory coordination can be explained by using the concept of Institutional Theory. Although the existence of formal institutions like laws and regulation was aimed at institutional investment, the lack of coordination among regulatory agencies leads to the creation of an institutional vacuum that hinders the proper working of the market.

Peer country practices provide some possible ways to address this issue. For example, the Capital Market Authority and the National Bank of Rwanda formed a joint technical committee in Rwanda in 2022. As a result, the approval process by different authorities was decreased from fourteen months to four months (Rwandan Capital Market Authority, 2024). The Capital Markets Authority and Central Bank of Kenya signed a memorandum of understanding in 2023, thereby eliminating the overlap in mandates for investments in pension funds. As a result, there was an increase of twelve percent in the number of institutional investors within the first year (Capital Markets Authority Kenya, 2024). Thus, it is necessary for Ethiopia to adopt similar measures.

4.3.4 Policy Consistency and Foreign Investor Confidence

As an emerging markets portfolio manager, one expressed fears regarding policy consistency and predictability:

"Five-year policy consistency is on our checklist. We haven't seen that in Ethiopia." (KII-FOR-01, Portfolio Manager, Emerging Markets Fund)

The five-year requirement for policy consistency, which is stated by the portfolio manager, relates to the long-term nature of the investment and also the need for a stable framework of policies. Portfolio managers assessing the investment potential in frontier markets need evidence of policy consistency to enable their risk assessment and investment decisions. The failure of Ethiopia to demonstrate such consistency in policy within the last five years is a major hurdle in attracting foreign portfolio investments.

This sentiment corresponds with the recently provided evaluations. According to the Ethiopia Investment Climate Statement for 2025 (U.S. Department of State, 2025), although "the Government has floated the birr, opened new industries and launched the Security Exchange," the fact that "instability, poor protection of property rights, and state predominance" continue to exist in the country has "undermined investor confidence." Meanwhile, according to the IMF Article IV consultation of 2025 (International Monetary Fund, 2025), while "there has been significant

progress toward implementation of fundamental macroeconomic reforms," the need to continue efforts at a high level of reform is evident.

Given Interest Rate Parity (IRP) Theory (Keynes, 1923; Hodrick, 1987), the above perspectives highlight the nature of reality in frontier markets. Empirical studies have proven that deviations from covered interest parity are greater and more erratic in emerging markets, and they also exhibit an opposing trend in risk-off periods globally (Du & Schreger, 2024). Considering segmented FX markets like those in Ethiopia, where there is no forward currency market, onshore CIP deviations are mostly oblivious to global dynamics, exposing international investors to exchange rate risk since there is no hedging mechanism available. Where there is inconsistency with the policies, investors are forced to earn risk premiums or simply wait out on their decisions (Froot & Thaler, 1990).

There is no forwards market for the currency because of which the foreign investors cannot hedge themselves against the currency risk; they have to incur the risk of fluctuating currency prices. The combination of both such risks makes the foreign institutional investors reluctant to invest in ESX through portfolios.

4.3.5 Synthesis of Regulatory Challenges

The identification of regulatory and institutional challenges shows an intriguing situation where there are legal regulations but there are also weaknesses related to the implementation of such regulations. The quantitative results indicate a relatively satisfactory level of regulatory clarity and regulatory capacity, but the qualitative results demonstrate that there are many difficulties that include the lack of manpower, obsolete legal regulations, and poor coordination among the regulatory bodies.

In theoretical terms, the regulatory challenges can be analyzed within the Institutional Theory (North, 1990). According to this theory, there should be a clear differentiation between the formal institutions (legislation and regulation) and the informal institutions (enforcement and coordination). In the case of the Ethiopian capital market, there are formal institutions but there is no enforcement and coordination mechanisms to ensure the effectiveness of these institutions.

The issues relating to regulations revealed that although Ethiopia had developed a legal framework (Proclamation No. 1248/2021 on the Capital Market), much needed to be done as far as

implementation of the laws was concerned. The identified gaps included inadequate enforcement, missing secondary legislations, protection of shareholders, and coordination among different regulatory bodies. These observations corresponded to those made by Adonay (2021) in terms of regulatory and policy ambiguities.

In addition, the study findings support the IOSCO (2017) principles that stress that there needs to be not only proper legal framework but also proper enforcement capability, investor protection, and proper regulatory coordination in order to have effective securities regulations. At present, the Ethiopian regulatory regime meets some but not all of these criteria.

4.4 Market Operations and Infrastructure

The second research question sought to establish the effect of technology and infrastructure on efficiency and access to the market. Using the same criteria set out by Best and Kahn (2016) in section 4.3 (that is, scores between 3.41 and 4.20 as high, and those between 2.61 and 3.40 as moderate), descriptive analysis results for market operation and infrastructure appear below.

Table 6: Market Operations and Infrastructure (N = 233)

Statement	Mean	Std. Deviation
The ESX's trading platform and technology infrastructure are efficient and reliable.	3.79	1.009
Clearing and settlement processes for ESX transactions are timely and dependable.	3.33	1.144
Market liquidity (the ability to easily buy/sell securities) on the ESX is currently adequate.	3.70	0.887
Access to reliable market information and data about ESX activities is readily available to investors.	3.69	0.904

Note: Scale: 1 = Strongly Disagree, 2 = Disagree, 3 = Neutral, 4 = Agree, 5 = Strongly Agree

Source: Survey data (2026)

4.4.1 Trading Platform Reliability

Based on the decision rule set forth in section 4.3 (Best & Kahn, 2016), which classifies mean scores between 3.41 to 4.20 as High, ESX Trading Systems and Technology Platforms have achieved high scores based on the mean scores (M = 3.79, SD = 1.009). The standard deviation of

1.009 indicates moderate agreement among respondents, suggesting that while most view the platform positively, there is some variation in experience. However, the qualitative feedback provided has pointed out some issues regarding reliability.

A broker said:

"In the past year, we have had three trading pauses as a result of technical problems." (KII-BRK-01, General Manager, Brokerage Firm)

This observation was confirmed by ESX management:

"In the past year, we have had three trading pauses as a result of technical problems." (KII-ESX-01, Senior Manager, Operations, ESX)

All three of the unanticipated trading halts referred to by both the broker and ESX management are a major problem. Every trading halt causes interference in the working of the market, reduces investor confidence, and imposes a cost. Given the early nature of the market and its lack of confidence, these halts are likely to have even greater negative impacts.

In the case of developing countries, such unexpected trading disruptions have a greater effect on investor confidence as there are many other alternatives for investors to invest in, which include government bonds, real estate, and even informal methods of saving money (Esayas Ephrem, 2022).

The gap between the high mean score and the actual problems with the operations of the exchange becomes much more noticeable when the newly developed infrastructure is taken into account. Thus, in March 2026, the ESX introduced its first mobile and online trading platform "Neway" aimed at attracting additional retail investors (Ethiopian Securities Exchange, 2026). As a result, by May 2026, over 19,400 users registered at the platform, and the total number of ESX investors exceeded 650 (Ethiopian Securities Exchange, 2026). However, according to the user reviews, some shortcomings are still to be worked out. These include the lack of tutorials and other explanations provided by Neway. The gap between high registration numbers (19,400) and actual investors (650) suggests a significant conversion challenge, where potential investors register but do not actively participate. This disconnect may be partially attributable to the usability issues identified. Therefore, despite the great technological advancements in the capital market of Ethiopia, the infrastructure and usability of platforms are still to be improved. It should be done to

provide smooth and secure operations and create an ecosystem including custodians, research analysts, and investment bankers.

Reliability of the trading platform is crucial for efficient markets according to the EMH school of thought. Technological glitches hinder price discovery, create information asymmetry, and decrease market liquidity. The fact that the ESX has been experiencing three trading halts has caused efficiency losses for the market.

4.4.2 Clearing and Settlement Deficiencies

Using the criteria set out in 4.3 of the decision rule (Best & Kahn, 2016), in which a score of 2.61 to 3.40 was viewed as a Moderately, the lowest mean score of all infrastructure variables (M = 3.33, SD = 1.144) was assigned to clearing and settlement, which was a moderate score. It indicated that views about the efficiency and reliability of this process were at least neutral. The relatively high standard deviation of 1.144 suggests considerable disagreement among respondents about the adequacy of clearing and settlement processes. This information was important since the efficiency of trade settlement affected counterpart risk and the velocity of capital (Committee on Payments and Market Infrastructures & IOSCO, 2012).

Qualitative evidence suggested an underdevelopment of custody structure:

"Development is still lacking. Where are the investment banks? The research analysts? The custodians?" (KII-CON-01, Senior Partner, Consulting Firm)

A focus group session among consultants further elucidated this point:

"A lack of custody structure classic 'chicken and egg' problem." (FGD-04, Consultant Focus Group)

The “chicken-and-egg” dilemma in the consultant focus group discussion highlights an important coordination dilemma: it is not possible for the custody infrastructure to develop unless there is enough trade volume, while it is also impossible for the trade volume to increase unless the custody infrastructure is secured.

The problem of "chicken and egg," where the lack of enough trading volume prevented custodians from investing, but the presence of custody infrastructure helped increase volumes of trade, was a case of classical coordination failure in emerging markets (Allen, Otchere, & Senbet, 2011).

Evidence has been provided in recent years suggesting that this is still the case. In the case of IMF Article IV Consultation Report of 2025 for Ethiopia, it has been stated that the underdeveloped post-trade infrastructure facilities, which include the lack of proper custody and central securities depository, constitute a constraint in frontier African exchanges (International Monetary Fund, 2025). Furthermore, according to the World Bank report of 2024, in the case of low income countries, among the major operational challenges faced by the exchanges in developing capital markets are the shortcomings in clearing and settlement facilities (World Bank, 2024). In the case of Ethiopia, there was not any commercial bank which held custody licenses for ESX transactions until mid-2026 (Ethiopian Capital Market Authority, 2026).

Lack of licensed custodians by mid-2026 would present a major infrastructure shortfall which would essentially restrict growth of the market. If there are no custodians available who would act on behalf of investors by holding and securing the securities, then there would be many risks associated with investment that would keep investors away from investing in the market.

Thus, the quantitative mean of 3.33 concealed another problem altogether: whereas the survey respondents appeared relatively confident in the current methods for clearing and settling transactions, there was still no comprehensive structure of institutions in place. This indicated that any improvements in clearing and settling would necessitate not only improving the central depositary framework but also licensing custody and investment banks. This finding highlights a critical distinction between individual transaction processing and institutional ecosystem development. The former may be adequate, but the latter requires coordinated action by regulators and market participants.

4.4.3 Liquidity and Information Availability

Based on the criteria used in section 4.3 (Best & Kahn, 2016), which categorized scores from 3.41 to 4.20 as High, both liquidity (M = 3.70, SD = 0.887) and information available in the market (M = 3.69, SD = 0.904) attained high scores. It could be said that the participants felt they had enough. However, the standard deviations suggest moderate agreement, and the qualitative evidence reveals significant underlying concerns.

"What do you do when you try to set up a stockbrokerage business with only one stock? There is nothing to sell!" (FGD-01, Broker Focus Group)

This point illustrates a critical problem – with very few listed stocks, trading became difficult, and bid-offer spread was large (Levine & Zervos, 1998). The broker's rhetorical question captures the fundamental liquidity challenge: with only one listed security, the market lacks the diversity and trading volume necessary for meaningful price discovery and efficient trading.

However, an explanation of the differences between the high scores obtained quantitatively and the concerns expressed qualitatively is important. Since the majority of survey participants were finance professionals holding master's degrees and above (79.4%), the liquidity levels could have been rated based on the participant's expectations from an exchange that was just being set up. On the other hand, the brokers and market intermediaries rated liquidity levels based on their operational requirements, which included getting enough trading volumes to maintain their business activities. Up to mid-2026, only one security was listed in the ESX (Ethiopian Securities Exchange, 2026). This divergence between quantitative and qualitative findings reflects differences in reference points. Finance professionals may assess liquidity as "adequate" relative to expectations for a newly established market, while brokers assess it relative to their business viability requirements.

Research from other frontier markets indicates that liquidity arises slowly. In 2025, a study by the African Development Bank showed that among twelve Sub-Saharan African stock markets established since the year 2000, the average period of time for attaining a fifth-listed security stood at 3.2 years while that of obtaining a monthly trading volume exceeding $1 million stood at 4.5 years (African Development Bank, 2025). The Nairobi Stock Exchange, which is often quoted as an example in the region, had only two listed firms during the first three years of operation (Omuchesi et al., 2014). These observations suggest that although Ethiopia faces significant liquidity challenges in its first year, such a problem is normal. The comparison with other frontier markets provides important context for interpreting Ethiopia's liquidity challenges. The ESX's experience is consistent with patterns observed in other markets, suggesting that liquidity issues are not unique to Ethiopia but rather reflect a normal developmental trajectory.

Also, the average of 3.69 concerning information availability did not reflect any existing problems. Although technical data might be available, the lack of research analysts and investment banks implies that there would be no analysis of these data (KII-CON-01). According to another investor interviewed, "Data without analysis is useless" (KII-INV-02). The distinction between data

availability and information analysis is crucial. While raw trading data may be technically available, the absence of research analysts to interpret and contextualize this data limits its value to investors. This creates a situation where information is theoretically available but effectively inaccessible to most investors. Hence, in addition to increasing the number of listed candidates, especially SOEs, more work on market information is needed to address liquidity issues.

From a Financial Development Theory perspective (Levine & Zervos, 1998), market liquidity is a key determinant of economic growth. Liquid markets reduce transaction costs, facilitate capital allocation, and improve corporate governance. The low liquidity observed in the ESX limits its potential contribution to economic growth and represents a significant development challenge.

4.4.4 Synthesis of Infrastructure Challenges

Market operation and infrastructure evaluation highlights the fact that the trading platform and information access are moderately well-rated but clearing and settlement, and the overall institutional structure, remain extremely underdeveloped. Based on the quantitative results, the satisfaction level with the market infrastructure is medium, while qualitative data points to significant shortcomings including trading suspension, lack of custodians, and the “chicken and egg” problem.

Analytically, infrastructure problems outlined above fall under the theoretical framework developed by Esayas Ephrem (2022). Specifically, inefficiencies in the clearing and settlement processes are recognized as an important barrier to capital market development in Ethiopia. In addition, the problems outlined above fit into the Committee on Payments and Market Infrastructures and IOSCO (2012) principles where clearing, settlement, and custody infrastructure is viewed as a precondition for financial stability.

Infrastructure problems outlined above pose not only an operational challenge but also a development barrier. While some infrastructure problems (trading platform usability) can be fixed through gradual improvements, other issues (custody infrastructure) are likely to be solved through coordinated policy interventions and investments. In particular, the "chicken and egg" problem represents a significant challenge and needs strategic interventions.

According to the findings on the infrastructure, whereas the ESX's trading system was performing well, clearing and settlement were behind the times, as well as the overall structure of the

complementary institutions such as custodians, research analysts, and investment banks. Such findings further build on the findings of Esayas Ephrem (2022) on clearing and settlement inefficiencies.

4.5 Market Participants and Capacity

The third research question aimed at investigating the impact of financial literacy and investor knowledge in the participation of capital markets in Ethiopia. Based on the decision rule given in section 4.3, whereby values between 3.41 and 4.20 meant high, those between 2.61 and 3.40 moderate, and those from 1.81 to 2.60 low (Best & Kahn, 2016), the descriptive statistics of participants and capacity are given below in Table 7.

Table 7: Market Participants and Capacity (N = 233)

Statement	Mean	Std. Deviation
There is a sufficient pipeline of Ethiopian companies ready and willing to list on the ESX.	3.58	0.921
Ethiopian institutional investors (e.g., pension funds, insurance firms) have the necessary expertise to invest effectively in the ESX.	3.71	0.891
There is adequate capacity and expertise among market intermediaries (brokers, dealers, analysts) operating in Ethiopia.	3.53	1.103
Retail investor awareness and understanding of capital market investment in Ethiopia are currently high.	3.90	0.921
Investor confidence in the fairness and potential profitability of the ESX is currently strong.	3.48	1.079

Note: Scale: 1 = Strongly Disagree, 2 = Disagree, 3 = Neutral, 4 = Agree, 5 = Strongly Agree

Source: Survey data (2026)

4.5.1 The Financial Literacy Paradox

One striking observation was found when comparing the two types of information concerning retail investors' awareness. The survey participants gave relatively high ratings to retail investors' awareness (M = 3.90, SD = 0.921), which represented the highest rating among all participant capacities. This high mean suggests that survey respondents, the majority of whom are finance professionals, perceive retail investor awareness as relatively strong. However, the standard

deviation indicates some disagreement, and the qualitative evidence reveals a completely different picture. Nevertheless, the qualitative data revealed a completely different picture.

According to a brokerage representative:

"Most Ethiopians do not understand the concept of stock exchange. They think it is about banks." (KII-BRK-02, Head of Trading, Brokerage Firm)

The academician researcher supported this opinion with statistics:

"Less than 15 percent of adults in Addis Ababa are able to define a share and a bond." (KII-ACA-02, Economist and Financial Inclusion Researcher)

The fact that less than 15% of Addis Ababa adults are financially literate presents a major hurdle for the development of the capital markets. In order to engage in share markets, an individual needs to understand the fundamentals of bonds and stocks. This illiteracy is indicative of the financial exclusion faced in Ethiopia, where according to African Development Bank (2021), more than 60% of the people are without access to financial services. The contradiction of high awareness levels with low levels of financial literacy is termed the "financial literacy paradox."

Such discrepancy raised several questions. The reasons behind such contradicting opinions could be explained.

Firstly, the survey sample comprised finance professionals (79.4%), who may have overestimated the retail awareness due to their nearness to financial markets and optimistic disposition (Guiso & Jappelli, 2005). The overestimation by finance professionals reflects a common cognitive bias where experts project their own knowledge and awareness onto the general population. This "false consensus effect" leads professionals to overestimate public understanding of their domain. Secondly, respondents may have assessed the term "high" in relation to the expectation level for a newly established market rather than as a standalone characteristic. The relative rather than absolute assessment of awareness may have led respondents to rate awareness as "high" compared to zero rather than compared to some objective standard. Thirdly, social desirability bias could have impacted respondents' answers as finance professionals may not be inclined to admit lack of awareness in their environment.

In contrast to quantitative results, qualitative data corresponded with objective measures better. According to Biazin and Waktola (2021), over 70% of adult Addis Ababa residents had a poor

understanding of capital markets. The African Development Bank (2021) noted that over 60% of Ethiopian population did not have access to any type of formal financial services whatsoever.

Theoretical implications for the financial literacy paradox can be drawn from the findings of Guiso and Jappelli (2005), who found that awareness, which involves knowing of the existence of the stock market and being aware of how one can participate, is an important determinant of market participation. The very low levels of basic financial literacy observed in this study indicate that awareness is a binding constraint to retail market participation. This result is also in line with the view by El Wassal (2013), that financial literacy in society creates analysts, advisers, and portfolio managers who develop institutions and intermediary services in the market.

4.5.2 Institutional Investor Caution

Although survey respondents rated the expertise of institutional investors rather high (M = 3.71, SD = 0.891), it became apparent through qualitative data analysis that expertise was not matched by participation. An insurance company chief investment officer stated:

"Our exposure to the ESX will continue to remain low at less than 1%." (KII-INV-01, Chief Investment Officer, Insurance Company)

The head of investments of a pension fund added:

"Where institutional investors lead, the rest will follow. We will not go first." (KII-PEN-01, Head of Investments, Pension Fund)

The allocation of "less than 1%" made by insurance firms and "we won't go first" made by the pension fund indicates serious coordination problem. Although there was permission by regulation to invest up to 5% of assets into stocks, institutional investors are investing much less because of uncertainty in the viability of the market. This is a vicious circle, because institutional investors will only invest when the market proves its viability, and the market can prove its viability only with institutional investments.

This was a very rational approach in an environment of uncertainty given that institutional investors were fiduciary in nature and would have put money into markets that were still experimental (Beck & Levine, 2004). This would result in a problem of coordination, whereby institutional investors would venture into the market when others prove the viability of the market, and vice versa. Coordination problem is a typical collective action problem whereby individuals

who behave rationally (wait and see) end up having a bad collective outcome (underdeveloped market).

Under the Financial Development Theory approach, the reluctance of the institutional investors in Ethiopia is not different from what happens in other frontier markets where institutional involvement comes after being legally allowed to do so. Institutional investor competence has to be developed through regulatory authorization and practical experience.

4.5.3 Intermediary Capacity and Company Readiness

Using the criterion for decision-making as stated in section 4.3 (Best & Kahn, 2016), whereby a mean score ranging from 3.41 to 4.20 was considered High, the intermediary capacity had a high mean score (M = 3.53, SD = 1.103). Nonetheless, the fairly large standard deviation pointed out great differences among the respondents. A consultant elaborated on the capacity deficiency as follows:

"The companies are not ready for it. There's always been that deficiency in the companies – poor financial reporting and poor governance." (KII-CON-02, Capital Markets Advisory Partner, Audit Firm)

The insight provided by the consultant underscores an important supply-side restriction – the issuers do not have the necessary financial reporting and governance capacity for listing on the stock exchange. The weakness here is not a technical one since it does not simply pertain to legal compliance issues but rather to the fundamental capacity issue facing corporations in Ethiopia.

This result supported the findings of the literature on Financial Development Theory. According to Levine and Zervos (1998), capital market development not only required the establishment of markets but also the readiness of the issuers. With the deficiency in financial reporting and governance, companies were unable to make their commitments to transparency credible (North, 1990).

Empirical research carried out recently proved that this remained a binding constraint. According to an issuer readiness assessment undertaken by the Ethiopian Capital Market Authority in 2025, out of the 120 companies that were assessed for possible listing in the market, only 12 reached financial reporting standards, and only five of them had proper corporate governance frameworks (Ethiopian Capital Market Authority, 2025). The issuer readiness assessment data reveals a stark

reality: of 120 companies assessed, only 12 met financial reporting standards and only 5 met governance requirements. This 10% readiness rate (for financial reporting) represents a significant constraint on market development. The lack of ready companies means that even if demand for listings exists, the supply of qualified issuers is severely constrained. Also, a report carried out by the World Bank (2024) indicated that insufficient issuer readiness was the most dominant cause for delays in listing for seven out of ten new stock exchange markets in frontier Africa.

This may mean that the high average value of 3.53 obtained from the surveys was an indicator of the assessment made by the respondents in regard to the intermediaries' capacity in absolute terms or an expectation of improvement in the future, rather than an indicator of existing readiness of potential issuers. As one respondent observed during the FGDs: "We have capable brokers, but they do not have anything to broker" (FGD-01). This implied that the binding constraint was not on the side of the intermediaries but on the side of issuer supply. The "nothing to broker" comment captures the supply-side constraint perfectly: the bottleneck is not intermediary capacity but the availability of qualified issuers.

From the viewpoint of Institutional Theory, the issuer readiness problem can be understood as the lack of formal institutions (transparency regulations) and informal institutions (governance practices) that promote accountability. The companies in Ethiopia need both regulatory and capacity-building measures to meet the criteria required for going public.

4.5.4 Informal Savings Mechanisms

The following statement from an academic research scholar on the existence and relevance of informal savings practices is cited below:

"Iddir, IQUB are not only savings institutions but also social institutions offering community and trust." (KII-ACA-02, Economist and Financial Inclusion Research Scholar)

This remark clearly pointed out both a problem as well as a possible solution. The reason why informal institutions like iddir or iqub were prominent forms of saving among households was that they could be easily accessed by people and were considered reliable (Allen et al., 2011). Yet another point to note is that these institutions worked beyond the conventional capital markets and directed funds to either personal consumption or towards real estate.

Some recent developments pointed out to a possible route towards integration. For instance, according to the African Development Bank (2024), in its 2024 pilot scheme in Rwanda, 15 percent of the funds collected by the savings groups operating informally have been funneled into government bonds via a digitized registration procedure. Other studies carried out in Kenya and Tanzania demonstrated that informal groups are ready to allocate some of their resources into formal investments under certain conditions, including appropriate training and a convenient onboarding scheme (World Bank, 2025). In Ethiopia, there is no shortage of savings conducted in an informal manner; a 2023 study showed that the total annual amount transferred through iddir and iqub amounted to 200 billion Ethiopian birr, which is about 15 percent of the country's GDP (Biazin & Waktola, 2023).

The key was formalization while preserving the social ties which made such institutions efficient. As one of the participants in focus group discussion put it: "I think people use iqub due to their acquaintances there; once a bank enters the scene, they'll exit" (FGD-02). This implied that for any attempt to integrate informal savings schemes with securities markets, their social character must be recognized through the development of hybrid products. It would be reasonable for ESX and ECMA to develop an 'iqub friendly' financial instrument with minimal thresholds and requirements.

4.5.5 Synthesis of Participation and Capacity Challenges

Market participant analysis and capacity demonstrate a complicated scenario where there is huge disparity between quantitative and qualitative data. In fact, the most intriguing discovery is that of the "financial literacy paradox," when despite high financial literacy awareness among finance professionals, objective assessment demonstrates extremely low financial literacy rates. "Less than 1%" institutional investor investment, "only 12 out of 120 companies" that conform to the financial reporting requirements, and 200 billion Ethiopian birr informal saving funds indicate serious problems regarding participation.

From the theoretical standpoint, such findings correlate with Financial Development Theory (Levine & Zervos, 1998), which takes into account the role of issuer readiness on one hand and investor participation on the other hand in the development of capital markets. Both the issues are relevant to the capital market of Ethiopia.

The results from the participant analysis showed a disjointed picture. Although survey results showed modest levels of confidence about the competence of participants, qualitative analysis showed that the level of financial literacy among the general public was quite poor, the institutional investors only served as observers and not as participants, and the readiness of the firms to be listed was low.

Findings from the synthesis of both quantitatively and qualitatively acquired data indicate that there is a pattern wherein financial professionals have positive perceptions about market participants and their capacity (high mean score). However, it is quite apparent that there is an underlying constraint, which can be seen in objective measures and qualitative findings.

4.6 Macroeconomic and External Environment

Research question four examined the effect of macroeconomic uncertainty on market performance and appeal. Using the decision criteria from section 4.3 (Best & Kahn, 2016), whereby mean score values between 3.41 and 4.20 meant High, between 2.61 and 3.40 was considered Moderate, while values between 1.81 and 2.60 represented Low, the descriptive statistics of macroeconomic and external environment variables are shown in Table 8.

Table 8: Macroeconomic and External Environment (N = 233)

Statement	Mean	Std. Deviation
Current macroeconomic conditions (e.g., inflation, exchange rate, FX availability) in Ethiopia are conducive to capital market development.	2.75	1.151
Government economic policies are generally supportive of the ESX's growth and stability.	3.67	0.809
Political stability in Ethiopia positively influences investor confidence in the ESX.	3.72	0.863
Global economic conditions currently present more opportunities than challenges for the ESX.	3.66	0.886

Note: Scale: 1 = Strongly Disagree, 2 = Disagree, 3 = Neutral, 4 = Agree, 5 = Strongly Agree

Source: Survey data (2026)

4.6.1 Macroeconomic Conditions as Binding Constraint

Following the decision rule set out in section 4.3 of Best & Kahn (2016), which classifies average values between 2.61 to 3.40 as Moderate, the variable for macroeconomic factors recorded the lowest mean value of all survey questions (M = 2.75, SD = 1.151). It fell within the moderate classification but less than the neutral classification value of 3.0, indicating that there was no agreement among the respondents regarding favorable conditions.

There were very persuasive reasons for this score. As mentioned by one of the brokers,

"Inflation at 25% means negative real returns. Why invest in stocks when you get 18% return from T-bills?" (KII-BRK-01, General Manager, Brokerage Firm)

This is an example of the implication of the CAPM that an investor would demand a compensation for the risks involved and inflation loss (Sharpe, 1964; Lintner, 1965). The fact was that even if there were fairly good returns in the government securities (18%), but since inflation (25%) was higher, it meant negative returns in general, and even more so when taking into account stock market risk.

The commercial bank treasury executive defined macroeconomic instability as the core impediment:

"Unless the rate of inflation is brought to single digit and exchange rate stabilized, the ESX cannot compete with the government debt." (KII-BNK-01, Treasury Executive, Commercial Bank)

This indicated that capital market development depended on macroeconomic stability. This was because capital market development came after macroeconomic stability in sequence (IMF, 2023).

Further information proved these fears valid. As pointed out by the IMF (2025), inflation in Ethiopia was estimated at 23.5 percent in 2024, and still above 20 percent in early 2025, while the value of the birr decreased by about 40 percent relative to the US dollar after the floatation of the exchange rate at the end of 2024. As estimated by the World Bank (2025), the returns realized by the securities listed on ESX were negative for its first 18 months of existence. In contrast to ESX, government treasury bills offered positive returns and were considered completely risk-free. As one participant in a focus group stated, "Why take equity risks when T-bills give double digit returns without any risk?" (FGD-02).

In fact, IMF (2025) also observed that capital market development always comes after macroeconomic stability. In Ethiopia's case, there was an opposite order in which ESX started operations when inflation rates were still very high. It meant an adverse beginning that could not be easily overcome even by improvements in the market's infrastructure. There were recent examples from peer countries that justified the sequencing process in developing capital markets. The Rwandan capital market came into operation only after achieving single-digit inflation and a forward foreign exchange market (African Development Bank, 2025). Kenya too succeeded in reducing inflation to single digits before launching equity marketing campaign (World Bank, 2024).

4.6.2 Currency Risk and Foreign Investment

A foreign portfolio manager highlighted currency risk as one of the barriers:

"Currency risk can be hedged in any way since there are no forward markets." (KII-FOR-01, Portfolio Manager, Emerging Markets Fund)

The lack of forward currency markets represents an infrastructure deficit that significantly limits foreign portfolio investments in this sector. The lack of forward markets means that there is no hedging of currency risks for foreign investors, leading to exposure to high risks. Together with the current 40% devaluation of the birr, this makes Ethiopia a very unattractive place for such investments.

This issue related directly to the theory of Interest Rate Parity (IRP). According to the Covered Interest Rate Parity (IRP) model, foreign investors can hedge against exchange rate risk through forward markets (Keynes, 1923). Without forward markets, foreign investors face unhedged currency risk, which forces them to require a higher risk premium from their investments (Froot & Thaler, 1990). The absence of forward markets means that Covered Interest Rate Parity cannot hold, as there is no mechanism for investors to eliminate exchange rate risk. This creates a fundamental barrier to foreign portfolio investment that cannot be addressed through market infrastructure improvements alone.

From an International Risk Premium standpoint, the lack of forward markets implies that foreign investors cannot hedge themselves against exchange risk. When coupled with the large amount of exchange rate volatility seen since the floating of the exchange rate, such risk premium is one that

is unacceptable for many institutions. It follows that such a risk premium would be larger than the returns on investment in Ethiopia.

4.6.3 Policy Support and Political Stability

According to the decision criteria set out in section 4.3 (Best & Kahn, 2016) whereby scores of 3.41 – 4.20 were considered as High, government policy support (Mean = 3.67, SD = 0.809) and political stability (Mean = 3.72, SD = 0.863) had high means while macroeconomic variables (Mean = 2.75) had moderate means. This was an indication that participants distinguished between economic reality (inflation, exchange rates, FX supply) and perception of government policy making process.

Nevertheless, the following quotations from the interviews brought important nuances. One foreign investor stated the following:

"Policies have to be consistent for at least five years. Ethiopia still falls short in that respect." (KII-FOR-01, Portfolio Manager, Emerging Markets Fund)

An academic analyst was worried about sustainability:

"The development of capital markets involves long-term dedication for many years to come. My worry is that political commitment might wane." (KII-ACA-01, Associate Professor of Finance, Unity University)

From the above statements, it can be seen that, despite being optimistic about the policy direction taken, it had not been translated into the necessary track record that the institutional and foreign investors demanded (World Bank, 2023).

4.6.4 Synthesis of Macroeconomic Findings

The macroeconomic analysis shows the most pronounced degree of consistency between quantitative and qualitative data in this study. The survey findings identify macroeconomic conditions as the weakest area of consideration (average rating = 2.75), and the qualitative findings consistently identify inflation, exchange rate instability, and foreign exchange shortages as the "binding constraint" on capital market development. This consistency between quantitative and qualitative findings provides strong evidence that macroeconomic instability is the most significant challenge facing the ESX.

The consensus on macroeconomic challenges reflects the fundamental economic reality: capital market development cannot succeed in the presence of severe macroeconomic instability. High inflation eliminates real returns, exchange rate uncertainty deters foreign investment, and foreign exchange shortages constrain capital flows. Until these macroeconomic challenges are addressed, the ESX will continue to face significant headwinds regardless of improvements in market infrastructure or regulatory frameworks.

The findings support the CAPM prediction that investors require compensation for systematic risk. In the Ethiopian context, systematic risk is extremely high due to macroeconomic instability, and the required compensation (returns) is not available. This makes equity investment economically irrational under current conditions.

Macro-economic analysis showed the most pronounced degree of consistency between quantitative and qualitative data in this study. From the survey, the macroeconomic environment came out as the weakest single area of consideration (average rating = 2.75). The interviews also indicated inflation, instability of exchange rates, and foreign exchange problems as the "constraining factor" in the development of capital markets. This corroborates the empirical finding of Ho and Odhiambo (2021) that macroeconomic stability is an important determinant of stock market development in Africa.

4.7 Prospects and Opportunities

Research question number six focused on possibilities of capital mobilization from local savings, providing finance to small and medium enterprises, and linking to international finance systems. Using the decision rule developed under Section 4.3 (Best & Kahn, 2016), which used scores of 3.41-4.20 to indicate High, all the opportunity factors were rated highly, as shown in Table 9 below.

Table 9: Prospects and Opportunities (N = 233)

Statement	Mean	Std. Deviation
Listing state-owned enterprises (SOEs) presents a major growth opportunity for the ESX.	3.54	1.090
Integrating financial technology (FinTech) solutions can significantly enhance the ESX's efficiency and reach.	3.73	0.965
The ESX has strong potential to attract significant foreign portfolio investment.	3.81	0.964
The ESX has strong potential to mobilize domestic savings (including from the diaspora).	3.63	0.867
The ESX offers a competitive and attractive alternative investment compared to existing options (e.g., bank deposits, real estate).	3.66	0.794

Note: Scale: 1 = Strongly Disagree, 2 = Disagree, 3 = Neutral, 4 = Agree, 5 = Strongly Agree

Source: Survey data (2026)

4.7.1 SOE Privatization as Market Catalyst

Applying the decision rule established in section 4.3 (Best & Kahn, 2016), where mean scores of 3.41 to 4.20 were interpreted as High, respondents rated the potential for SOE listings as a high opportunity (M = 3.54). However, the standard deviation (SD = 1.090) was the largest among all opportunity items, indicating significant disagreement among respondents. An institutional investor voiced a positive perspective:

“An Ethio-Telecom IPO will be the trigger that can change the ESX from being ‘curiosity’ to a market.” (KII-INV-01, Chief Investment Officer, Insurance Company)

As expressed in the broker focus group discussion, there was strong emphasis on the importance of anchor listings:

“How do you build a brokerage firm with one product? There is nothing to offer our clients.” (FGD-01, Broker Focus Group)

But experts highlighted that SOEs might be unprepared for their stock exchange listing.

"Very few companies are ready for that because they have a lot of gaps: lack of financial reporting, good governance practices." (KII-CON-02, Capital Markets Advisory Partner, Audit Firm)

This situation indicated that the timing was important to consider. Listing SOEs too soon might hurt the reputation of the stock exchange due to any governance failure, while listing SOEs too late might deprive the market of required liquidity (World Bank, 2022).

This became evident in recent assessments carried out. According to the assessment by the Ethiopian Capital Market Authority (2025), of the first SOEs chosen for listing, Ethio-Telecom was the only one to have made any progress in aligning with the requirements of financial reporting, but it had not fully succeeded in doing so. Another assessment was conducted by the African Development Bank (2025) on the issue of privatization of SOEs in frontier markets where it established that too fast privatization resulted in scandalous issues of corporate governance in three out of seven cases, while too slow privatization brought about closure of exchanges for lack of liquidity in two others.

4.7.2 Diaspora Finance as Low-Hanging Opportunity

Using the decision rule stated in section 4.3 (Best & Kahn, 2016), where scores of 3.41 to 4.20 were interpreted as High, diaspora finance received a score on the higher side (M = 3.63, SD = 0.867). A consultant presented the following quantitative assessment:

"Diasporas send $5-7 billion each year. That means even a meager 5% will still generate $250-350 million yearly." (KII-CON-01, Senior Partner, Consulting Firm)

The institutional investor added:

"Diaspora is an enormous business opportunity. They have the intention of investing in their home countries." (KII-INV-02, Investment Manager, Pension Fund)

The Diaspora Finance opportunity was especially important because it met several constraints at once; it offered foreign exchange (FX constraint), investors with financial literacy (awareness constraint), and patient money (liquidity constraint) (UNECA, 2023).

The recent data further confirmed the potential. According to the National Bank of Ethiopia (2025), annual diaspora remittances reached $6.2 billion in the financial year 2024/25. It is also known that there are about 3 million Ethiopians abroad, but less than 1 percent of their remittances have been invested in formal investment schemes, most of which are being used for family expenses and property investments (World Bank, 2025). Some peer countries proved to be successful in tapping the diaspora. Kenya's diaspora bond issued in 2017 collected over $300 million through

subscription by over 65 percent of non-resident Kenyans (Kenyan Capital Markets Authority, 2024). Nigeria, too, was able to collect $500 million in its first diaspora bond (Nigerian Debt Management Office, 2023). Very recently, Rwanda launched a digital diaspora investment facility in 2024 allowing remote account opening and mobile trading; it has brought in 12,000 investors in six months (Rwandan Capital Market Authority, 2025).

For Ethiopia, taking advantage of this would entail surmounting several challenges. A focus group participant indicated: “The challenge isn’t in their willingness. The issue is the process. It can take months, if not years, just to open an account from outside the country” (FGD-02). A consultant said: "What we need is something that will attract diaspora investors' confidence. They are smart people. They can tell the difference between good investments and bad ones" (KII-CON-01). Among the suggestions made by United Nations Economic Commission for Africa (2023) include the establishment of a specialized unit at ECMA to handle diaspora investment initiatives, simplification of onboarding procedures through digitization, and a pilot diaspora bond with tax incentives. Ethiopian Securities Exchange (2026) planned to launch its first diaspora investment product by end of 2026.

4.7.3 Product Innovation: Islamic and Green Finance

Though the survey question on FinTech integration earned a very high mean score (M = 3.73, SD = 0.965) based on the decision rule outlined in section 4.3 (Best & Kahn, 2016), the qualitative analysis identified two niche areas of product innovation that were not fully addressed in the survey questions. A consultant stated:

"There are probably 35-40 percent Muslims in the Ethiopian population, but no Shariah compliant investment products at all" (KII-CON-02).

A focus group added:

"Ethiopia will never compete in terms of size, but it will be competitive in terms of innovations. Identify your niches and become an expert" (FGD-04).

This strategy had already been applied in the case of Morocco, which saw its Casablanca Stock Exchange become a leader in green and Islamic financing despite the smaller size of its market (AMMC, 2022). Morocco had sold $2.5 billion worth of green bonds and $1.8 billion worth of sukuk by 2025, while also drawing in considerable foreign portfolio investments (Moroccan

Capital Market Authority, 2025). For Ethiopia, the opportunity to leverage its Islamic finance was high. At 35-40 percent, the Muslim population in the country accounted for some 45-50 million people, and there still existed a need for Shariah-compliant financial products (Pew Research Center, 2020). According to the World Bank (2024), the annual green infrastructure financing gap in the country stood at $3 billion per year.

The regulatory changes were promising. In 2025, the National Bank of Ethiopia released its first directive on Islamic finance, licensing seven banks without interest (National Bank of Ethiopia, 2025). Yet, no directive existed from the ECMA for sukuk or green bonds, and no products were available on the ESX by mid-2026 (Ethiopian Capital Market Authority, 2026). The reasons behind the delay were explained by an expert: "The framework of sukuk issuance is complicated. You need a new tax and contracts legislation. But it can be done, and there is demand for it" (KII-CON-02). The example of neighboring countries pointed to a certain sequence to follow: pilot issue of green bonds from a SOE (e.g., Ethiopian Electric Power) and then sukuk issuance by the government to show how it works. Kenya managed to issue its sukuk worth $150 million in 2022; the bond was oversubscribed by 40 percent (Kenyan Capital Markets Authority, 2023).

4.7.4 Regional Integration

Progress on regional integration was noted in ESX's communication to its management:

"We have been talking to both the NSE and RSE about cooperation agreements." (KII-ESX-01, Senior Manager, Operations, ESX)

The ESX's engagement with the Nairobi Securities Exchange (NSE) and Rwanda Securities Exchange (RSE) represents an important step toward regional integration. Cooperation agreements with these more established exchanges could facilitate knowledge transfer, technical assistance, and potentially cross-listing arrangements.

Benefits of regional integration included knowledge transfer from exchanges that were more experienced (NSE, RSE), cross-listing possibilities, and infrastructure sharing (ASEA, 2023). Although regional integration was a promising approach, it scored relatively low on the thematic coding matrix, indicating it was not seen as immediate by most stakeholders. While regional integration is recognized as a promising opportunity, it is not seen as an immediate priority by most stakeholders. This suggests that while the long-term potential of regional integration is

recognized, stakeholders view domestic capacity development as a more immediate and urgent priority.

4.7.5 Synthesis of Opportunities

The analysis of prospects and opportunities reveals that stakeholders are optimistic about the long-term potential of the ESX, with all opportunity items scoring above 3.5. Foreign portfolio investment received the highest average score (3.81), followed by FinTech integration (3.73), domestic savings mobilization (3.63), alternative investment appeal (3.66), and SOE privatization (3.54).

The high scores on opportunities suggest that stakeholders believe the ESX has significant long-term potential despite current challenges. However, the qualitative analysis reveals important nuances: SOE privatization is seen as the most important catalyst but also the riskiest, diaspora finance is seen as a low-hanging opportunity with significant potential, and niche product development (Islamic and green finance) is seen as a competitive advantage in a small market.

From a Financial Development Theory perspective (Levine & Zervos, 1998), the realization of these opportunities depends on addressing the binding constraints identified in previous sections. The opportunities identified represent potential catalysts for market development, but they cannot succeed in the absence of the regulatory, infrastructural, human capital, and macroeconomic conditions necessary for market functioning.

Opportunities were perceived optimistically in their long-run outlook, with foreign portfolio investment having the highest average score (3.81). Realizing these opportunities was only possible upon overcoming the challenges associated with regulation, infrastructure, literacy, and macroeconomics previously identified in previous sections. This observation corresponded with the Financial Development Theory, which stated that for a market to thrive, there must be appropriate institutions and an ideal macroeconomic climate (Levine & Zervos, 1998; Beck & Levine, 2004).

4.8 Integration of Qualitative and Quantitative Findings

The integration of qualitative and quantitative findings is essential for a comprehensive understanding of the research problem. Table 10 synthesizes the convergence and divergence patterns across the six research questions. This integration provides a transparent framework for

synthesizing findings from different methodologies and identifying patterns of convergence, divergence, and complementarity.

Table 10 synthesized the convergence and divergence patterns across the six research questions.

Table 10: Integration Matrix: Qualitative and Quantitative Convergence

Research Question	Quantitative Finding	Qualitative Finding	Convergence Type
RQ1: Regulatory	Shareholder protection weakest (M=3.00)	Commercial Code outdated; enforcement gaps	Strong convergence
RQ2: Infrastructure	Clearing/settlement weakest (M=3.33)	Trading halts; ecosystem incomplete	Moderate convergence
RQ3: Literacy	Perceived high (M=3.90)	Objectively low (<15% define share/bond)	Divergence
RQ4: Macroeconomic	Only sub-3.0 item (M=2.75)	"Binding constraint"; 14/14 participants	Strong convergence
RQ5: Political	Positive (M=3.72)	Foreign investor concerns; will may fade	Divergence
RQ6: Opportunities	All >3.5; SOE highest variance	SOE catalyst; diaspora; Islamic finance	Strong convergence

Source: Author's compilation (2026)

The integration matrix reveals three distinct patterns:

First, strong convergences on RQ1 (regulatory), RQ4 (macroeconomic), and RQ6 (opportunities) indicate that these are areas where the evidence is most consistent across methods. The regulatory challenges identified (especially shareholder protection), the macroeconomic constraints (especially high inflation), and the opportunities identified (especially SOE privatization and diaspora finance) represent findings that can be reported with a high degree of confidence. This consistency across methods strengthens the evidence base for these conclusions.

Second, the divergence on RQ3 (financial literacy) is particularly instructive from a methodological perspective. Survey respondents (finance professionals) perceived high retail investor awareness, while interviewees and objective evidence showed extremely low financial literacy (less than 15% of Addis Ababa adults can define a share and a bond). This divergence likely reflects: (1) different reference points (finance professionals assessing awareness relative to expectations, academics assessing absolute levels), (2) different definitions (awareness versus understanding), and (3) potential biases (optimism among finance professionals, objective measures in academic assessments).

Third, the divergence on RQ5 (political factors) reflects stakeholder differences. Ethiopian professionals rated political stability more positively than foreign investors and academics. This suggests that proximity to local institutions and familiarity with political processes may influence perceptions of stability. The divergence highlights the importance of stakeholder perspective: what appears stable to local actors may not be perceived as sufficiently stable by external investors requiring a demonstrated track record.

Three patterns emerged from the integration process.

First, clear convergences on RQ1, RQ4, and RQ6 showed that regulatory problems (especially related to shareholder protection), macroeconomic challenges (especially related to inflation rates), and opportunity zones (especially concerning the listing of state-owned enterprises and diaspora financing) were consistent issues. They could be reported with a high degree of certainty.

Second, the divergent results regarding RQ3 (financial literacy) were interesting from a methodological perspective but did not pose any problems. Survey participants, who mainly comprised financial experts, felt that the level of retail knowledge was high, whereas interviewees, who included academics and people with solid numbers, believed that it was extremely low. The difference probably came from the nature of the samples and definitions used. The divergence on financial literacy highlights the importance of triangulation in mixed-methods research: relying solely on either quantitative or qualitative data would have produced an incomplete picture. The quantitative data provides insights into stakeholder perceptions, while the qualitative data provides objective measures of actual literacy levels. Together, they reveal a significant perception-reality gap.

Third, divergences on RQ5 (political aspects) were caused by the perspectives of the stakeholders. Ethiopia's professionals believed that political stability was moderate, while investors and academics had more concerns about it. The results implied that additional signals might be necessary to increase the confidence of foreign investors. The divergence on political factors highlights the importance of stakeholder perspective: domestic professionals and foreign investors have different reference points, information sources, and risk assessments. This suggests that confidence-building measures targeted specifically at foreign investors may be necessary.

Overall, the integration of quantitative and qualitative findings provides a comprehensive picture of the challenges and opportunities facing Ethiopia's capital market. The patterns of convergence and divergence identified in Table 10 provide a transparent framework for interpreting findings and identifying areas of consensus and disagreement. This integrated approach strengthens the validity of the conclusions and provides a robust evidence base for recommendations.

CHAPTER FIVE

SUMMARY, CONCLUSIONS, AND RECOMMENDATIONS

5.1 Introduction

The present chapter discusses the conclusion, findings, and recommendations of the study conducted in order to examine the problems faced after the launch of the capital market and opportunities arising out of this problem in the Ethiopian capital market, particularly focusing on the ESX. The chapter starts with a brief discussion on the objectives, methods, and main results of the research. The subsequent sections of the chapter give conclusion made after a combined analysis of quantitative and qualitative data.

5.2 Summary of the Study

The subsequent bullets list major features of the study, ranging from its purpose to methodologies adopted, and findings made in various areas of investigation.

- To investigate post-launch problems and potential opportunities in Ethiopia's capital markets, especially those of the ESX.
- Mixed methods approach that is predominately qualitative; survey was administered to 233 respondents (90.3% return rate); 14 key informant interviews conducted; 4 FGDs carried out; analysis employed descriptive statistics and thematic analysis.
- The lowest survey mean was attained by minority shareholder protection (M = 3.00, SD = 1.209). Outdated 1960 Commercial Code, inadequate ECMA enforcement capabilities, lack of secondary legislation, poor cooperation of ECMA with NBE.
- Clearing and settlement received the lowest score (M = 3.33, SD = 1.144). There were three unplanned shutdowns in trading because of technical reasons. Underdevelopment of custody, research, and investment banking systems.
- While the perception about retail awareness was very high (M = 3.90), qualitative information revealed that less than 15% of the Addis Ababa residents could understand the concepts of shares and bonds. The institutional investor portfolio had been invested below 1% in the ESX even though 5% was allowed. Informal saving mechanisms like iddir and iqub were dominant.

- Macroeconomics ranked last with a very low mean score of (M = 2.75). An inflation rate of 25%, exchange rate risk, and forex shortage were found to be the binding constraints. However, the returns on government security was 18% with negative returns from inflation.
- High scores were recorded for political stability (M = 3.72) and government policy support (M = 3.67). However, the five-year policy consistency required by foreign investors is not yet in place.
- All opportunities had mean scores above 3.5. Foreign Portfolio Investment (FPI) received the highest mean (M = 3.81). Opportunities identified: privatization of SOE (Ethio Telecom IPO); finance from Diaspora (US$5-US$7 billion per year); Islamic Finance (35%-40% Muslims); Green Bond (US$3 billion annual gap); and Integration with NSE and RSE.

5.3 Conclusions

From the comprehensive findings, the following conclusions have been made.

- Ethiopia has Proclamation No. 1248/2021 and ECMA; however, minority shareholder protection is not developed owing to Commercial Code of 1960. Legislation related to foreign portfolio investment is insufficiently developed. Collaboration between ECMA and NBE is not present and institutional involvement is not possible because of that.
- The platform of ESX operates; however, clearing and settlement systems are not sufficiently developed. Technological failures result in halting trades. In addition, lack of custodian banks, analysts and investment banking is creating vicious circle of liquidity issues.
- Less than 15% of adult residents of Addis Ababa have knowledge of the capital market basics. Institutional investors use a "wait-and-watch" attitude, dedicating less than 1% of their portfolios to the same. Savings through informal structures (iddir, iqub) are successful, however informal.
- High inflation around 25%, volatile exchange rates, and FX shortages are hindering equity investments in favor of government securities. There is no forward currency market, thus no hedge against the exchange rate risk.

- Internal stakeholders show a positive view towards policy stability and continuity. Still, international investors demand five years of policy continuity, which has yet to be demonstrated by Ethiopia.
- Privatizations of SOEs such as Ethio Telecom may stimulate the capital market if they are prepared for issuing securities. Diaspora finance provides stable and FX-invested funding, while Islamic finance and green bonds offer a special edge.

5.4 Recommendations

Based on the findings and conclusions of this study, the following recommendations are made for policymakers, regulators, and market participants to address the post-launch challenges and leverage the emerging prospects of Ethiopia's capital markets.

First, regulatory and macroeconomic reforms are essential prerequisites for capital market development. The government must coordinate monetary and fiscal policies to reduce inflation to single-digit levels, enabling equity investments to generate positive real returns. The 1960 Commercial Code should be amended without delay to provide adequate protection for minority shareholders, incorporating modern corporate governance standards aligned with IOSCO principles. All secondary legislation, particularly regulations governing foreign portfolio investment and institutional investor participation, should be finalized and enacted within six months. A formal coordination mechanism between ECMA and NBE, modeled after successful frameworks in Rwanda and Kenya, should be established to eliminate regulatory overlaps and expedite institutional investment mandates.

Second, infrastructure development and market capacity building require significant and sustained investment. The ESX should improve clearing and settlement systems to enhance operational efficiency and reduce counterparty risk. A robust redundancy plan for telecommunication lines and trading systems should be implemented to prevent unplanned trading halts. Regulatory incentives should be introduced to encourage commercial banks to obtain custody licenses and establish securities depository services. Research capacity should be developed through collaboration between ESX, ECMA, universities, and professional bodies to train research analysts and investment bankers. A comprehensive national financial literacy program should be launched, leveraging existing informal savings mechanisms such as iddir and iqub as delivery channels.

Third, market development and product innovation should focus on anchor listings, diaspora mobilization, niche products, and regional integration. The listing of Ethio-Telecom should be prioritized as an anchor listing that can catalyze market development and transform the ESX from a novelty into a functional market. Technical support and capacity building should accompany this for other SOEs to ensure they meet financial reporting and corporate governance standards prior to listing. Specialized investment products with simplified digital onboarding processes should be developed to mobilize diaspora finance, with a pilot diaspora bond with tax incentives serving as a proof of concept. ECMA should issue directives for sukuk and green bonds, drawing on technical assistance from more experienced African stock exchanges. Regional integration should be pursued through cooperation agreements with the Nairobi Securities Exchange and Rwanda Securities Exchange.

Fourth, institutional coordination and stakeholder engagement must be strengthened to build market confidence. A steering committee comprising pension funds, insurance companies, and commercial banks should be established to work collaboratively with ECMA and NBE on capital market development initiatives. Research capabilities should be strengthened through exchange visits and secondment arrangements with established exchanges such as the Nairobi Securities Exchange. Finally, to build foreign investor confidence, the government must demonstrate sustained policy consistency over time, recognizing that institutional investors typically require a five-year track record of policy stability.

5.5 Limitations and Future Research Directions

There were some limitations associated with this study, and they need to be highlighted. The investigation was limited to Addis Ababa City only, where no consideration was made for perspectives from other parts of Ethiopia, reducing the external validity of results obtained in terms of application to the entire nation. This research used cross-sectional design to collect data on one single occasion (April 2026, just 27 months after the establishment of ESX), making it challenging to analyze trends, crises, and development of governance practices throughout the life cycle of this market. Purposive and quota sampling were used for sampling, while the sample included highly educated people (79.4% with graduate education). Bias due to participants holding certain opinions was overcome using triangulation, and potential bias on account of the position of researchers as Ethiopians was controlled using memos and investigator triangulation.

Considering these constraints, it is imperative that future studies incorporate a longitudinal approach extending three to five years in order to examine the dynamic nature of ESX as well as the existence of causation in the phenomenon. It is important for researchers to objectively gauge the level of financial literacy using validated instruments, including the World Bank's Financial Capability Survey with representative samples across nations. Comparative cases of countries such as Rwanda and Kenya will also be instrumental in determining appropriate sequences of regulatory reforms and diaspora mobilizations. In addition, there is need for pilot projects investigating ways to merge informal saving practices (iddir and iqub) with formal capital markets. Research on diaspora investment product development and promotion to ensure effective use of billions of dollars of remittances every year is also crucial. Lastly, time series analysis of macroeconomic-market interaction and political economy analysis through process tracing and elite interviewing is necessary.

References

Abebe, D. (2021). *The infancy stage of capital market development in Ethiopia: Structural and institutional constraints*. Ethiopian Economics Association.

Absa & OMFIF. (2023). *African capital markets: South Africa and Morocco country reports*. Absa Group Limited.

Acharya, V. V., & Richardson, M. (2009). *Restoring financial stability: How to repair a failed system*. John Wiley & Sons.

Adonay, N. (2021). Regulatory challenges in emerging capital markets: The Ethiopian perspective. *Journal of African Financial and Economic Development, 4*(2), 45–67.

African Development Bank. (2005). *African development report: Bankwide operational plan for the privatization of public enterprises in Africa*. Oxford University Press.

African Development Bank. (2021). *Financial sector development in Africa: Opportunities and challenges*. African Development Bank Group.

African Development Bank. (2024). *Informal savings groups and capital market integration: Lessons from Rwanda*. AfDB.

African Development Bank. (2025a). *Forward FX markets and foreign portfolio investment in frontier Africa*. AfDB.

African Development Bank. (2025b). *Frontier capital markets in Africa: A longitudinal study of exchange development*. AfDB.

African Development Bank. (2025c). *Sequencing financial sector reforms: Lessons from Rwanda and Kenya*. AfDB.

African Development Bank. (2025d). *SOE privatizations and capital market development in frontier Africa*. AfDB.

African Securities Exchanges Association. (2022). *Annual report and market statistics 2022*. ASEA.

African Securities Exchanges Association. (2023). *Annual report and market statistics 2023*. ASEA.

Alfaro, L., Kalemli-Ozcan, S., & Sayek, S. (2008). FDI, productivity, and financial development. *The World Economy, 31*(1), 111–135.

Allen, F., Otchere, I., & Senbet, L. W. (2011). African financial systems: A review. *Review of Development Finance, 1*(2), 79–113.

American Psychological Association. (2020). *Publication manual of the American Psychological Association* (7th ed.).

AMMC (Moroccan Capital Market Authority). (2020). *Annual report 2020: Strengthening oversight and transparency*. AMMC.

AMMC (Moroccan Capital Market Authority). (2022). *Green and sustainable finance in Morocco: Progress report*. AMMC.

AMMC (Moroccan Capital Market Authority). (2025). *Sustainable finance dashboard 2025*. AMMC.

Ball, R., & Brown, P. (1968). An empirical evaluation of accounting income numbers. *Journal of Accounting Research, 6*(2), 159–178.

Bank for International Settlements. (2022). *Basel III: Finalising post-crisis reforms*. BIS.

Beck, T., & Levine, R. (2004). Stock markets, banks, and growth: Panel evidence. *Journal of Banking & Finance, 28*(3), 423–442.

Bekaert, G., & Harvey, C. R. (1995). Time-varying world market integration. *Journal of Finance, 50*(2), 403–444.

Ben Omri, W., Ben Salah, M., & Ben Mbarek, H. (2020). Economic growth and stock market development: An empirical analysis. *Journal of the Knowledge Economy, 11*(3), 1123–1143.

Best, J. W., & Kahn, J. V. (2016). *Research in education* (10th ed.). Pearson Education.

Biazin, T., & Waktola, D. (2021). Financial literacy and investor awareness in Ethiopia: Barriers to capital market participation. *Ethiopian Journal of Business and Economics, 11*(1), 34–56.

Biazin, T., & Waktola, D. (2023). The scale and scope of informal savings in Ethiopia: Estimates from Addis Ababa. *Ethiopian Journal of Economics, 32*(1), 45–68.

Black, F. (1974). International capital market equilibrium with investment barriers. *Journal of Financial Economics, 1*(4), 337–352.

Bodie, Z., Kane, A., & Marcus, A. J. (2021). *Investments* (12th ed.). McGraw-Hill Education.

Borensztein, E., De Gregorio, J., & Lee, J. W. (1998). How does foreign direct investment affect economic growth? *Journal of International Economics, 45*(1), 115–135.

Borio, C. (2003). Towards a macroprudential framework for financial supervision and regulation? *CESifo Economic Studies, 49*(2), 181–215.

Braun, V., & Clarke, V. (2006). Using thematic analysis in psychology. *Qualitative Research in Psychology, 3*(2), 77–101.

Capital Markets Authority Kenya. (2023). *Green bond issuance report*. CMA Kenya.

Capital Markets Authority Kenya. (2024). *Diaspora bond performance evaluation*. CMA Kenya.

Carson, J. (2011). *Self-regulatory organizations: A comparative analysis of regulatory paradigms*. IOSCO.

Cepni, O., Guney, I. E., & Swanson, N. R. (2020). Political instability and stock market returns: Evidence from emerging markets. *Emerging Markets Review, 45,* Article 100736.

Climate Bonds Initiative. (2023). *Green bonds in Africa: Morocco as a regional hub*. Climate Bonds Initiative.

Committee on Payments and Market Infrastructures & International Organization of Securities Commissions. (2012). *Principles for financial market infrastructures*. BIS.

Creswell, J. W., & Clark, V. L. P. (2017). *Designing and conducting mixed methods research* (3rd ed.). SAGE Publications.

Creswell, J. W., & Creswell, J. D. (2018). *Research design: Qualitative, quantitative, and mixed methods approaches* (5th ed.). SAGE Publications.

Creswell, J. W., & Plano Clark, V. L. (2018). *Designing and conducting mixed methods research* (3rd ed.). SAGE Publications.

Creswell, J. W., & Poth, C. N. (2018). *Qualitative inquiry and research design: Choosing among five approaches* (4th ed.). SAGE Publications.

Du, W., & Schreger, J. (2024). Uncovering CIP deviations in emerging markets: Distinctions, determinants, and disconnect. *IMF Economic Review, 72*, 196–252.

El Wassal, K. A. (2013). *The role of the legal and regulatory environment in stock market development* (Working Paper). International Finance Corporation.

Esayas Ephrem. (2022). *Market infrastructure and capital market efficiency in Ethiopia* [Unpublished master's thesis]. Addis Ababa University.

Ethiopian Capital Market Authority. (2025). *Issuer readiness assessment report*. ECMA.

Ethiopian Capital Market Authority. (2026a). *Foreign portfolio investment regulations: Status update*. ECMA.

Ethiopian Capital Market Authority. (2026b). *Quarterly institutional investor survey Q2 2026*. ECMA.

Ethiopian Capital Market Authority. (2026c). *Quarterly market report Q2 2026*. ECMA.

Ethiopian Securities Exchange. (2026a). *ESX launches Neway mobile and web trading platform* [Press release]. Addis Ababa.

Ethiopian Securities Exchange. (2026b). *Market statistics report Q2 2026*. ESX.

Ethiopian Securities Exchange. (2026c). *Strategic roadmap 2026–2028*. ESX.

European Securities and Markets Authority. (2023). *Guidelines on market conduct and investor protection*. ESMA.

Fabozzi, F. J., Modigliani, F., & Jones, F. J. (2022). *Foundations of financial markets and institutions* (5th ed.). Pearson Education.

Fama, E. F. (1970). Efficient capital markets: A review of theory and empirical work. *Journal of Finance, 25*(2), 383–417.

Fama, E. F., & French, K. R. (1992). The cross-section of expected stock returns. *Journal of Finance, 47*(2), 427–465.

Federal Democratic Republic of Ethiopia. (2021a). *Capital market proclamation No. 1248/2021*. Federal Negarit Gazeta.

Federal Democratic Republic of Ethiopia. (2021b). *Ten years perspective plan (2021–2030)*. National Planning and Development Commission.

Field, A. (2013). *Discovering statistics using IBM SPSS Statistics* (4th ed.). SAGE Publications.

Financial Stability Board. (2022). *Global monitoring report on non-bank financial intermediation*. FSB.

Financial Times. (2024, January 15). Nigeria's foreign exchange volatility tests capital market resilience. *Financial Times*.

Froot, K. A., & Thaler, R. H. (1990). Anomalies: Foreign exchange. *Journal of Economic Perspectives, 4*(3), 179–192.

Guiso, L., & Jappelli, T. (2005). Awareness and stock market participation. *Review of Finance, 9*(4), 537–567.

Hair, J. F., Black, W. C., Babin, B. J., & Anderson, R. E. (2019). *Multivariate data analysis* (8th ed.). Cengage Learning.

Ho, S. Y., & Odhiambo, N. M. (2021). Financial development and economic growth: Evidence from selected African countries. *Journal of African Development, 23*(1), 45–63.

Hodrick, R. J. (1987). *The empirical evidence on the efficiency of forward and futures foreign exchange markets*. Harwood Academic Publishers.

Hull, J. C. (2022). *Options, futures, and other derivatives* (11th ed.). Pearson Education.

International Monetary Fund. (2017). *Global financial stability report: Is growth at risk?* IMF.

International Monetary Fund. (2021). *Securities regulation and emerging markets: A framework for assessment*. IMF.

International Monetary Fund. (2022). *South Africa: Financial sector assessment program*. IMF.

International Monetary Fund. (2023). *Ethiopia: Staff report for the 2023 Article IV consultation*. IMF.

International Monetary Fund. (2025a). *Ethiopia: Staff report for the 2025 Article IV consultation.* IMF.

International Monetary Fund. (2025b). *IMF Executive Board completes third review under the Extended Credit Facility (ECF) arrangement for Ethiopia and concludes the 2025 Article IV consultation* (Press Release No. 25/234). IMF.

International Organization of Securities Commissions. (2017). *Principles for securities regulation*. IOSCO.

International Organization of Securities Commissions. (2021). *Supervision of market intermediaries: Final report*. IOSCO.

JSE Limited. (2023). *Johannesburg Stock Exchange historical overview and annual report*. JSE.

Kenyan Capital Markets Authority. (2024). *Institutional investor participation report 2024*. CMA Kenya.

Keynes, J. M. (1923). *A tract on monetary reform*. Macmillan.

Kunt, A. D., Klapper, L. F., Singer, D., & Van Oudheusden, P. (2015). *The Global Findex Database 2014: Measuring financial inclusion around the world*. World Bank.

Kvale, S., & Brinkmann, S. (2009). *InterViews: Learning the craft of qualitative research interviewing* (2nd ed.). SAGE Publications.

Levine, R., & Zervos, S. (1998). Capital control liberalization and stock market development. *World Bank Economic Review, 12*(1), 41–76.

Lincoln, Y. S., & Guba, E. G. (1985). *Naturalistic inquiry*. SAGE Publications.

Lintner, J. (1965). The valuation of risk assets and the selection of risky investments in stock portfolios and capital budgets. *Review of Economics and Statistics, 47*(1), 13–37.

Lo, A. W., & MacKinlay, A. C. (1988). Stock market prices do not follow random walks: Evidence from a simple specification test. *Review of Financial Studies, 1*(1), 41–66.

Madura, J. (2014). *Financial markets and institutions* (11th ed.). Cengage Learning.

Meron Desta. (2023). Blockchain and artificial intelligence in emerging capital markets: Prospects for Ethiopia. *Ethiopian Journal of Finance and Development, 2*(1), 78–99.

Mishkin, F. S., & Eakins, S. G. (2021). *Financial markets and institutions* (9th ed.). Pearson Education.

Mondaq. (2024, February 10). Egypt capital market reforms: Taxation and investor confidence. *Mondaq Business Briefing*.

Morgan, D. L. (1997). *Focus groups as qualitative research* (2nd ed.). SAGE Publications.

Moroccan Capital Market Authority. (2025). *Sustainable finance dashboard 2025*. AMMC.

Muchiri, S. (2015). *Automation and demutualization of the Nairobi Securities Exchange: Challenges and outcomes* [Unpublished master's thesis]. University of Nairobi.

Muiruri, J. (2023). Product innovation and investor education at the Nairobi Securities Exchange. *East African Journal of Business and Economics, 5*(2), 112–130.

Muiruri, J., & Maina, L. (2021). Green bonds and sustainability-linked products in East Africa. *Journal of Sustainable Finance and Investment, 11*(4), 345–362.

National Bank of Ethiopia. (2025a). *Annual diaspora remittance report 2024/25*. NBE.

National Bank of Ethiopia. (2025b). *Islamic banking directive and licensed institutions*. NBE.

NGX Group. (2020). *Nigerian Exchange Group: From demutualization to digital transformation*. NGX Group.

Nigerian Debt Management Office. (2023). *Nigeria diaspora bond: Final issuance report*. DMO Nigeria.

North, D. C. (1990). *Institutions, institutional change and economic performance*. Cambridge University Press.

Nunnally, J. C., & Bernstein, I. H. (1994). *Psychometric theory* (3rd ed.). McGraw-Hill.

Organisation for Economic Co-operation and Development. (2023). *OECD principles of corporate governance*. OECD.

Omuchesi, A. J., Oluoch, O., & Mwangi, M. (2014). Central depository system and efficiency of the Nairobi Securities Exchange. *International Journal of Finance and Accounting, 3*(6), 345–358.

Oxford Business Group. (2020). *The report: Egypt 2020 – Capital markets*. Oxford Business Group.

Pew Research Center. (2020). *Religious composition by country, 2010–2050*. Pew Research Center.

Prasad, E. S., Rajan, R. G., & Subramanian, A. (2007). Foreign capital and economic growth. *Brookings Papers on Economic Activity, 2007*(1), 153–230.

PwC. (2023). *Nigeria capital market: Digital assets and regulatory adaptation*. PwC.

Radelet, S., & Sachs, J. D. (1998). The East Asian financial crisis: Diagnosis, remedies, prospects. *Brookings Papers on Economic Activity, 1998*(1), 1–90.

Raubenheimer, H. (2019). SME listing platforms in South Africa: Experiences and lessons. *South African Journal of Economic and Management Sciences, 22*(1), 1–12.

Reinhart, C. M., & Rogoff, K. S. (2009). *This time is different: Eight centuries of financial folly*. Princeton University Press.

Rwandan Capital Market Authority. (2024). *Annual report 2023–2024*. RCMA.

Rwandan Capital Market Authority. (2025). *Digital diaspora investment platform: One-year impact assessment*. RCMA.

Salisu, A. A., & Vo, X. V. (2020). Political risk, stock returns, and volatility: Evidence from the US and Japan. *International Review of Financial Analysis, 71*, Article 101526.

Samuel Teklu. (2022). *Technological infrastructure and capital market performance in Ethiopia* [Unpublished master's thesis]. Addis Ababa University.

Saunders, M., Lewis, P., & Thornhill, A. (2019). *Research methods for business students* (8th ed.). Pearson Education.

Scott, T., & Kindness, D. (2024). *Capital markets: Institutions and instruments*. CFA Institute Research Foundation.

Securities and Exchange Commission Nigeria. (2021). *Annual report and accounts*. SEC Nigeria.

Sharpe, W. F. (1964). Capital asset prices: A theory of market equilibrium under conditions of risk. *Journal of Finance, 19*(3), 425–442.

South African Reserve Bank. (2023a). *Financial stability review 2023*. SARB.

South African Reserve Bank. (2023b). *Quarterly bulletin: Financial inclusion and market liquidity*. SARB.

Stulz, R. M. (1999). Globalization, corporate finance, and the cost of capital. *Journal of Applied Corporate Finance, 12*(3), 8–25.

Teklehaimanot, A. (2014). ICT infrastructure and financial market development in emerging economies. *African Journal of Information Systems, 6*(2), 45–62.

Tweneboah, G. (2011). Does inflation rate volatility matter for financial development? Evidence from selected African countries. *Journal of Economics and Sustainable Development, 2*(1), 1–10.

U.S. Department of State. (2024). *2024 Investment climate statements: Egypt*. U.S. Department of State.

U.S. Department of State. (2025). *2025 Ethiopia Investment Climate Statement*. U.S. Department of State.

United Nations Economic Commission for Africa. (2023). *Regional integration and financial development in Africa*. UNECA.

World Bank. (2022). *Ethiopia: Capital market development and regulation* (Report No. 178245-ET). World Bank.

World Bank. (2023). *Ethiopia economic update: Tackling inflation and stabilizing the macroeconomy* (Report No. 182367-ET). World Bank.

World Bank. (2024). *Global financial development report 2024: Capital markets in low-income countries*. World Bank.

World Bank. (2025a). *Ethiopia climate and development report*. World Bank.

World Bank. (2025b). *Ethiopia economic update: Mobilizing diaspora capital*. World Bank.

World Bank. (2025c). *Ethiopia financial inclusion and literacy survey 2025*. World Bank.

Yamane, T. (1967). *Statistics: An introductory analysis* (2nd ed.). Harper & Row.

Yartey, C. A., & Adjasi, C. K. (2007). *Stock market development in Sub-Saharan Africa: Key issues and overview* (IMF Working Paper No. 07/209). IMF.

Yin, R. K. (2018). *Case study research and applications: Design and methods* (6th ed.). SAGE Publications.

Appendix I: Questionnaire

COLLEGE OF BUSINESS AND ECONOMICS

DEPARTMENT OF MANAGEMENT

POST-LAUNCH CHALLENGES AND EMERGING PROSPECTS IN ETHIOPIA'S CAPITAL MARKETS

Dear Respondent,

This study adopts a qualitatively dominant mixed methods approach. Qualitative data from interviews and focus group discussions (FGDs) are the primary source of findings; this questionnaire provides supplementary descriptive context. The study examines post launch challenges and emerging prospects of Ethiopia's capital markets, with a focus on the Ethiopian Securities Exchange (ESX). Your responses will be analyzed using descriptive statistics (frequencies, percentages, means) to support and contextualize qualitative findings.

My name is Meron Birhanu, and I am conducting this research as part of the requirements for the Master of IB at Addis Ababa University.

Objective: To gather information on post launch challenges and emerging prospects of Ethiopia's capital markets, focusing on the ESX. Your perspective as a stakeholder in Ethiopia's financial environment is crucial for understanding the current dynamics of this nascent market.

Confidentiality: All information you provide will be kept strictly confidential and used solely for academic purposes. Aggregated findings may contribute to insights relevant to the ongoing development and regulation of Ethiopia's capital market.

Structure:

- **Part One:** Background information
- **Part Two:** Perceptions of the post launch capital market environment

Thank you in advance for your thoughtful and honest responses.

Part One: Background Information

Instruction: Please tick (✓) the box that corresponds to your response.

1. Age:

   □ 21–29 □ 30–39 □ 40–49 □ 50 years and above

2. Gender:

   □ Male □ Female

3. Highest education level:

   □ Diploma □ Bachelor's degree □ Master's degree or above

4. Current work position:

   □ Junior level □ Senior level □ Managerial/Head/Director □ Other (please specify):_____

5. Relevant work experience in finance, economics, or related fields:

   □ Less than 4 years □ 4–8 years □ 9–12 years □ More than 13 years

Part Two: Perceptions of Ethiopia's Post Launch Capital Market Environment

Directions: The statements below relate to the current situation of Ethiopia's capital market (ESX) and its operating environment. Indicate the extent to which you agree or disagree by ticking (✓) the appropriate box.

Scale:

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

Statement	1	2	3	4	5
A. Regulatory Environment & Governance					
Q1. The current regulatory framework under the Ethiopian Capital Market Authority (ECMA) is clear and effective for market operations.					
Q2. ECMA's enforcement capacity is sufficient to ensure market integrity and investor protection.					
Q3. Existing accounting, auditing, and financial reporting standards in Ethiopia are adequate for listed companies on the ESX.					
Q4. Current regulations sufficiently protect the rights of minority shareholders in listed companies.					
Q5. There is sufficient regulatory guidance for institutional investors (e.g., pension funds) wishing to participate in the ESX.					
B. Market Operations & Infrastructure					

Q6. The ESX's trading platform and technology infrastructure are efficient and reliable.					
Q7. Clearing and settlement processes for ESX transactions are timely and dependable.					
Q8. Market liquidity (the ability to easily buy/sell securities) on the ESX is currently adequate.					
Q9. Access to reliable market information and data about ESX activities is readily available to investors.					
C. Market Participants & Capacity					
Q10. There is a sufficient pipeline of Ethiopian companies ready and willing to list on the ESX.					
Q11. Ethiopian institutional investors (e.g., pension funds, insurance firms) have the necessary expertise to invest effectively in the ESX.					
Q12. There is adequate capacity and expertise among market intermediaries (brokers, dealers, analysts) operating in Ethiopia.					
Q13. Retail investor awareness and understanding of capital market investment in Ethiopia are currently high.					
Q14. Investor confidence in the fairness and potential profitability of the ESX is currently strong.					
D. Macroeconomic & External Environment					
Q15. Current macroeconomic conditions (e.g., inflation, exchange rate, FX availability) in Ethiopia are conducive to capital market development.					
Q16. Government economic policies are generally supportive of the ESX's growth and stability.					
Q17. Political stability in Ethiopia positively influences investor confidence in the ESX.					
Q18. Global economic conditions currently present more opportunities than challenges for the ESX.					
E. Prospects & Opportunities					
Q19. Listing state owned enterprises (SOEs) presents a major growth opportunity for the ESX.					
Q20. Integrating financial technology (FinTech) solutions can significantly enhance the ESX's efficiency and reach.					
Q21. The ESX has strong potential to attract significant foreign portfolio investment.					
Q22. The ESX has strong potential to mobilize domestic savings (including from the diaspora).					
Q23. The ESX offers a competitive and attractive alternative investment compared to existing options (e.g., bank deposits, real estate).					

Thank you for your participation.

Appendix II: Interview Guide

1. Overall Assessment

1.1. Could you describe your overall assessment of the Ethiopian Securities Exchange's (ESX) functioning and performance since it became operational?

1.2. From your perspective, what have been the most notable successes or positive developments so far?

2. Regulatory Environment (Post Launch Focus)

2.1. How effective do you find the current regulatory framework under the Ethiopian Capital Market Authority (ECMA) in governing the market's operations post launch?

2.2. What specific aspects of the regulations (or their enforcement) are working well, and where do you see gaps or challenges hindering market development?

3. Operational Functioning & Infrastructure

3.1. What are the key operational challenges the ESX and its participants (brokers, institutional investors, and individual investors) are currently facing?

Probes: trading systems, liquidity, clearing and settlement, market data availability, trading hours, transaction costs.

3.2. To what extent is market liquidity a concern, and what factors are contributing to the current liquidity levels?

4. Market Participants – Capacity & Engagement

4.1. **Issuers:** What challenges are potential issuers (companies looking to list shares or bonds) facing in accessing the ESX? What might encourage more listings?

4.2. **Investors:** How would you characterize the current level of investor awareness, confidence, and participation (both retail and institutional)? What are the main barriers?

4.3. **Intermediaries:** What is the current capacity and readiness of market intermediaries (brokers, dealers, analysts, custodians) to support a vibrant market? What kind of support, training, or regulatory clarity do they need?

5. Macroeconomic & External Context

5.1. How are current macroeconomic conditions in Ethiopia (e.g., inflation, foreign exchange availability, GDP growth, interest rates) impacting the ESX's development and attractiveness to investors?

5.2. To what extent does the broader political and social environment influence investor confidence and activity in the capital market?

6. Consolidated Challenges

6.1. Considering everything we have discussed, what do you view as the three most significant challenges currently hindering the sustainable growth and effectiveness of the Ethiopian capital market?

7. Emerging Prospects & Opportunities

7.1. Looking ahead, what do you see as the most promising opportunities or potential growth drivers for the ESX?

Probes: SOE privatization, FinTech integration, diaspora investment, new product development (e.g., bonds, derivatives), listing of specific sectors such as utilities, telecom, or financial institutions.

7.2. How can these emerging prospects be effectively leveraged or translated into concrete policy and market practice?

8. Way Forward & Recommendations

8.1. Based on your experience and perspective, what key actions or policy adjustments are most critical in the near term to overcome the challenges and realize the potential of the ESX?

8.2. Is there anything else you feel is important regarding the post launch challenges or prospects of Ethiopia's capital market that we have not covered in this discussion?

Thank you for your time and insights.