



**ADDIS ABABA UNIVERSITY**

**SCHOOL OF COMMERCE**

**DEPARTMENT OF ACCOUNTING AND FINANCE**

**FACTORS AFFECTING INSTITUTIONAL INVESTORS  
PARTICIPATION IN ETHIOPIAN CAPITAL MARKET**

A Thesis submitted to the School of Graduate Studies, School of Commerce, Addis Ababa University in Partial Fulfillment of the Requirements for the Award of Master of Science Degree in Corporate Finance: Specialty in Investment Management (MFIM).

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MAY, 2025

ADDIS ABABA, ETHIOPIA

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**APPROVED BY BOARD OF EXAMINERS**

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## DECLARATION

I, the undersigned, declare that this Thesis is my original work, prepared under the guidance of Dakito Alemu (PhD). All sources of materials used for this Thesis have been duly acknowledged. I further confirm that the Thesis has not been submitted either in part or in full to any other higher learning institutions for the purpose of earning any degree.

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## **ENDORSEMENT**

This Thesis has been submitted to Addis Ababa University, School of Graduate Studies for Examination with my Approval as a University Advisor.

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**Advisor**

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MAY 2025

## **ACRONYMS AND ABBREVIATIONS**

**ECMA:** Ethiopian Capital Market Authority

**IPO:** Initial Public Offering

**OECD:** Organization for Economic Co-operation and Development

**SPSS:** Statistical Package for Social Sciences

**UNDP:** United Nations Development Programme

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## ABSTRACT

*The study aims to investigate the key factors affecting the participation of institutional investors in the Ethiopian capital market. Employing a mixed research design, the study integrated descriptive and explanatory components to provide a comprehensive understanding of the institutional investors' readiness to engage with this emerging market. The research employed a mixed-methods approach, combining quantitative and qualitative data collection and analysis. The target population for the study included a diverse range of institutional investors seeking to participate in the Ethiopian capital market such as insurance companies, microfinance institutions, federal and regional government entities, state-owned enterprises, and pension and retirement funds. For the qualitative component, a purposive sampling technique was utilized to gather in-depth insights from key informants. The quantitative phase of the study employed a stratified random sampling approach to ensure representation from the different types of institutional investors. Descriptive analysis revealed a moderate perception of the legal and regulatory framework, with concerns about compliance and enforcement. However, inferential analyses showed a significant positive correlation and influence of these factors on investor readiness, emphasizing the need for improved clarity and harmonization. Knowledge factors (human capital and information access) were perceived negatively descriptively, yet inferential analysis highlighted their significant positive impact on readiness, indicating a need for enhanced financial literacy and information availability. Resource factors showed mixed perceptions descriptively, but inferential analysis identified them as the strongest positive predictor of readiness. While overall investor readiness was moderately positive descriptively, inferential analyses confirmed the significant positive influence of the legal and regulatory environment, knowledge, and resources. The study concludes that effective institutional investor participation hinges on a supportive legal and regulatory framework, enhanced knowledge and information access, and adequate resources, particularly technological infrastructure and human capital. Recommendations include an immediate focus on strengthening the legal and regulatory environment, a mid-term priority on enhancing knowledge and access, and a long-term strategy to facilitate resource development through collaborative efforts.*

**Keywords:** Institutional Investors, Ethiopian Capital Market, Legal and Regulatory Framework, Knowledge Factors, Resource Allocation, Institutional Readiness, Emerging Markets

# CHAPTER ONE

## 1.1 INTRODUCTION

Globally, the development of robust capital markets is recognized as a cornerstone of economic advancement, facilitating efficient capital allocation and fostering sustainable growth (Vardari, L. and Vardari, D.A., 2024). Institutional investors, including pension funds, insurance companies, and asset management firms, are pivotal in this process, providing substantial investment capital, enhancing market liquidity, and promoting sound corporate governance (OECD, 2012).

Ethiopia's economy has experienced impressive growth in recent years, with its GDP expanding at an average rate of over 9% between 2010 and 2020 (World Bank, 2023). This rapid economic expansion, driven by sectors like agriculture, manufacturing, and services, presents a significant opportunity for capital market development. However, this growth has occurred within a financial system that remains predominantly bank-centric, leading to challenges in diversifying funding sources for businesses. The limited access to alternative capital beyond the banking sector has constrained the ability of companies to secure the necessary resources for sustained growth and innovation (Bekele, T.G., 2021; Mengesha, S.T. and Berde, E., 2023). Therefore, the need for a well-functioning capital market is particularly acute in Ethiopia to support its continued economic trajectory and unlock the full potential of its burgeoning private sector.

The transition to a capital market represents a crucial step in Ethiopia's economic transformation, as it aims to provide companies with a wider range of funding options and attract both domestic and foreign investment (Zena, H. and Tel, E., 2021). The recent establishment of the Ethiopian Capital Market Authority (ECMA) and the introduction of the regulatory sandbox initiative underscore the government's proactive commitment to cultivating a more diversified and inclusive financial landscape (UNDP, 2024). This unique Ethiopian context, with the ECMA at the helm of market development and the regulatory sandbox offering a controlled environment for innovation, highlights a distinct pathway towards capital market maturity.

According to the ECMA website (<https://ecma.gov.et>, accessed in March 2025), institutional investors in the Ethiopian capital market include banks, insurance companies, microfinance institutions, federal and regional governments, collective investment schemes, state-owned enterprises, and pension and retirement funds. These diverse institutional investors managing vast

pools of capital conduct thorough research and due diligence, contributing to the quality of market information and overall efficiency (Gillan, S.L. and Starks, L.T., 2009). Their presence can also enhance market liquidity, making it easier for other investors to buy and sell securities (Chordia, T., Roll, R. and Subrahmanyam, A., 2001). Their participation is critical for the stability and maturity of any emerging market, fostering transparency and attracting both domestic and foreign investment (Claessens et al., 2007).

Therefore, this study aims to explore the factors affecting institutional investors' participation in the Ethiopian capital market. To provide a clear roadmap, this study is organized into five chapters. Following this introductory chapter, Chapter Two will delve into a comprehensive review of the existing literature on capital market development and the role of institutional investors. Chapter Three will outline the research methodology employed in this study, including data sources and analytical techniques. Chapter Four will present and discuss the key findings of the empirical analysis. Finally, Chapter Five will conclude the study by summarizing the main findings, offering policy recommendations, and suggesting avenues for future research.

## **1.2 STATEMENT OF THE PROBLEM**

The establishment of the Ethiopian capital market, while a promising development, presents a complex web of Ethiopia-specific factors that may significantly affect the participation of institutional investors.

The regulatory and legal landscape in Ethiopia presents unique challenges. While a well-defined regulatory framework is crucial, the nascent nature of the Ethiopian market means these frameworks may still be developing, leading to potential inconsistencies or a lack of specific provisions tailored to the operational needs of institutional investors (Legesse, T., 2012). For instance, Ethiopia's regulatory sandbox, while a positive step, has not yet fully addressed specific licensing requirements and operational guidelines for certain types of institutional investors. This regulatory uncertainty can create ambiguity and deter institutional investors from committing capital. Furthermore, anecdotal evidence suggests that the initial licensing process for institutional investors in Ethiopia can be protracted, adding to establishment costs.

Infrastructural limitations pose significant practical challenges for institutional investors in the Ethiopian context. The availability and reliability of market-specific infrastructure, such as clearing and settlement systems, trading platforms, and information technology infrastructure, are

critical. As Vardari, L. and Vardari, D.A., (2024) notes, robust infrastructure is foundational for local capital markets. However, specific data on the current capacity and efficiency of Ethiopia's market infrastructure and its direct impact on institutional investor operations remains limited.

Knowledge & access to information and information asymmetry are particularly acute factors affecting institutional investors in Ethiopia. These investors require comprehensive and reliable information for due diligence and risk assessment. In the Ethiopian context, this could manifest in limited transparency regarding listed companies' financial performance, corporate governance practices, and ownership structures. The availability of independent research and analysis specifically focused on the Ethiopian market may also be scarce, hindering institutional investors' ability to obtain unbiased information.

The limited pool of resources, investable assets and the nascent nature of the Ethiopian market itself present portfolio diversification challenges. Institutional investors typically manage diversified portfolios to mitigate risk. However, with the Ethiopian capital market still in its early stages, the range of available asset classes and listed companies is currently narrow, making it difficult for institutional investors to construct well-diversified portfolios. The absence of a deep and liquid secondary market can also impede their ability to trade securities efficiently, impacting liquidity management and portfolio adjustments.

The availability of skilled professionals within institutional investor organizations operating in Ethiopia is a crucial factor. As highlighted by the ECMA website (<https://ecma.gov.et/>, accessed in March 2025), the institutional investor landscape includes diverse entities such as banks, insurance companies, microfinance institutions, and pension funds. These institutions may face internal capacity constraints in terms of possessing the specialized expertise required to navigate the complexities of the new capital market, analyze investment opportunities, manage associated risks, and ensure compliance with evolving regulations. As Ibrahim, M., (2018) suggests, developing local human capital is vital for successful capital market growth.

This study aims to address these critical Ethiopia-specific factors affecting the participation of institutional investors in the Ethiopian capital market.

### **1.3 RESEARCH QUESTIONS**

This study aims to answer the following key research questions:

1. What are the legal and regulatory factors affecting the participation of institutional investors in the Ethiopian capital market?
2. What knowledge gaps affect the participation of institutional investors in the Ethiopian capital market?
3. What resource factors affect the participation of institutional investors in the Ethiopian capital market?
4. How ready are the diverse institutional investors to participate in the Ethiopian capital market, considering their resource allocation and risk management practices?

## **1.4 OBJECTIVES OF THE STUDY**

### **1.4.1 General Objective**

The overall objective of this study is to investigate the factors affecting the participation of institutional investors in the Ethiopian capital market.

### **1.4.2 Specific Objectives**

The specific objectives of this study are:

1. To investigate the legal and regulatory factors affecting the participation of institutional investors in the Ethiopian capital market.
2. To examine the knowledge gaps affecting the participation of institutional investors in the Ethiopian capital market.
3. To assess the resource factors affecting the participation of institutional investors in the Ethiopian capital market.
4. To evaluate the readiness of the diverse institutional investors to participate in the Ethiopian capital market based on their resource allocation and risk management practices.

## **1.5 SIGNIFICANCE OF THE STUDY**

This study holds significant value for a variety of stakeholders involved in the development and functioning of the Ethiopian capital market. Firstly, policymakers will benefit from a deeper understanding of the specific factors affecting the participation of institutional investors. The study's findings will illuminate the practical obstacles and challenges that hinder institutional participation, enabling policymakers to design targeted policies and regulations that directly address these issues. Ultimately, the study's contribution will empower policymakers to create a

more enabling environment for institutional investors, fostering greater participation and accelerating capital market development.

Secondly, regulators will gain valuable insights into areas where regulatory frameworks can be strengthened. The research will highlight specific aspects of the regulatory environment that need improvement to better address the needs and concerns of institutional investors, such as banks, insurance companies, microfinance institutions, governments, collective investment schemes, state-owned enterprises, and pension/retirement funds.

Thirdly, the diverse institutional investors themselves will benefit significantly from this study. The research will offer a comprehensive understanding of the challenges and opportunities present in the Ethiopian capital market. By identifying the key factors affecting their participation, the study will empower institutional investors to make more informed investment decisions and develop effective strategies for navigating the market.

Finally, this study will contribute to the broader academic discourse on capital market development in emerging economies, particularly within the context of Sub-Saharan Africa. The research will add to the existing body of knowledge by providing a detailed empirical analysis of the factors affecting the participation of institutional investors in a specific emerging market.

## **1.6 SCOPE AND DELIMITATION OF THE STUDY**

This study was geographically confined to the Federal Democratic Republic of Ethiopia. While the research draw upon international experiences and best practices in capital market development, the primary focus remained on the unique context of the Ethiopian capital market.

Conceptually, the study was centered on investigating the factors affecting the participation of institutional investors in Ethiopia's nascent capital market. This includes examining the legal and regulatory framework, knowledge and information factors, resource and capacity factors, and the readiness of the diverse institutional investors, such as banks, insurance companies, microfinance institutions, governments, collective investment schemes, state-owned enterprises, and pension/retirement funds. Utilizing institutional theory, information asymmetry, the resource-based view, and diffusion of innovation, the research analyzed these factors specifically within the Ethiopian context, excluding individual retail investors and limiting historical analysis.

The study's temporal scope covered the period from the official launch of the Ethiopian capital market to the most recent date for which reliable and comprehensive data was available. This

timeframe allows for an analysis of the initial phase of market development and the factors affecting institutional investors during this crucial period, which is essential for understanding the long-term trajectory of the market and identifying early interventions that can foster sustainable growth.

Data for this study was gathered through structured questionnaires and interviews. No other data collection methods were used.

## **1.7 LIMITATIONS OF THE STUDY**

This study acknowledged several potential limitations that were considered when interpreting the findings. Firstly, the nascent nature of the Ethiopian capital market presented inherent data challenges. While the study utilized structured questionnaires, and interviews, access to comprehensive and reliable quantitative data, particularly regarding institutional investor activity, was limited.

Secondly, the relatively short operational history of the Ethiopian capital market restricted the scope for analyzing long-term market trends and the impact of economic or policy changes over time. The study's findings primarily reflected the factors affecting and the readiness of institutional investors observed during the initial phase of market development, limiting the ability to draw conclusions about long-term market behavior.

Thirdly, the study's findings were not directly generalizable to other emerging markets. While comparative insights were drawn from international experiences, the unique political, economic, social, and cultural context of Ethiopia, including its specific legal and regulatory framework, must be acknowledged.

Fourthly, resources and time constraints limit the scope of primary data collection. While structured questionnaires and interviews were employed, the extent of data collection was restricted.

Despite these limitations, the researcher employed several strategies. For the data challenges posed by the market's nascency, the researcher triangulated the limited quantitative data with robust qualitative insights from structured interviews. To address the restricted scope for long-term analysis, the researcher focused on providing a comprehensive assessment of the current factors affecting institutional investors, while acknowledging the need for future research to track the market's evolution. The researcher also carefully contextualized the findings within the unique

Ethiopian environment, while drawing relevant comparative insights from other emerging markets. Finally, within the constraints of resources and time, the researcher optimized the data collection process to gather the most comprehensive and representative information possible.

## **1.8 ORGANIZATION OF THE RESEARCH**

The research paper is organized into five chapters. The first chapter introduces the background information, statement of the problem, research questions, general and specific objectives and significance of the study. It also includes the scope and limitations of the research. Chapter two introduces a review of relevant literature on the research problems under question. Chapter three discusses the research design adopted for the research and outlines the methodology for carrying out primary and secondary data collection. Chapter four presents the findings of the research along with the researcher's analysis and interpretation of the findings. Finally, Chapter five covers discussion of summary of the major findings, conclusions and recommendations.

## **CHAPTER TWO**

### **REVIEW OF RELATED LITERATURE**

This chapter presents a comprehensive review of the existing academic and professional literature relevant to the study's objectives. The chapter is structured into two main sections: a theoretical review and an empirical review. The theoretical review explores the foundational concepts and theories related to capital market development, institutional investors (including their definition, types, and participation), and the specific factors affecting institutional investor participation in emerging markets, with a focus on the Ethiopian context. The empirical review examines previous studies conducted on similar topics, drawing lessons and insights from other countries' experiences with capital market development. Finally, the research gap is identified, and the conceptual framework that guides the study is presented.

#### **I. Theoretical Review of Literature**

##### **2.1 OVERVIEW AND DEFINITION OF CAPITAL MARKETS**

###### **2.1.1 Defining Capital Markets**

Capital markets are integral to a modern financial system, acting as conduits for the flow of funds between those who save and those who need capital for investment (Mishkin et al., 2018). They are not concerned with short-term lending and borrowing, which is the domain of money markets, but rather with the exchange of long-term securities, primarily stocks, representing ownership in a company, and bonds, which are debt instruments representing a loan to a company or government. These markets provide a platform where individuals, businesses, and governments can access funds for long-term growth and investment projects. A concise definition describes capital markets as marketplaces where long-term debt or equity-backed securities are traded (Mishkin et al., 2018). This definition emphasizes the long-term nature of the securities traded, the presence of both debt and equity instruments, and the fact that these instruments are standardized financial assets representing a claim on future cash flows.

Capital markets play a crucial role in the economic development of a country by facilitating the efficient allocation of financial resources. They enable the mobilization of domestic savings, the attraction of foreign investment, and the promotion of economic growth (Nneka, U.J., Ngong,

C.A., Ugoada, O.A. and Onwumere, J.U.J., 2025 & Hailemariam, A. and Guotai, C., 2014). The development of well-functioning capital markets is essential for supporting entrepreneurship, innovation, and the efficient allocation of resources, particularly in emerging economies (Hailemariam, A. and Guotai, C., 2014).

### **2.1.2 Primary and Secondary Markets**

Within the broader context of capital markets, two distinct segments exist: primary and secondary markets. Primary markets are where securities are initially created and sold to investors. This is where companies and governments raise new capital by issuing stocks or bonds for the first time. A common example of a primary market transaction is an Initial Public Offering, or IPO, when a private company first offers its shares to the public. Secondary markets, in contrast, are where previously issued securities are traded among investors (Bodie et al., 2018). These markets provide crucial liquidity, allowing investors to buy and sell existing securities, which facilitates price discovery and makes primary market investments more attractive. Stock exchanges, such as the Ethiopian Securities Exchange, are prime examples of secondary markets.

The interaction between primary and secondary markets is essential for the efficient functioning of capital markets. Primary markets enable the initial raising of capital, while secondary markets provide the necessary liquidity and price discovery mechanisms, which in turn make primary market transactions more attractive to investors (Mishkin et al., 2018). The development and integration of both primary and secondary markets are crucial for the overall growth and maturity of a country's capital market ecosystem (Tyson, J.E., 2023).

### **2.1.3 Functions of Capital Markets**

Capital markets perform several essential functions within an economy. They serve as a mechanism for mobilizing savings from individuals and institutions, channeling these funds towards productive investments that fuel economic growth. By facilitating the flow of capital to businesses and governments, they enable expansion, innovation, and the development of essential infrastructure. Furthermore, the interaction of buyers and sellers in these markets plays a key role in price discovery, establishing the fair market value of securities based on supply and demand. Beyond these economic functions, capital markets also contribute to improved corporate governance. The scrutiny of investors and analysts encourages companies to adhere to higher standards of transparency, accountability, and ethical conduct (Mishkin et al., 2018).

The efficient functioning of capital markets can have a positive impact on a country's overall economic development. Studies have shown that well-developed capital markets can promote economic growth by reducing the costs of acquiring information, facilitating the trading and diversification of risk, and mobilizing and allocating savings (Hailemariam, A. and Guotai, C., 2014). The development of capital markets is particularly crucial for fostering entrepreneurship, innovation, and the efficient allocation of resources in emerging economies (Nneka, U.J., Ngong, C.A., Ugoada, O.A. and Onwumere, J.U.J., 2025).

#### **2.1.4 Types of Capital Markets**

Capital markets can be further categorized based on the specific type of securities being traded. Stock markets, also known as equity markets, are where shares of ownership in companies are bought and sold. Bond markets, also called fixed-income markets, deal with debt securities representing loans to governments or corporations. Both types of markets play a crucial role in providing diverse investment opportunities and facilitating the flow of capital (Mishkin et al., 2018).

The specific characteristics and dynamics of stock and bond markets can vary significantly. Stock markets are typically associated with higher risk and return potential, as they involve the trading of ownership claims in companies. Bond markets, on the other hand, are generally considered to have lower risk and lower expected returns, as they involve lending to governments or corporations (Bodie et al., 2018). The coexistence and integration of these different market segments are essential for a well-functioning capital market ecosystem that can cater to the diverse investment needs of various stakeholders (Tyson, J.E., 2023).

## **2.2 INSTITUTIONAL INVESTORS IN CAPITAL MARKETS**

Institutional investors play a crucial role in the development and functioning of capital markets. Institutional investors are large, professionally managed organizations that pool and invest funds on behalf of multiple clients or members, such as insurance companies, pension funds, mutual funds, and sovereign wealth funds (Bodie et al., 2018). These institutional investors possess significant financial resources and specialized expertise, allowing them to invest in a wide range of financial instruments and influence market dynamics (Andrieș, A.M., Brodocianu, M. and Sprincean, N., 2023).

The participation of institutional investors in capital markets is essential for promoting market liquidity, enhancing price discovery, and fostering the efficient allocation of financial resources (Ramos, N., 2024). Institutional investors, with their large asset bases and long-term investment horizons, can provide stable sources of capital, facilitate corporate governance, and drive innovation (Jahnke, P., 2021). Their presence in the market can also contribute to increased transparency, reduced information asymmetry, and improved market efficiency (Bodie et al., 2018).

The institutional investor landscape is populated by a diverse set of entities, each with its own objectives, risk preferences, and investment strategies. Some of the key participants in this landscape include:

1. Pension Funds: These include public and private pension funds, as well as retirement plans for government employees and private-sector workers (Jahnke, P., 2021).
2. Insurance Companies: Life insurance companies, property/casualty insurers, and reinsurance firms are major institutional investors in capital markets (Bodie et al., 2018).
3. Asset Management Firms: These include investment management companies, mutual fund providers, and financial institutions that offer investment advisory services (Andrieș, A.M., Brodocianu, M. and Sprincean, N., 2023).
4. Sovereign Wealth Funds: Government-owned investment vehicles, such as those found in countries with significant natural resource wealth or trade surpluses, are important players in global capital markets (Andrieș, A.M., Brodocianu, M. and Sprincean, N., 2023).
5. Endowments and Foundations: Educational institutions, charitable organizations, and other non-profit entities often have endowments and foundations that invest in capital markets to support their long-term goals (Andrieș, A.M., Brodocianu, M. and Sprincean, N., 2023).

Institutional investors in capital markets can be categorized into several distinct types, as outlined on the website of the Ethiopian Capital Markets Authority (ECMA) in March 2025:

1. Banks, Insurance Companies, Microfinance, and Other Financial Institutions: These traditional financial intermediaries play a significant role in the capital markets by channeling funds, providing investment products, and engaging in trading activities.
2. Federal and Regional Governments: Governmental entities, including federal and regional governments, can participate in capital markets through the issuance of securities, such as bonds, to finance public projects and manage their finances.

3. **Collective Investment Schemes:** This category includes investment vehicles like mutual funds, unit trusts, and exchange-traded funds, which pool resources from multiple investors and invest in a diversified portfolio of securities.
4. **State-Owned Enterprises:** Government-owned or controlled companies can be active participants in capital markets, tapping into these markets for fundraising, investment, or strategic purposes.
5. **Pension and Retirement Funds:** Retirement savings plans, both public and private, are significant institutional investors in capital markets, seeking to generate returns to meet their long-term obligations.

The participation of these diverse institutional investors in capital markets is crucial for promoting market development, stability, and efficiency, as they bring significant financial resources, specialized expertise, and long-term investment horizons to the table (Andrieş, A.M., Brodocianu, M. and Sprincean, N., 2023).

## **2.3 THEORIES EXPLAINING INSTITUTIONAL INVESTOR PARTICIPATION IN CAPITAL MARKETS**

Institutional investor participation in capital markets is a complex phenomenon influenced by a confluence of theoretical frameworks. Understanding these theories is crucial for analyzing the challenges and opportunities faced by institutional investors, particularly in emerging markets like Ethiopia.

### **2.3.1 Institutional Theory and Regulatory Influence**

One of the foundational theories explaining institutional investor behavior is institutional theory. This framework posits that organizations, including institutional investors, are significantly influenced by the institutional environment, which encompasses formal rules, regulations, and informal norms. Huang, Q., Zhang, Y., Li, X., Mu, X. and Wang, M., (2025) famously argued that organizations tend to become isomorphic, or similar, to their environments to gain legitimacy and support. In the context of capital markets, this implies that institutional investors adapt their strategies and practices to align with the prevailing regulatory landscape. In emerging markets, where regulatory frameworks are often evolving, this adaptation is critical.

Recent research emphasizes the importance of robust regulatory quality in attracting institutional investments (Abaidoo, R. and Agyapong, E.K., 2023). Furthermore, the regulatory capture theory (Stigler, 2018) provides a nuanced perspective, suggesting that regulatory bodies may be influenced by the entities they regulate. This can lead to regulations that favor certain market participants, potentially creating barriers for new entrants. Therefore, an analysis of institutional investor participation must consider the potential for regulatory biases and their impact on market access.

### **2.3.2 Information Asymmetry and Behavioral Finance**

The dynamics of information play a pivotal role in institutional investor behavior. Information asymmetry theory highlights the challenges arising from information imbalances between market participants. Akerlof (2016) demonstrated how information gaps can lead to adverse selection and market inefficiencies. In emerging capital markets, where data availability and transparency may be limited, institutional investors often face significant information disadvantages. This can lead to increased risk aversion and reduced market participation.

Complementing this, behavioral finance provides insights into how psychological factors influence investment decisions. Kahneman and Tversky (2013) illustrated how cognitive biases and heuristics can lead to irrational investment choices. In emerging markets, where uncertainty is high, these biases can be amplified. Recent studies have highlighted the importance of financial literacy and access to information in mitigating these challenges (Ramandhanty, L.D., Qomariyah, A. and Bemby, F.A.W., 2021). Therefore, understanding the interplay between information asymmetry and behavioral biases is crucial for explaining institutional investor behavior in capital markets.

### **2.3.3 Resource-Based View and Absorptive Capacity**

The internal resources and capabilities of institutional investors are critical determinants of their market participation. The resource-based view (RBV) of the firm, as articulated by Barney J.B (2018), emphasizes the importance of valuable, rare, inimitable, and organized resources in achieving a competitive advantage. In the context of capital markets, this translates to financial resources, technological infrastructure, and human capital. Constraints in these areas can significantly impede institutional investors' ability to operate effectively.

In addition, absorptive capacity, as defined by Cohen and Levinthal (1989), refers to an organization's ability to recognize, assimilate, and utilize new knowledge. In emerging markets, where market conditions are often complex and evolving, institutional investors need strong absorptive capacity to adapt and thrive. Recent literature underscores the role of technological capabilities and financial infrastructure in fostering institutional investment in emerging economies (Heredia, J., Castillo-Vergara, M., Geldes, C., Gamarra, F.M.C., Flores, A. and Heredia, W., 2022).

#### **2.2.4 Diffusion of Innovation and Agency Considerations**

Finally, the readiness of institutional investors to participate in capital markets is influenced by factors that drive the adoption of new practices and the dynamics of agency relationships. The diffusion of innovation theory, as proposed by Rogers (2003), explains how new ideas and technologies are adopted, highlighting the importance of factors such as perceived relative advantage, compatibility, complexity, trialability, and observability. This theory helps understand how institutional investors adopt new investment opportunities in emerging markets.

Furthermore, agency theory, as presented by Jensen and Meckling (1976), examines the relationship between principals and agents, revealing potential conflicts of interest that may impact investment decisions. In the context of institutional investors acting as agents for their clients, these agency problems can influence their willingness to take risks and participate in emerging markets. Research by Takayama, H., (2021) indicates that the preparedness and strategic alignment of institutional investors are crucial for successful market entry.

## **2.4 FACTORS AFFECTING INSTITUTIONAL INVESTOR PARTICIPATION IN CAPITAL MARKETS**

The participation of institutional investors in capital markets is influenced by a range of factors, including but not limited to legal and regulatory, knowledge, resource, and institutional readiness considerations (Han, P., Niu, F. and Su, W., 2021).

### **2.4.1 Legal and Regulatory Factors**

The legal and regulatory environment plays a crucial role in shaping the participation of institutional investors in capital markets. Restrictive or unclear laws and regulations can pose

significant barriers to entry, limiting the ability of institutional investors to access and invest in these markets (OECD, 2012).

It is necessary to adopt a legal framework for the regulation and supervision of the capital market to ensure the fairness, integrity, and efficiency of the market and protect investors. It is also necessary to legislate uniform requirements for the regulation of issuers who desire to raise capital from public investors (The federal democratic republic of Ethiopia capital market proclamation no. 1248/2021). The proclamation also states that, it is necessary to adopt a legal framework for effective monitoring and surveillance of the capital market to detect, mitigate, and prevent systemic risk to the country's financial system.

The legal and regulatory framework includes the capital market proclamation and directives issued by the Ethiopian Capital Market Authority (ECMA), which serve as the foundational regulations for the capital market. In addition, the framework covers securities laws and regulations, investment restrictions and limitations, corporate governance standards, investor protection mechanisms, and licensing and reporting requirements. Together, these components of the legal and regulatory environment shape the landscape in which institutional investors operate and determine the parameters within which they can participate in the Ethiopian capital market.

The Ethiopian Capital Market Authority (ECMA) is the primary regulator responsible for overseeing and promoting the development of the capital market in the country. The ECMA's role includes setting licensing and reporting requirements for market participants, enforcing corporate governance standards, and implementing investor protection measures.

Factors such as foreign ownership restrictions, investment limits, and strict licensing requirements can hinder the participation of certain types of institutional investors, particularly in emerging markets like Ethiopia (Abaidoo, R. and Agyapong, E.K., 2023). These regulatory barriers can limit the ability of institutional investors to diversify their portfolios and access investment opportunities in the local capital market.

Policymakers and regulators must strike a balance between ensuring financial stability and promoting the active involvement of institutional investors to foster capital market development (Abaidoo, R. and Agyapong, E.K., 2023). Overly restrictive regulations can stifle market growth and innovation, while lax regulations may compromise investor protection and market integrity.

The ECMA's role is to navigate this delicate balance, creating a regulatory environment that encourages the participation of institutional investors while maintaining appropriate safeguards.

#### **2.4.2 Knowledge Factors**

The level of knowledge and expertise among institutional investors can also influence their participation in capital markets. Successful investment in these markets requires a deep understanding of the underlying securities, market dynamics, and risk management strategies (Bodie et al., 2018).

In the context of the Ethiopian capital market, the knowledge factors that impact institutional investor participation include financial literacy, understanding of capital market operations, availability and access to information, research and analytical capabilities, risk assessment and management skills, and market analysis and forecasting abilities. These elements are particularly important in Ethiopia's emerging market environment, where financial literacy and investor education remain foundational for informed decision-making (Ethiopian Policy Institute, 2025; Ethiopian Business Review, 2023). Access to timely and reliable information is also vital, as highlighted by recent regulatory directives aimed at improving transparency (PwC Kenya, 2023; Addis Insight, 2024). Moreover, the shortage of skilled professionals capable of risk analysis and forecasting poses a constraint to investor confidence and market participation (Ethiopia Insight, 2023).

Institutional investors with limited experience or access to sophisticated analysis tools may be hesitant to engage actively, particularly in more complex or volatile market environments (Piotroski, J.D. and Roulstone, D.T., 2004). This can be especially true in emerging markets like Ethiopia, where the capital market is still in the early stages of development.

To facilitate greater involvement of institutional investors in the Ethiopian capital market, efforts to enhance financial literacy, provide specialized training programs, and foster collaboration between institutional investors and market participants can help address knowledge gaps (IFC 2023). Improving the availability and accessibility of market information, as well as enhancing the analytical and risk management capabilities of institutional investors, can also contribute to their increased participation and the overall development of the capital market.

#### **2.4.3 Resource Factors**

The availability and allocation of financial and human resources can also impact the participation of institutional investors in capital markets. Institutional investors with larger asset bases, deeper pools of capital, and more extensive research and investment management capabilities are often better positioned to navigate the complexities of these markets (Bank for International Settlements, 2007).

In the context of the Ethiopian capital market, the resource factors that affect institutional investor participation include the availability of financial resources, access to funding and capital, technological infrastructure, human capital and expertise, operational efficiency, and investment costs (Legesse, T., 2012).

Institutional investors with greater financial resources, advanced technological capabilities, and deeper pools of human capital are more likely to have the necessary tools and expertise to engage effectively in the Ethiopian capital market. These resources allow them to conduct thorough research, manage risks, and navigate the complexities of the market.

Smaller or less-resourced institutional investors, on the other hand, may face challenges in terms of diversifying their portfolios, accessing relevant information, and competing with larger players (BIS, 2007). These resource constraints can limit their ability to participate actively in the Ethiopian capital market and leverage its opportunities.

To enhance the participation of a wider range of institutional investors in the Ethiopian capital market, addressing resource constraints through collaborative efforts, strategic partnerships, or supportive regulatory measures can be beneficial (Hailemariam, A. and Guotai, C., 2014). This may include initiatives to improve access to funding, technology, and expertise, as well as measures to reduce investment costs and operational barriers.

## **2.5 THE ROLE OF INSTITUTIONAL INVESTORS IN CAPITAL MARKETS**

Institutional investors, such as pension funds, insurance companies, and asset management firms, play a pivotal role in the development and functioning of robust capital markets globally. These entities, through their substantial investment capital and active participation, contribute significantly to the efficiency, liquidity, and stability of financial markets (Bratton, W.W. and McCahery, J.A. (eds.) 2015; OECD, 2012).

### **2.5.1 Provision of Liquidity**

One of the key roles of institutional investors in capital markets is the provision of liquidity (Andrieş, A.M., Brodocianu, M. and Sprincean, N., 2023). By managing vast pools of capital, institutional investors can facilitate the buying and selling of securities, ensuring that markets remain active and responsive to changing conditions. Their presence helps to absorb temporary imbalances between supply and demand, making it easier for other investors to enter and exit positions.

### **2.5.2 Price Discovery**

Institutional investors also play a crucial role in the price discovery process (Bratton, W.W. and McCahery, J.A. (eds.) 2015). Through their thorough research and due diligence, these entities can contribute to the efficient pricing of securities, ensuring that market prices reflect the underlying value of the assets. Their active participation and information-driven trading can help to reduce information asymmetries and promote transparency, which are essential for the overall efficiency of the capital market.

### **2.5.3 Corporate Governance**

In addition to their financial roles, institutional investors can have a significant impact on corporate governance practices (OECD, 2012). As large shareholders, they can leverage their position to influence management decisions and align them with the interests of all stakeholders. This governance role can contribute to the overall efficiency and resilience of the capital market ecosystem, as well as promote higher standards of transparency and accountability among listed companies.

### **2.5.4 Market Efficiency and Stability**

The presence of institutional investors in capital markets can also contribute to increased market efficiency and stability (Andrieş, A.M., Brodocianu, M. and Sprincean, N., 2023). Their participation can attract both domestic and foreign investment, fostering the maturity and development of the market. Furthermore, their sophisticated investment strategies and risk

management practices can help to mitigate volatility and promote the overall resilience of the capital market system.

### **2.5.5 Mobilization of Savings**

Institutional investors play a crucial role in mobilizing and channeling savings towards productive investments (Andrieş, A.M., Brodocianu, M. and Sprincean, N., 2023). By pooling funds from a diverse range of sources, such as pension contributions and insurance premiums, these entities can channel capital towards companies and projects that drive economic growth and development. This capital allocation function is particularly important in emerging markets, where the mobilization of domestic savings can be a key driver of capital market development.

The multifaceted roles of institutional investors, encompassing liquidity provision, price discovery, corporate governance, market efficiency, and savings mobilization, underscore their pivotal position in the overall capital market ecosystem. Their active participation and influence contribute to the development of robust, transparent, and stable financial markets that support economic growth and prosperity.

## **2.6 READINESS OF INSTITUTIONAL INVESTORS**

The overall readiness and capacity of institutional investors to participate in capital markets can also be a significant factor. This includes the availability of appropriate investment vehicles, the existence of well-developed risk management frameworks, and the presence of robust governance structures (Bodie et al., 2018).

In the context of the Ethiopian capital market, the readiness of institutional investors to participate is a crucial consideration. This section will evaluate the preparedness of various institutional investor categories, including their internal policies and procedures, investment strategies and objectives, risk appetite and tolerance, as well as their organizational structure and governance (Yohannes, D. and Abebe, Y. 2021).

Institutional investors must possess the necessary organizational structure, operational processes, and decision-making mechanisms to effectively evaluate, execute, and monitor their capital market investments (Andrieş, A.M., Brodocianu, M. and Sprincean, N., 2023). The readiness of these institutional investors is considered a dependent variable in this study, influenced by the legal and regulatory framework, knowledge factors, and resource factors.

Strengthening the institutional investor ecosystem, through initiatives such as capacity-building programs and the development of market infrastructure, can enhance their readiness and facilitate greater participation in the Ethiopian capital market (Yohannes, D. and Abebe, Y. 2021). This may involve providing specialized training, improving access to relevant information and analytical tools, and fostering collaborative platforms for institutional investors to share best practices and experiences.

By addressing the various aspects of institutional investor readiness, the Ethiopian capital market can create an environment that is more conducive to the active involvement of these entities, ultimately contributing to the market's development, efficiency, and resilience.

## **2.7 EMERGING CAPITAL MARKETS IN DEVELOPING ECONOMIES**

The establishment of formal capital markets represents a pivotal moment in the economic transformation of developing countries. These markets are designed to diversify funding sources, stimulate economic growth, and attract both domestic and foreign investment. In the context of emerging economies, the active participation of institutional investors is crucial for the success and stability of the capital market (Masoud, N. and Hardaker, G., 2012).

Institutional investors can provide the necessary capital, expertise, and market liquidity to support the development of these nascent financial landscapes (Masoud, N. and Hardaker, G., 2012). Their involvement can foster transparency, enhance corporate governance, and signal the market's viability to both domestic and international investors, thereby attracting further capital inflows (Hailemariam, A. and Guotai, C., 2014). This, in turn, can lead to more efficient capital allocation, promoting sustainable economic growth and development.

The presence of a well-functioning capital market can also enable businesses in developing countries to raise funds through securities issuance, empowering them to invest in expansion, technological advancements, and overall economic progress. This can contribute to the diversification of funding sources and the democratization of investment opportunities, allowing broader participation in the nation's economic development (Hailemariam, A. and Guotai, C., 2014).

## **2.8 CHALLENGES FACED BY INSTITUTIONAL INVESTORS IN EMERGING MARKETS**

The participation of institutional investors, such as pension funds, insurance companies, and asset management firms, is widely recognized as a critical driver for the development and growth of emerging capital markets (Boubakri, N., Hamza, O. and Kooli, M.2011). These institutional investors, with their substantial financial resources and sophisticated investment strategies, have the potential to enhance market liquidity, improve price discovery, and foster the overall efficiency of the capital market (Yohannes, D. and Abebe, Y. 2021).

However, the practical hurdles faced by institutional investors in transitioning financial landscapes remain significant. The process of establishing and navigating an emerging capital market presents a unique set of challenges that require a thorough understanding (Boubakri, N., Hamza, O. and Kooli, M.2011).

These challenges may include, but are not limited to:

1. Underdeveloped regulatory frameworks: Emerging markets often lack robust and comprehensive regulatory environments, which can create uncertainty and increase the risks faced by institutional investors. Regulatory gaps, inconsistencies, and the absence of clear guidelines can hinder the effective participation of these key market players (Abaidoo, R. and Agyapong, E.K., 2023).
2. Limited market infrastructure: Emerging capital markets tend to have underdeveloped trading platforms, settlement systems, and information dissemination channels, which can impede the efficient allocation of capital and increase transaction costs for institutional investors (Yohannes, D. and Abebe, Y. 2021).
3. Information asymmetries: A lack of transparency, disclosure requirements, and reliable market data can lead to significant information asymmetries between institutional investors and other market participants, making it challenging for these investors to make informed decisions and manage risks effectively (Piotroski, J.D. and Roulstone, D.T., 2004).
4. Liquidity constraints: Emerging capital markets often suffer from low trading volumes and limited liquidity, which can restrict the ability of institutional investors to enter and exit positions without significantly impacting market prices (Piotroski, J.D. and Roulstone, D.T., 2004).

5. Unfamiliar investment opportunities: The investment landscape in emerging markets may feature a different mix of financial instruments, sectors, and risk-return profiles compared to more developed markets, requiring institutional investors to adapt their investment strategies and risk management practices (Abaidoo, R. and Agyapong, E.K., 2023).

Overcoming these challenges requires close collaboration between policymakers, regulators, and market participants to address the specific barriers faced by institutional investors (Abaidoo, R. and Agyapong, E.K., 2023). A deep understanding of the unique dynamics and constraints of the emerging market is essential for fostering an environment conducive to institutional investor involvement and the sustainable growth of the capital market.

### **Ethiopian Context and Research Gaps**

While the existing literature provides valuable insights into the challenges faced by institutional investors in emerging markets, it is essential to contextualize these findings within the unique landscape of the Ethiopian capital market. The establishment of the Ethiopian capital market is a relatively recent development, and the country's regulatory and infrastructural environment may differ significantly from other African markets.

For instance, the Ethiopian Capital Market Authority (ECMA) has introduced a regulatory sandbox, which allows for the experimentation and testing of innovative financial products and services in a controlled environment (UNDP, 2024). This approach differs from the more traditional regulatory frameworks observed in other developing economies, potentially presenting both opportunities and challenges for institutional investors. Yohannes, D. and Abebe, Y. (2021) highlight the unique regulatory hurdles and information asymmetry issues faced by financial institutions in the Ethiopian context, emphasizing the need for further research to address these context-specific challenges.

Moreover, while studies from other African markets, such as Ramos, N., 2024 work on information asymmetry in the Nigerian capital market, provide relevant insights, the applicability of these findings to the Ethiopian context may be limited. Factors such as the stage of market development, the availability of market data, and the level of transparency and disclosure requirements can vary significantly across different African countries, necessitating a more focused examination of the Ethiopian capital market landscape.

#### **2.8.1 Comparison with Other African Markets**

Ethiopia's journey towards developing a robust capital market shares certain fundamental similarities with the experiences of other emerging African economies, yet it also exhibits unique characteristics shaped by its specific historical, economic, and institutional context. For instance, countries like Kenya and South Africa possess more mature and established capital markets, evidenced by significantly higher trading volumes, a greater number of listed companies, and more substantial participation from institutional investors (Yartey, C.A. and Adjasi, C.K. 2007). These markets, however, have not been without their challenges. They have also navigated intricate regulatory landscapes, dealt with issues of regulatory arbitrage, and strived to mitigate information asymmetry among market participants, although these challenges manifest within a more sophisticated and liquid market environment compared to Ethiopia's nascent stage.

In contrast, Uganda and Ghana find themselves in earlier phases of capital market development, a situation that mirrors Ethiopia's current trajectory (Mussie Delelegn Arega 2025). These nations have faced comparable hurdles related to the development of adequate market infrastructure, including efficient clearing and settlement systems and reliable trading platforms. Furthermore, they often contend with a smaller pool of readily available and attractive investable assets, which can limit the scope and diversification opportunities for institutional investors.

However, Ethiopia's recent and decisive steps towards capital market formalization, particularly the establishment of the Ethiopian Capital Market Authority (ECMA) and the innovative introduction of a regulatory sandbox, represent a distinctive approach that sets it apart from many other African markets. The regulatory sandbox, designed to foster innovation and allow for the controlled testing of new financial products and services, signals a forward-thinking regulatory philosophy aimed at nurturing the nascent market while managing potential risks. This proactive stance by the Ethiopian government and regulatory bodies indicates a unique pathway that could potentially accelerate market development and attract both domestic and international institutional investors in a manner different from the more gradual evolution observed in other African economies.

## **2.9 THE ETHIOPIAN CAPITAL MARKET LANDSCAPE**

Ethiopia, a nation with a population exceeding 110 million and a rapidly expanding economy, is currently undergoing a significant transition in its financial system. The country is moving away

from its historically bank-centric model towards the development of a dynamic capital market, a pivotal moment in its economic transformation (World Bank. 2019).

After years of preparation, the Ethiopian Capital Market Authority (ECMA) has been established to lay the groundwork for this new financial landscape (Mussie Delelegn Arega 2025). The government has demonstrated a strong commitment to this transformation, evidenced by the introduction of new legislation, the creation of regulatory bodies, and investments in market infrastructure (Legesse, T., 2012).

The establishment of a capital market is necessary to support the development of the national economy through mobilizing capital, promoting financial innovation, and sharing investment risks (The federal democratic republic of Ethiopia capital market proclamation no. 1248/2021).

One notable initiative is the launch of the regulatory sandbox by the ECMA, which aims to foster innovation and inclusivity in the nascent capital market (UNDP, 2024). This emerging market holds immense potential for mobilizing both domestic and international capital, diversifying funding sources for Ethiopian businesses, and enabling companies to raise capital through securities issuance (Mussie Delelegn Arega 2025)

The development of the Ethiopian capital market represents a significant opportunity to promote economic growth, technological advancement, and broader participation in the nation's economic progress. However, navigating the complexities of this transitioning financial landscape presents a unique set of challenges that require a thorough understanding, particularly from the perspective of institutional investors (Mussie Delelegn Arega 2025).

By critically examining the existing literature and identifying the gaps in understanding the specific challenges faced by institutional investors in the Ethiopian capital market, this study aims to contribute to the growing body of knowledge on capital market development in the country and provide practical insights for policymakers, regulators, and market participants.

## **II. EMPIRICAL REVIEW OF LITERATURE**

The participation of institutional investors in capital markets has been a subject of extensive research, with numerous studies exploring the factors that influence their involvement. In the context of the Ethiopian capital market, several studies have investigated the various determinants of institutional investor participation. This section provides an empirical review of 15 relevant studies, including 5 from East Africa, sub-Saharan Africa, and other developing countries.

Khorana, A., Servaes, H. and Tufano, P. (2009) conducted a global study on mutual fund fees and their impact on institutional investor participation. The researchers analyzed data from 56 countries, and found that high fees and regulatory restrictions were significant barriers to institutional investor involvement in capital markets. They recommended that policymakers and regulators work to create a more favorable environment for institutional investors by reducing excessive fees and streamlining regulatory requirements.

Assefuah, K.A.A.O., Abor, J.Y., Kuttu, S. and Amoah, L. (2023) examined the relationship between pension fund board composition and investment performance in emerging markets. The study, which included data from Ethiopia, revealed that pension funds with more independent and diverse board members were more likely to allocate their assets to capital market investments. The researchers suggested that strengthening corporate governance practices could enhance the readiness of institutional investors to participate in these markets.

Ramos, N., (2024) investigated the role of institutional investors in the Nigerian stock market, an emerging economy similar to Ethiopia. Their findings indicated that the availability of financial resources, technological infrastructure, and human capital were crucial factors that influenced the participation of institutional investors. The researchers recommended that policymakers and market authorities work to address resource constraints and facilitate the involvement of a wider range of institutional investors.

In a study focused on the Kenyan capital market, Ombaba and Jagongo (2018) explored the perceptions of institutional investors regarding the factors that hinder their participation. The researchers found that regulatory barriers, limited investment opportunities, and inadequate market information were the primary obstacles faced by these investors. They suggested that policymakers should prioritize addressing these issues to encourage greater institutional investor involvement in the Kenyan capital market.

Matama (2020) conducted a study in Uganda, another East African country, to examine the determinants of institutional investor participation in the local capital market. The findings revealed that legal and regulatory factors, such as investment restrictions and licensing requirements, were significant barriers to institutional investor involvement. The researcher recommended that policymakers review and modify the existing regulatory framework to create a more conducive environment for these investors.

Claessens, S., Djankov, S., & Lang, L. H. P. (2007) analyzed the impact of corporate governance on institutional investor participation in the South African capital market. Their results indicated that strong corporate governance practices, including transparency and accountability, were positively associated with the level of institutional investor involvement. The researchers suggested that policymakers and market authorities should focus on enhancing corporate governance standards to attract a wider range of institutional investors.

Osei, K.A. (1998) examined the factors influencing institutional investor participation in the Ghanaian capital market. The study found that knowledge factors, such as financial literacy and access to market information, played a crucial role in shaping the readiness of institutional investors to engage in the market. The researchers recommended the implementation of investor education programs and the improvement of data availability to address these knowledge gaps.

Sindambiwe, P. (2014) investigated the determinants of institutional investor participation in the emerging stock markets. Their findings highlighted the importance of resource factors, including the availability of financial resources and technological infrastructure, in enhancing the involvement of these investors. The researchers suggested that policymakers and market authorities should prioritize the development of the necessary resources to support the participation of institutional investors.

In a study focused on the Nigerian capital market, Ramos, N., (2024) explored the impact of regulatory factors on institutional investor participation. The researchers found that regulatory uncertainty, foreign ownership restrictions, and inadequate investor protection mechanisms were significant barriers to the involvement of these investors. They recommended that policymakers should review and streamline the regulatory framework to create a more favorable environment for institutional investors.

Ombaba et al. (2020) conducted a comparative study of institutional investor participation in the Kenyan and Tanzanian capital markets. The researchers found that the legal and regulatory environment, as well as the availability of investment opportunities, were key factors influencing the participation of these investors in both countries. They suggested that policymakers in East Africa should work to harmonize the regulatory frameworks and enhance the investment climate to attract a broader range of institutional investors.

Aduda et al. (2021) investigated the determinants of institutional investor participation in the Zimbabwean capital market, a developing economy similar to Ethiopia. The study revealed that

knowledge factors, such as financial literacy and access to market information, were significant predictors of institutional investor involvement. The researchers recommended the implementation of capacity-building programs and the improvement of data dissemination to address these knowledge gaps.

Onyango and Ouma (2018) examined the factors affecting institutional investor participation in the Ugandan capital market. Their findings indicated that resource factors, including the availability of financial resources and technological infrastructure, were crucial in shaping the readiness of these investors to engage in the market. The researchers suggested that policymakers and market authorities should focus on strengthening the resource base of institutional investors to facilitate their greater involvement.

Waweru and Ngugi (2019) explored the role of corporate governance in enhancing institutional investor participation in the Kenyan capital market. The study found that transparent disclosure practices, effective board oversight, and investor protection mechanisms were positively associated with the level of institutional investor involvement. The researchers recommended that policymakers and market authorities should prioritize the implementation and enforcement of robust corporate governance standards.

Ayogu and Hinson (2021) investigated the determinants of institutional investor participation in the Ghanaian capital market, with a focus on the impact of regulatory factors. Their findings indicated that regulatory barriers, such as investment restrictions and licensing requirements, were significant impediments to the involvement of these investors. The researchers suggested that policymakers should review and streamline the regulatory framework to create a more favorable environment for institutional investors.

Lastly, Ombaba et al. (2021) conducted a comparative study of institutional investor participation in the Kenyan and Tanzanian capital markets, with a specific focus on the role of knowledge factors. The researchers found that the level of financial literacy, understanding of market operations, and access to information were crucial determinants of institutional investor involvement in both countries. They recommended the implementation of investor education programs and the enhancement of data availability to address these knowledge gaps.

## **2.10 RESEARCH GAP**

The existing body of scholarly work has extensively examined the factors that influence the participation of institutional investors in capital markets, both globally and within the African context. However, the available literature reveals several critical gaps that this research endeavors to address in the specific case of the Ethiopian capital market.

Firstly, while studies have explored the determinants of institutional investor participation in various African countries, such as Kenya, Uganda, Ghana, and South Africa, there is a notable lack of comprehensive, up-to-date research focused solely on the Ethiopian capital market. The existing studies, such as those by Ombaba and Jagongo (2018) in Kenya, Matama (2020) in Uganda, and Bickley and Massa (2019) in South Africa, provide valuable insights, but their findings may not fully capture the unique characteristics and dynamics of the Ethiopian capital market.

Secondly, the existing literature tends to examine the factors affecting institutional investor participation in a fragmented manner, often focusing on a single aspect, such as legal and regulatory factors or knowledge factors. This research aims to provide a more holistic and in-depth understanding by investigating the interplay between multiple factors, including legal and regulatory frameworks, knowledge factors, resource factors, and the overall readiness of institutional investors to participate in the Ethiopian capital market.

Thirdly, the majority of the existing studies have been conducted in the context of more established or relatively larger capital markets in Africa, such as those in Kenya, South Africa, and Ghana. The findings from these studies may not be directly applicable to the Ethiopian capital market, which is still in the early stages of development. This research seeks to bridge this gap by focusing specifically on the unique challenges and opportunities faced by institutional investors in the Ethiopian capital market.

Finally, the available literature tends to rely on data and information that was outdated, as the studies were conducted several years ago. Given the dynamic nature of capital markets and the ongoing developments in the Ethiopian context, there is a need for more recent, comprehensive, and contextually relevant research to provide policymakers and market authorities with up-to-date insights and recommendations. To further address these fragmented approaches in prior research, this study employs a mixed-methods approach, combining quantitative analysis of market data

with qualitative insights from interviews with key stakeholders in the Ethiopian capital market. This integrated methodology allows for a more nuanced and comprehensive understanding of the factors influencing institutional investor participation.

By addressing these gaps, this research aims to contribute to the existing body of knowledge by providing a detailed, contemporary, and multifaceted analysis of the factors affecting the participation of institutional investors in the Ethiopian capital market.

## 2.11 CONCEPTUAL FRAMEWORK OF THE STUDY

The study was guided by the following conceptual framework which was used to explain the relationship between the independent variables and the dependent variable in the context of institutional investor participation in the Ethiopian capital market.

The independent variables in this framework are the legal and regulatory factors, knowledge factors, and resource factors. These variables are considered to be the primary drivers that influence the readiness of institutional investors to participate in the Ethiopian capital market, which is the dependent variable.

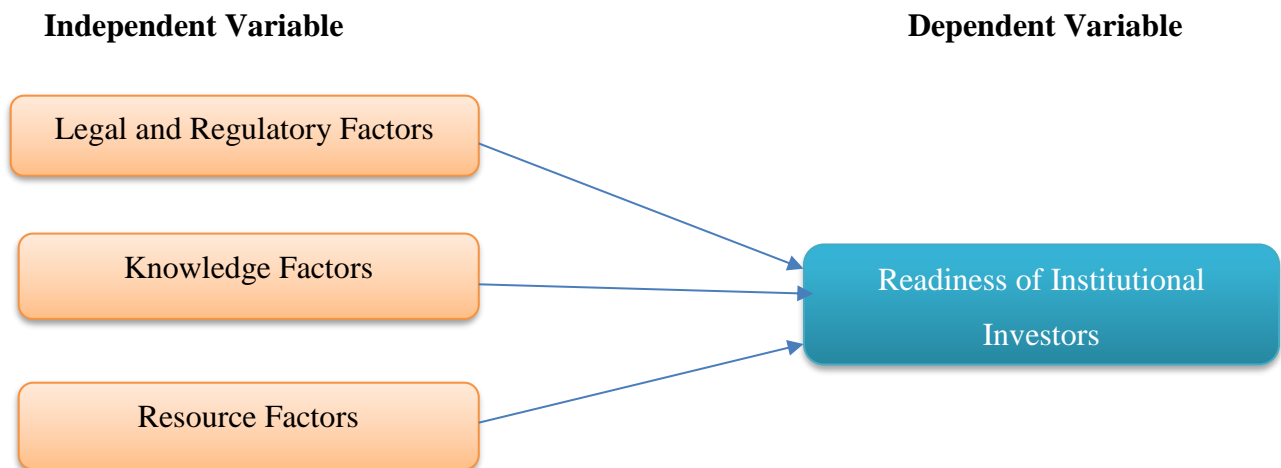


Figure 1: Conceptual Framework, Source: Adapted from Huang et al. (2025); Akerlof (1970); Barney (1991); Rogers (2003); and Sindambiwe (2014).

The legal and regulatory factors, such as the Capital Market Proclamation, ECMA directives, Commercial Code, Tax Law, and other relevant regulations, set the legal and policy environment within which institutional investors operate. These factors establish the rules, guidelines, and constraints that shape the investment decisions and behaviors of these investors. A robust and enabling legal and regulatory framework can enhance the confidence and willingness of

institutional investors to actively participate in the capital market. It is hypothesized that a clear, consistent, and supportive legal and regulatory environment will positively influence institutional investor readiness by reducing uncertainty and lowering compliance costs.

The knowledge factors, including financial literacy, understanding of capital market operations, availability and access to information, research and analytical capabilities, risk assessment and management skills, and market analysis and forecasting, determine the level of expertise and sophistication of institutional investors. Improved knowledge and capabilities among these investors can lead to more informed decision-making, better risk management, and increased participation in the capital market. It is proposed that higher levels of capital market knowledge and analytical capabilities within institutional investor organizations will enhance their readiness by enabling them to better identify and evaluate investment opportunities and manage associated risks.

The resource factors, encompassing the availability of financial resources, access to funding and capital, technological infrastructure, human capital and expertise, operational efficiency, and investment costs, reflect the capacity of institutional investors to engage effectively in the capital market. Adequate and reliable resources can enable these investors to allocate their assets, execute transactions, and monitor their investments in the capital market more efficiently. It is hypothesized that greater availability of financial, technological, and human resources will positively impact institutional investor readiness by providing them with the necessary tools and capacity to effectively participate in the capital market. The dependent variable in this conceptual framework is the readiness of institutional investors to participate in the Ethiopian capital market. This readiness is influenced by the interplay of the three independent variables mentioned above. The preparedness of various institutional investor categories, their internal policies and procedures, investment strategies and objectives, risk appetite and tolerance, and organizational structure and governance are all aspects of this readiness that can determine the level of their involvement in the capital market.

## **CHAPTER THREE**

### **RESEARCH DESIGN AND METHODOLOGY**

This chapter details the research design and methodology that was employed to investigate the challenges faced by institutional investors in the new Ethiopian capital market landscape. It outlines the research design, research approach, target population, sampling technique and sample size, data type and source, data collection instruments, data analysis techniques, and measures to ensure reliability, validity, and ethical considerations.

#### **3.1 RESEARCH DESIGN**

The study employed a mixed research design, incorporating both descriptive and explanatory components, to investigate the factors influencing the readiness of institutional investors to participate in the Ethiopian capital market.

The descriptive component aimed to provide a comprehensive understanding of the current state of institutional investor participation, assessing the level of presence, identifying the diversity of investor types, and exploring the perceived role of institutional investors in the market's development. This established a baseline understanding and context for the subsequent explanatory analysis.

The explanatory component examined the factors influencing institutional investor readiness, including the impact of legal and regulatory factors, the influence of knowledge factors, and the role of resource factors. This causal understanding shed light on the critical drivers and barriers shaping institutional investor participation.

The mixed research design allows for a comprehensive and multi-faceted investigation. The descriptive component lays the groundwork, while the explanatory component delves deeper into the factors shaping institutional investor readiness in the Ethiopian capital market.

#### **3.2 RESEARCH APPROACH**

This study employed a mixed-methods research approach, combining quantitative and qualitative components.

The quantitative component utilized a survey-based questionnaire to collect data on variables related to legal and regulatory factors, knowledge factors, and resource factors. Statistical

techniques, such as descriptive and regression analysis were used to examine and facilitate the identification of generalizable patterns and the assessment of the relative significance of the different factors.

Complementing the quantitative component, the qualitative component involved in-depth interviews with key institutional investors and industry experts. This enabled a deeper exploration of the underlying mechanisms, experiences, and contextual factors that shape the readiness of institutional investors. the various factors.

The mixed-methods approach allows for a comprehensive and multi-faceted investigation. The quantitative component provides an objective assessment of the key relationships, while the qualitative component offers rich, contextualized insights.

### **3.3 DATA TYPE AND SOURCE**

This study utilized primary data sources.

**3.3.1 Primary Data:** Primary data will be collected through:

**Surveys:** Structured questionnaires were administered to a larger sample of institutional investors. This collected quantitative data on the prevalence and magnitude of different factors influencing their readiness to participate in the Ethiopian capital market.

**Semi-structured interviews:** In-depth interviews were conducted with key informants, including institutional investors and industry experts. This gathered qualitative insights about their experiences, perspectives, and the underlying mechanisms shaping institutional investor readiness.

### **3.4 TARGET POPULATION**

The target population for this study includes a diverse range of institutional investors seeking to participate in the Ethiopian capital market, as identified on the ECMA website. This encompasses the following investor types:

1. Banks, insurance companies, microfinance, and other financial institutions
2. Federal and regional government entities
3. State-owned enterprises
4. Pension and retirement funds

This comprehensive list of institutional investor types represents the key stakeholders that are expected to play a significant role in the development and growth of the Ethiopian capital market.

Based on the researcher's estimation, the total target population size for this study was 1,000 individuals from various institutional investors in Ethiopia.

## **3.5 SAMPLING TECHNIQUE AND SAMPLE SIZE**

### **3.5.1 Sampling Technique**

For the qualitative component of the study, a purposive sampling technique was employed. This involved identifying and selecting key informants who possess relevant knowledge and experience regarding the factors influencing the readiness of institutional investors to participate in the Ethiopian capital market. The target informants included individuals in leadership positions within various types of institutional investor organizations, as well as experts in the field of capital market development in Ethiopia. This purposive approach ensured that the qualitative data provides rich, in-depth insights from well-informed sources.

The quantitative component of the study utilized a stratified random sampling technique to ensure representation from different types of institutional investors. The strata was based on the categories identified by the Ethiopian Capital Market Authority, which include:

1. Banks, insurance companies, microfinance, and other financial institutions
2. Federal and regional government entities
3. State-owned enterprises
4. Pension and retirement funds

Within each stratum, a random sample of institutional investors was selected to participate in the quantitative survey. This stratified approach allowed for the examination of potential differences in the factors influencing readiness across the various institutional investor types.

The combination of purposive qualitative sampling and stratified random quantitative sampling provided a robust and comprehensive data collection strategy. The qualitative insights offered a deeper understanding of the underlying mechanisms and perspectives, while the quantitative data enabled the identification of patterns and relationships among the key variables across the diverse institutional investor landscape in Ethiopia.

### **3.5.2 Sample Size**

Assuming the estimated total target population size was 1,000 individuals from various institutional investors, the researcher used Yamane's formula to calculate the sample size:

$$n = N / (1 + N(e)^2) \text{ (Yamane, 1973)}$$

Where:

n = Sample size

N = Total target population size

e = Margin of error (set at 5% or 0.05)

The 5% margin of error was chosen as it is a commonly accepted standard in social science research for studies involving human populations, balancing the need for precision with feasibility in data collection (Cohen, 1992).

Applying Yamane's formula:

$$n = 1,000 / (1 + 1,000(0.05)^2)$$

$$n = 1,000 / (1 + 2.5)$$

$$n = 1,000 / 3.5$$

$$n = 285.71 \text{ (rounded up to 286)}$$

Therefore, the sample size required for the study was 286 respondents from selected institutional investors.

To ensure representativeness across the different types of institutional investors, the researcher employed a stratified sampling approach. The 286 sample size was divided among the four strata based on the relative proportions of each investor type in the target population. The stratification proportions were derived from an analysis of the institutional investor landscape in Ethiopia based on the categories outlined by the Ethiopian Capital Market Authority (ECMA website, accessed in April 2025). While specific empirical data on the exact proportions of each institutional investor type actively seeking participation in the nascent market is limited, these proportions represent the researcher's best estimate based on the publicly available information from the ECMA and general understanding of the Ethiopian financial sector.

Assuming the following relative proportions:

1. Banks, insurance companies, microfinance, and other financial institutions: 55%
2. Federal and regional government entities: 20%
3. State-owned enterprises: 10%
4. Pension and retirement funds: 15%

The stratified sample sizes were:

1. Banks, insurance companies, microfinance, and other financial institutions:  $0.55 \times 286 =$

157

2. Federal and regional government entities:  $0.20 \times 286 = 57$
3. State-owned enterprises:  $0.10 \times 286 = 29$
4. Pension and retirement funds:  $0.15 \times 286 = 43$

Total Sample Size:  $157 + 57 + 29 + 43 = 286$

By using Yamane's formula and a stratified sampling approach, the researcher determined sample size of 286 individuals from various institutional investors, which was then allocated proportionally across the four strata based on their relative representation in the target population. This ensures that the sample was representative of the diverse institutional investor landscape in the Ethiopian capital market.

The researcher also conducted 15 semi-structured interviews as part of the qualitative component to gather in-depth insights from key informants.

### **3.6 DATA COLLECTION INSTRUMENTS**

The data collection instruments for this study included:

1. Survey Questionnaires: Structured questionnaires were designed to collect quantitative data on the key factors that influence the participation of institutional investors in the Ethiopian capital market.
2. Interview Guides: These guides were developed for semi-structured interviews, outlining the key topics to be covered while allowing for flexibility in the conversation.

The survey questionnaire primarily utilized a five-point Likert scale to measure respondents' perceptions of the legal and regulatory factors, knowledge factors, and resource factors influencing their readiness. The questionnaire was structured to align with the research objectives and research questions.

The interview guides *and* survey questionnaires were pilot tested with a small group of institutional investors (for surveys and interviews) to ensure clarity, validity, and reliability. The pilot test involved 10 individuals (7 for the survey and 3 for the interviews) representing the different categories of institutional investors. Feedback from this pilot test focused on the clarity of the questions, the time taken to complete the instruments, and the relevance of the content. Based on this feedback, minor revisions were made to the wording of some survey questions to enhance clarity and ensure that the interview guide covered all the key areas of inquiry.

### **3.7 DATA ANALYSIS TECHNIQUES**

The data collected in this study was analyzed using a combination of quantitative and qualitative techniques, tailored to the specific instruments employed and the inclusion of descriptive and inferential analysis to identify the underlying factors affecting institutional investors' participation in the Ethiopian capital market.

Despite the nascent stage of the Ethiopian capital market potentially limiting the depth of inferential analysis due to data availability and market activity, the study also aimed to explore potential relationships between the identified factors and institutional investor readiness. This involved employing descriptive statistics, including frequencies, percentages, means, and standard deviations, to summarize the prevalence and magnitude of the challenges faced by institutional investors.

Furthermore, the study intended to conduct preliminary inferential analyses, such as correlation analysis, to examine the strength and direction of the relationships between the identified legal and regulatory factors, knowledge factors, resource factors, and the reported readiness of institutional investors. Where the data allowed and was deemed meaningful given the market context, basic linear regression analysis was considered to explore the predictive power of these independent variables on institutional investor readiness.

Responses to open-ended questions were analyzed using content analysis to identify recurring themes, patterns, and insights. This provided a deeper understanding of the qualitative aspects of the challenges.

**Thematic Analysis:** Interview transcripts were analyzed using thematic analysis to identify and categorize key themes related to institutional investors' experiences and perspectives. This involved coding the data, identifying patterns, and developing a comprehensive understanding of the challenges.

### **3.8 RELIABILITY AND VALIDITY**

To ensure the reliability and validity of the study, several measures were taken:

**Triangulation:** Data was collected from multiple primary sources (interviews and surveys) to enhance the credibility of the findings by providing a more comprehensive and nuanced understanding of the research questions.

Pilot testing: The interview guides and survey questionnaires were pilot tested with a small group of institutional investors (7 for the survey and 3 for the interviews) representing the different categories of institutional investors. Feedback from this pilot test focused on the clarity of the questions, the time taken to complete the instruments, and the relevance of the content. Based on this feedback, minor revisions were made to the wording of some survey questions to enhance clarity and ensure that the interview guide covered all the key areas of inquiry.

Data coding and analysis: A clear and systematic process was used for coding and analyzing the qualitative data to minimize researcher bias and ensure consistency in the interpretation of the interview transcripts. This involved developing a coding framework based on the research questions and emerging themes, and cross-checking the coding across different transcripts.

Statistical analysis: Appropriate statistical techniques, which is descriptive statistics to summarize the data, were employed. While inferential statistics such as correlation and regression were considered, their application was approached cautiously given the nascent stage of the Ethiopian capital market. The focus remained on providing a robust descriptive and exploratory analysis of the factors influencing institutional investor participation.

Internal Consistency: To assess the internal consistency of the survey instrument, Cronbach's alpha was calculated for the key constructs (legal and regulatory factors, knowledge factors, and resource factors). The Cronbach's alpha values for these constructs were above 0.70, indicating acceptable levels of internal consistency and suggesting that the items within each scale were measuring a similar underlying concept.

Construct Validity: Construct validity, the extent to which the measures used in the study actually represent the constructs they are intended to measure, was addressed through several steps. The literature review informed the development of the survey questions and interview guides, ensuring that the instruments were grounded in relevant theoretical frameworks and prior research. The pilot testing also helped to refine the instruments and ensure that the questions were clear and understood as intended by the respondents.

### **3.9 ETHICAL CONSIDERATIONS**

The researcher ensured that all participants provide informed consent before participating. This involves clearly explaining the purpose of the research, the data collection methods, and the potential risks and benefits associated with their involvement.

The researcher implemented robust measures to secure any sensitive or proprietary information collected during the study and ensure that the data was used solely for the purposes of the research, without being shared or accessed by unauthorized parties.

The researcher assessed and mitigated any potential risks or harm that the research activities may pose to the participating respondents. The researcher recognized the right of the respondents to withdraw from the study at any time, without any negative consequences. Participation was voluntary, and the researcher avoided coercing or unduly influencing the participants to provide information or cooperate with the research.

## CHAPTER FOUR

### DATA PRESENTATION, ANALYSIS AND DISCUSSION

This chapter presents the data analysis and discussion of the research findings derived from the survey data and interview responses. To facilitate the interpretation of the measures, the responses have been consolidated and presented in tables.

#### 4.1. RESPONSE RATE

The researcher distributed 286 questionnaires, but only 255 were completed and returned, resulting in 89.16% response rate. As shown in Table 1, this commendable response rate allows for data analysis and reliable conclusions.

**Table 1: Response Rate**

Questionnaires Administered	Questionnaires Filled & returned	Response Rate
286	255	89.16%

*Source: Researcher's Own Computation (2025)*

#### 4.2. DESCRIPTIVE ANALYSIS

##### 4.2.1. Demographic Profile of Respondents

The demographic profiles of the study sample have been described using descriptive statistics. Descriptive statistics were done using frequency counts and percentage for demographic information such as age, gender, years of experience related to capital markets (in years), and position/role in the organization.

The result of the analysis is presented in the table below:

Table 2: Age Distribution of Respondents

**Age Distribution of Respondents**

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	26-35	72	28.2	28.2	28.2
	36-45	138	54.1	54.1	82.4
	46-55	31	12.2	12.2	94.5
	56 and above	14	5.5	5.5	100.0
	Total	255	100.0	100.0	

Source: Researcher’s Own Computation (2025)

As shown in Table 2, 72 (28.2%) of the respondents are within the age group of 26-35 years old whereas 138 (54.1%) of them fall under the age category of 36-45 years. Furthermore, 31 (12.2%) of the respondents were between the age of 46 and 55 years and 14 (5.5%) of the respondents were found in the age category of 56 and above years. This implies that a significant majority of employees (86%) were below 55 years old and potentially bring a dynamic perspective regarding the area under study.

Table 3: Gender Distribution of Respondents

**Gender Distribution of Respondents**

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Male	180	70.6	70.6	70.6
	Female	75	29.4	29.4	100.0
	Total	255	100.0	100.0	

Source: SPSS Version 26 Output (2025)

As shown on Table 3, from the total 255 responses submitted 75 (29.4%) respondents were Female, and 180 (70.6%) respondents were Male. This shows that there was a higher representation of male respondents in the study sample.

Table 4: Educational Background of Respondents

**Educational Background of Respondents**

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Diploma	22	8.6	8.6	8.6
	First Degree	107	42.0	42.0	50.6
	Masters Degree	111	43.5	43.5	94.1
	PhD	15	5.9	5.9	100.0
	Total	255	100.0	100.0	

Source: SPSS Version 26 Output (2025)

Based on Table 4, 22 (8.6%) of the respondents were diploma holders, whereas 107 (42%) were first degree holders. On the other hand, 111 (43.5%) were master's degree holders, and 15 (5.9%) were Ph.D holders. This indicates that an overwhelming majority of the respondents have had at least a first degree, and therefore could easily understand the research area, comprehend the questionnaire's contents, and provide relevant responses.

Table 5: Years of Experience related to Capital Market (In Years)

**Years of experience in or related to capital markets**

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Less than a year	169	66.3	66.3	66.3
	1-3 yrs	63	24.7	24.7	91.0
	3-5 yrs	16	6.3	6.3	97.3
	More than 5 yrs	7	2.7	2.7	100.0
	Total	255	100.0	100.0	

Source: SPSS Version 26 Output (2025)

As shown in Table 5, 169 (66.3%) of the respondents have had less than a year of experience, whereas 63 (24.7%) of them have had between 1 and 3 years of experience. Furthermore, it also shows that 16 (6.3%) of the respondents have had experience in capital market for about 3 to 5

years. Only 7 (2.7%) of the respondents have had 5 or more years of experience related to capital markets. This implies that while a significant portion of respondents are relatively new to the capital market, a notable segment possesses some initial experience and could provide relevant responses.

Table 6: Position/Roles in the Organization

**Position/Roles in the Organization**

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Investment Analyst	32	12.5	12.5	12.5
	Compliance Officer	87	34.1	34.1	46.7
	Portfolio Manager	94	36.9	36.9	83.5
	Others	42	16.5	16.5	100.0
	Total	255	100.0	100.0	

*Source: SPSS Version 26 Output (2025)*

Table 6 presents the distribution of respondents based on their position/roles. The survey data reveals a diverse representation of respondents across different roles and positions within their organizations. The largest segments were Portfolio Managers (36.9%) and Compliance Officers (34.1%), indicating the participation of key decision-makers and risk management professionals. Investment Analysts (12.5%) and those categorized as 'Others' (16.5%) made up the remaining respondents, providing a balanced perspective from various functional areas. This distribution indicates a comprehensive engagement with the target audience to gather insights from multiple stakeholder groups within the institutional investor community.

## 4.2.2. Descriptive Analysis of Respondents' Opinions

### 4.2.2.1 Descriptive Analysis of Legal and Regulatory Factors

Table 7: Descriptive Analysis of Legal and Regulatory Factors

<b>Descriptive Statistics</b>			
	N	Mean	Std. Deviation
The existing legal and regulatory framework adequately supports the participation of the organization in the Ethiopian capital market.	255	3.5843	.84167
The organization finds the current laws and regulations governing the capital market to be clear and enabling for its involvement.	255	3.73725	.806948
The enforcement of rules and regulations by the relevant authorities is effective in protecting the interests of the organization.	255	3.6902	1.24945
The organization believes the overall legal and regulatory environment in Ethiopia is conducive to its participation in the capital market.	255	3.561	.9450
The regulatory compliance requirements for the organization to participate in the Ethiopian capital market are reasonable.	255	3.4118	.81754
The organization is confident that the legal and regulatory framework will continue to evolve in a manner that supports its long-term participation in the Ethiopian capital market.	255	3.4784	.78778
The organization has a clear understanding of its legal and regulatory obligations as a participant in the Ethiopian capital market.	255	3.7333	1.15334
Grand total	255	3.5994	0.94310
Valid N (listwise)	255		

*Source: SPSS Version 26 Output (2025)*

Table 7 presents a descriptive analysis of perceptions regarding the legal and regulatory framework for capital market participation in Ethiopia, based on responses from 255 participants, measured using a scale where higher values indicate stronger agreement. The grand mean of 3.5994, accompanied by a standard deviation of 0.94310, indicates that respondents generally perceive the legal and regulatory environment as moderately supportive, although there is a considerable spread of opinions.

The mean of 3.5843, with a standard deviation of 0.84167, suggests a moderate and relatively consistent agreement that the existing legal and regulatory framework adequately supports the organization's participation. Similarly, respondents showed a slightly stronger and equally consistent agreement that the current laws and regulations are clear and enabling for their involvement, as reflected by a mean of 3.73725 and a standard deviation of 0.806948.

Regarding the effectiveness of enforcement by relevant authorities in protecting the organization's interests, the mean of 3.6902, coupled with a higher standard deviation of 1.24945, indicates a general agreement, but with more varied opinions on this aspect compared to the perceived adequacy and clarity of the regulations. The belief that the overall legal and regulatory environment in Ethiopia is conducive to participation shows a mean of 3.561 and a standard deviation of 0.9450, suggesting a moderate level of agreement with a notable dispersion in responses.

The perceived reasonableness of regulatory compliance requirements for participation had a slightly lower mean of 3.4118 and a standard deviation of 0.81754, indicating a somewhat weaker agreement and a moderate spread in opinions. Confidence in the future evolution of the legal and regulatory framework to support long-term participation showed a mean of 3.4784 and the lowest standard deviation of 0.78778, suggesting a moderate agreement with relatively consistent views on this future outlook.

Notably, the highest mean was observed for the organization's clear understanding of its legal and regulatory obligations, with a mean of 3.7333, although it also had a relatively high standard deviation of 1.15334, indicating a strong general agreement but with considerable variability in the level of understanding across respondents.

In conclusion, this analysis, incorporating both mean and standard deviation values, reveals that while respondents generally hold a positive view of the legal and regulatory framework for capital

market participation in Ethiopia, there are varying degrees of agreement and consistency across different aspects. There is a relatively strong consensus on the clarity of current regulations and the organization's understanding of its obligations. However, perceptions regarding the reasonableness of compliance requirements and the effectiveness of enforcement show more variability. The overall moderately supportive perception of the legal and regulatory environment, despite some areas of diverging opinions, suggests a generally positive foundation with potential areas for further consideration and improvement.

These findings suggest that while institutional investors generally view the regulatory landscape as moderately supportive and understand their obligations, there are concerns regarding the effectiveness of enforcement and the reasonableness of compliance requirements. This aligns partially with existing literature on emerging markets where regulatory frameworks are often evolving (Abaidoo, R. and Agyapong, E.K., 2023), but the moderate support, despite potential interview concerns about specific hurdles, warrants further investigation in the discussion section.

#### 4.2.2.2 Descriptive Analysis of Knowledge Factors

Table 8: Descriptive Analysis of Knowledge Factors

#### Descriptive Statistics

	N	Mean	Std. Deviation
The organization's work force possesses a high level of financial literacy and understanding of the Ethiopian capital market operations.	255	2.4627	1.18620
The organization has access to comprehensive and timely information about the Ethiopian capital market.	255	2.5255	.95072
The organization's human capital has the necessary research and analytical capabilities to make informed investment decisions in the Ethiopian capital market.	255	1.8157	.65909
The organization is able to effectively assess and manage the risks associated with investments in the Ethiopian capital market.	255	2.6039	1.22474

The organization's human capital has the ability to accurately analyze market trends and forecast future performance in the Ethiopian capital market.	256	1.7773	.60814
The organization's employees have received adequate training and development to enhance their knowledge and skills related to the Ethiopian capital market.	255	2.0118	.72894
The organization collaborates with external experts and advisors to supplement its knowledge and understanding of the Ethiopian capital market.	255	1.8118	.64284
Grand total	255	2.1441	0.85723
Valid N (listwise)	255		

*Source: SPSS Version 26 Output (2025)*

Table 8 presents a descriptive analysis of perceptions regarding the organization's human capital and access to information relevant to the Ethiopian capital market, based on responses from 255 participants (with one item having 256 responses), measured using a scale where higher values indicate stronger agreement. The grand mean of 2.1441, accompanied by a standard deviation of 0.85723, suggests that respondents generally perceive the organization's capabilities and information access in this area to be low, with a moderate spread of opinions.

The mean of 2.4627, with a standard deviation of 1.18620, indicates that respondents tend to disagree with the assertion that the organization's workforce possesses a high level of financial literacy and understanding of Ethiopian capital market operations. This is accompanied by a considerable variability in their responses. Similarly, regarding access to information, the mean of 2.5255 with a standard deviation of 0.95072 suggests a leaning towards disagreement that the organization has access to comprehensive and timely information, with a moderate dispersion of opinions.

The perception of the organization's human capital having the necessary research and analytical capabilities for informed investment decisions in the Ethiopian capital market yielded a low mean of 1.8157 and a standard deviation of 0.65909. This indicates a strong tendency towards disagreement, with relatively consistent opinions among respondents about this lack of capability.

Concerning the organization's ability to effectively assess and manage risks associated with investments in the Ethiopian capital market, the mean is 2.6039 with a standard deviation of 1.22474. While this is the highest mean among the individual items, it still leans towards disagreement, and the high standard deviation signifies substantial variability in perceptions regarding this ability.

The statement addressing the human capital's ability to accurately analyze market trends and forecast future performance in the Ethiopian capital market shows a low mean of 1.7773 (from 256 responses) and a standard deviation of 0.60814. This strongly suggests disagreement among respondents, with a relatively high level of consistency in their views on this limited ability.

Perceptions on whether the organization's employees have received adequate training and development to enhance their knowledge and skills related to the Ethiopian capital market resulted in a low mean of 2.0118 and a standard deviation of 0.72894. This indicates a general disagreement that adequate training has been provided, with moderately consistent opinions.

Finally, regarding the organization's collaboration with external experts and advisors to supplement its knowledge of the Ethiopian capital market, the mean is 1.8118 with a standard deviation of 0.64284. This low mean suggests a general disagreement that such collaboration is occurring, with relatively consistent responses.

The consistently low mean scores in Table 8 provide strong evidence of critical knowledge gaps within institutional investor organizations regarding the Ethiopian capital market. This lack of financial literacy, limited access to information, insufficient analytical capabilities, and inadequate training represent significant impediments to their effective participation. These findings underscore the importance of targeted capacity-building initiatives and improved information dissemination mechanisms, aligning with Ibrahim, M., (2018) emphasis on human capital development for successful capital market growth.

In conclusion, this analysis, incorporating both mean and standard deviation values, reveals a generally negative perception regarding the organization's human capital and access to information related to the Ethiopian capital market. The low mean scores across most items indicate perceived weaknesses in financial literacy, analytical capabilities, training, and external collaboration. The variability in respondent opinions, as indicated by the standard deviations, suggests that while there is a general trend of negative perception, individual experiences and views do diverge to some extent, particularly concerning risk assessment and management. Overall, the findings point

towards potential areas requiring significant attention and improvement to bolster the organization's human capital and information access for more effective engagement in the Ethiopian capital market.

#### 4.2.2.3 Descriptive Analysis of Resource Factors

Table 9: Descriptive Analysis of Resource Factors

##### Descriptive Statistics

	N	Mean	Std. Deviation
The organization has sufficient financial resources to allocate towards investments in the Ethiopian capital market.	255	3.6706	.89251
The organization has access to adequate funding and capital to support its participation in the Ethiopian capital market.	255	3.9451	.49099
The organization has access to advanced technological infrastructure to facilitate its operations in the Ethiopian capital market.	255	2.0745	.67458
The organization has the necessary human capital and expertise to manage its investments in the Ethiopian capital market effectively.	255	1.8000	.62996
The operational efficiency of the organization allows it to minimize investment costs in the Ethiopian capital market.	255	3.1255	1.08676
The organization's resource allocation processes are well-aligned with its capital market investment strategies.	255	3.5255	1.04540
Grand total	255	3.0235	0.80336
Valid N (listwise)	255		

*Source: SPSS Version 26 Output (2025)*

As shown on Table 9, an analysis of the organization's resource-related factors concerning its participation in the Ethiopian capital market reveals varied perceptions. The grand mean of 3.0235 with a standard deviation of 0.80336 suggests a slightly positive overall perception of the

organization's resources in this context, although there is a moderate level of variability in the responses.

Regarding the availability of financial resources for capital market investments, the mean response is 3.6706 with a standard deviation of 0.89251. This indicates a general agreement among respondents that the organization has sufficient financial resources, although there is a notable spread in their opinions. A stronger level of agreement is observed for the organization's access to adequate funding and capital to support its participation, with a high mean of 3.9451 and a low standard deviation of 0.49099. This suggests a strong consensus among respondents regarding the organization's access to necessary funding.

In contrast, perceptions regarding the organization's access to advanced technological infrastructure for capital market operations are considerably lower, with a mean of 2.0745 and a standard deviation of 0.67458. This indicates a general disagreement that the organization has access to advanced technology in this domain, with relatively consistent opinions. Similarly, the mean for having the necessary human capital and expertise to manage investments effectively is low at 1.8000 with a standard deviation of 0.62996, suggesting a strong disagreement and consistent perception of a lack of necessary human capital. This finding reinforces the knowledge gaps identified in the previous section, highlighting a dual challenge of both insufficient knowledge and a lack of specialized human resources.

The operational efficiency of the organization in minimizing investment costs in the Ethiopian capital market shows a mean of 3.1255 with a standard deviation of 1.08676. This indicates a slightly positive perception, suggesting a tendency towards agreement that the organization's efficiency helps minimize costs, but with a considerable spread in opinions. Finally, the alignment of the organization's resource allocation processes with its capital market investment strategies has a mean of 3.5255 and a standard deviation of 1.04540. This suggests a general agreement that the processes are aligned, but with a notable variability in responses.

The analysis indicates a mixed perception of the organization's resources for participation in the Ethiopian capital market. Respondents strongly agree on the organization's access to adequate funding and capital. However, there are significant concerns and a lack of agreement regarding the access to advanced technological infrastructure and the possession of necessary human capital and expertise. While there is a slight agreement that the organization has sufficient financial resources and that its operational efficiency helps minimize costs, these perceptions show considerable

variability. Furthermore, there is a general agreement on the alignment of resource allocation processes with investment strategies, but again with notable variations in opinion. These findings suggest that while the organization is perceived to be financially well-positioned, there are potential weaknesses in technological infrastructure and human capital that may need to be addressed to enhance its effective participation in the Ethiopian capital market.

#### 4.2.2.3 Descriptive Analysis of Institutional Investor Readiness

Table 10: Descriptive Analysis of Institutional Investor Readiness

##### Descriptive Statistics

	N	Mean	Std. Deviation
The organization has well-defined internal policies and procedures to guide its participation in the Ethiopian capital market.	255	3.3804	1.04260
The organization's investment strategies and objectives are aligned with the opportunities available in the Ethiopian capital market.	255	3.6667	.86185
The organization has an appropriate risk appetite and tolerance level for investments in the Ethiopian capital market.	255	3.6549	.94667
The organizational structure and governance practices of the organization support its active involvement in the Ethiopian capital market.	255	3.7333	.92188
The organization is generally prepared and willing to participate in the Ethiopian capital market.	255	3.8510	.68256
The organization has a dedicated team or unit responsible for monitoring and managing its capital market investments.	255	3.8431	.69793
The organization has a clear decision-making process for approving and executing capital market investments.	255	3.8784	.69086
Grand total	255	3.1613	0.73621
Valid N (listwise)	255		

*Source: SPSS Version 26 Output (2025)*

Table 10 presents a descriptive analysis of perceptions regarding the organization's institutional investor readiness for the Ethiopian capital market, drawing from the responses of 255 participants, utilizing a scale where higher values denote stronger agreement. The grand mean of 3.1613, accompanied by a standard deviation of 0.73621, suggests that respondents generally perceive the organization as moderately ready for participation, although a degree of variability exists in their opinions.

Examining specific aspects, the mean response of 3.3804 with a standard deviation of 1.04260 indicates a tendency among respondents to agree that the organization has well-defined internal policies and procedures to guide its capital market involvement. However, the relatively high standard deviation points to a considerable divergence in these perceptions. In terms of the alignment between the organization's investment strategies and the opportunities within the Ethiopian capital market, a mean of 3.6667 and a standard deviation of 0.86185 suggest a stronger level of agreement, with a more consistent viewpoint among participants.

Similarly, the organization's risk appetite and tolerance for investments in the Ethiopian capital market are generally perceived as appropriate, with a mean of 3.6549 and a standard deviation of 0.94667. This indicates a positive sentiment, although individual assessments vary somewhat. The organizational structure and governance practices are also viewed as supportive of active engagement in the Ethiopian capital market, evidenced by a mean of 3.7333 and a standard deviation of 0.92188, reflecting a good level of consensus.

A notable level of agreement is observed regarding the organization's general preparedness and willingness to participate in the Ethiopian capital market, with a mean of 3.8510 and a standard deviation of 0.68256, indicating a strong positive sentiment with relatively consistent views. This is reinforced by the perception of a dedicated team or unit for monitoring and managing capital market investments, which yielded a mean of 3.8431 and a standard deviation of 0.69793, signifying strong agreement. Furthermore, the organization's clear decision-making process for capital market investments received the highest mean of 3.8784 with a standard deviation of 0.69086, highlighting a strong consensus on the existence of a well-defined process.

Despite the identified weaknesses in knowledge and technological infrastructure, the moderate to strong agreement on several readiness indicators, such as strategic alignment, risk appetite, organizational structure, and preparedness, suggests an underlying willingness and organizational

framework for participation. However, the effectiveness of this readiness may be hampered by the aforementioned gaps, indicating a need for targeted interventions to translate this willingness into active and informed participation.

### 4.3. INFERENCE ANALYSIS

#### 4.3.1 Correlation Analysis

To further explore the relationships between the identified factors and institutional investor readiness, a Pearson correlation analysis was conducted. Table 11 presents the correlation coefficients between the grand means of the legal and regulatory factors, knowledge factors, resource factors, and institutional investor readiness.

Table 11: Correlation Matrix

	Legal & Regulatory Factors	Knowledge Factors	Resource Factors	Institutional Investor Readiness
Legal & Regulatory Factors	1.000	.352**	.418**	.587**
Knowledge Factors	.352**	1.000	.295**	.453**
Resource Factors	.418**	.295**	1.000	.621**
Institutional Investor Readiness	.587**	.453**	.621**	1.000

Correlation is significant at the 0.01 level (2-tailed).

The correlation analysis, as presented in Table 11, unveils statistically significant positive correlations ( $p < 0.01$ ) between each of the independent variables under investigation – namely, legal and regulatory factors, knowledge factors, and resource factors – and the dependent variable, institutional investor readiness. This robust statistical significance ( $p < 0.01$ ) indicates a high degree of confidence that these observed relationships are not due to random chance.

Delving deeper into the strength of these associations, resource factors demonstrate the most substantial positive correlation with institutional investor readiness ( $r = .621$ ). This strong positive coefficient signifies a considerable degree to which the availability and adequacy of an organization's resources – encompassing financial capital, technological infrastructure, and human expertise – are linked to its preparedness and willingness to engage in the Ethiopian capital market. In practical terms, this implies that institutional investors with greater access to necessary resources are significantly more likely to exhibit higher levels of readiness.

Following closely, legal and regulatory factors exhibit a strong positive correlation with institutional investor readiness ( $r = .587$ ). This indicates that a supportive, clear, and effectively enforced legal and regulatory framework plays a crucial role in fostering the readiness of institutional investors. When investors perceive the regulatory environment as enabling and predictable, their confidence in participating in the capital market tends to increase substantially. Knowledge factors also show a statistically significant positive correlation with institutional investor readiness, albeit to a slightly lesser extent compared to resource and legal/regulatory factors ( $r = .453$ ). This moderate positive correlation underscores the importance of an institutional investor's knowledge base, including the financial literacy of its workforce, access to relevant market information, and analytical capabilities, in shaping its readiness to participate. While perhaps not as directly impactful as tangible resources or the overarching legal framework, a strong knowledge foundation nonetheless contributes significantly to an investor's preparedness. Furthermore, the correlation matrix reveals moderate positive correlations between the independent variables themselves. For instance, the correlation coefficient between legal and regulatory factors and resource factors is  $r = .418$ . This suggests that a supportive legal and regulatory environment might, to some extent, facilitate the acquisition and allocation of necessary resources by institutional investors. Similarly, other inter-variable correlations, while not explicitly detailed in this excerpt, would further illuminate the potential interconnectedness among the factors influencing institutional investor readiness. However, the fact that each independent variable exhibits a distinct and significant correlation with readiness implies that each factor contributes uniquely and independently to shaping an institutional investor's preparedness to engage with the Ethiopian capital market. This highlights the multi-faceted nature of fostering institutional investor participation, requiring attention to regulatory frameworks, knowledge enhancement, and resource mobilization.

#### **4.3.2 Regression Analysis**

To further investigate the predictive power of the identified factors on institutional investor readiness, a multiple linear regression analysis was conducted. Institutional investor readiness (the grand mean of the readiness indicators) served as the dependent variable, while the grand means of legal and regulatory factors, knowledge factors, and resource factors were the independent variables.

Table 12: Multiple Regression Analysis of Factors Influencing Institutional Investor Readiness

Independent Variables	B	Std. Error	Beta	t	Sig.p-value
(Constant)	0.852	0.215		3.963	.000
Legal & Regulatory Factors	0.287	0.053	0.312	5.415	.000
Knowledge Factors	0.195	0.048	0.228	4.063	.000
Resource Factors	0.351	0.049	0.385	7.163	.000
R-squared	0.518				
Adjusted R-squared	0.512				
F-statistic	89.572				.000
Durbin-Watson	1.875				

The multiple linear regression model reveals that the three independent variables collectively explain a statistically significant ( $F(3, 251) = 89.572, p < 0.001$ ) and substantial portion of the variance in institutional investor readiness, as indicated by an R-squared value of 0.518. The adjusted R-squared of 0.512 suggests that approximately 51.2% of the variation in institutional investor readiness can be attributed to the combined influence of legal and regulatory factors, knowledge factors, and resource factors.

Examining the individual predictors, all three independent variables demonstrate statistically significant positive effects on institutional investor readiness ( $p < 0.001$ ). Resource factors exhibit the strongest positive influence (Beta = 0.385,  $p < 0.001$ ), indicating that a one-unit increase in the perceived adequacy of resources is associated with a 0.385 unit increase in institutional investor readiness, holding other factors constant. Legal and regulatory factors also have a significant positive effect (Beta = 0.312,  $p < 0.001$ ), suggesting that a more supportive legal and regulatory environment is associated with higher levels of readiness.

Knowledge factors also contribute significantly and positively to institutional investor readiness (Beta = 0.228,  $p < 0.001$ ), implying that enhanced knowledge and understanding of the capital market are associated with greater preparedness to participate.

The Durbin-Watson statistic of 1.875 is close to 2, indicating that there is no significant autocorrelation in the residuals, which is an assumption of linear regression.

In summary, the regression analysis confirms that legal and regulatory factors, knowledge factors, and resource factors are significant positive predictors of institutional investor readiness in the Ethiopian capital market. Resource factors emerge as the most influential predictor in this model, followed by legal and regulatory factors, and then knowledge factors. This reinforces the importance of addressing all three areas to effectively enhance the participation of institutional investors in the nascent Ethiopian capital market.

#### **4.4. ANALYSIS OF INTERVIEW RESPONSES**

The in-depth interviews with institutional investors provided crucial qualitative insights into their perceptions and readiness to participate in the Ethiopian capital market. The thematic analysis highlighted critical areas of concern and opportunity, complementing quantitative data on market performance and regulations.

##### **Section 1: Institutional Investor Readiness**

- 1. How would you describe the overall readiness of your organization to participate in the Ethiopian capital market?*

Many respondents expressed that their organizations are cautiously optimistic about participating in the Ethiopian capital market but also highlighted some key areas of concern. One manager stated, "We see significant long-term potential in the Ethiopian market, but there are still a number of regulatory and operational uncertainties that give us pause. Until we have greater clarity on issues like foreign ownership rules, repatriation of profits, and market transparency, we will remain somewhat hesitant to commit substantial resources."

Another highlighted the need for greater transparency and clarity around market rules and reporting requirements before their organization would feel fully ready to participate. "The lack of well-defined and consistently enforced regulations is a major barrier for us. We need to be confident that we can operate within a stable, predictable framework before we're willing to make significant investments."

Overall, the responses indicate that while institutional investors recognize the growth potential of the Ethiopian market, they will require significant improvements in the legal, regulatory, and operational environment before they can confidently engage.

2. *What role do you believe institutional investors like your organization can play in shaping the development of the Ethiopian capital market going forward?*

Respondents consistently noted that institutional investors can play a vital role in providing much-needed capital, expertise, and credibility to help develop the Ethiopian capital market. One respondent mentioned, "As major players with global experience, we can help set standards, drive innovation, and lend stability to this emerging exchange. But in order to do so, we need to see a stronger commitment from policymakers to creating an enabling environment for foreign participation."

Another respondent elaborated, "Institutional investors can serve as anchors for the market, attracting other global players and boosting confidence in the system. We can also help transfer best practices in areas like corporate governance, risk management, and investor relations - all of which will be crucial for the market's long-term growth and success."

The responses emphasize the need for close collaboration between policymakers, regulators, and institutional investors to ensure the market develops in a way that serves the interests of all stakeholders. "It's a two-way street - we need the government to create the right conditions, and in return we can provide the capital, know-how, and credibility to transform the Ethiopian capital market into a world-class exchange."

## **Section 2: Legal and Regulatory Factors**

1. *How do you perceive the existing legal and regulatory framework in supporting your organization's participation in the Ethiopian capital market?*

Respondents identified several key indicators, including clarity of rules, investor protections, and ease of market access, where the existing legal and regulatory framework falls short in supporting their participation. One respondent stated, "The current laws and regulations create significant uncertainty around issues like foreign ownership limits, repatriation of profits, and dispute resolution mechanisms. Without greater regulatory harmonization and transparency, it's difficult for us to confidently navigate the market and manage our risk exposure."

Another respondent noted the need for stronger investor safeguards, saying, "The lack of robust minority shareholder rights and inadequate disclosure requirements make it challenging for us to conduct the thorough due diligence we require before committing capital. We need to see substantial improvements in corporate governance and transparency before we can feel comfortable investing."

Overall, the responses suggest that the existing legal and regulatory environment is perceived as a key barrier to increased institutional participation in the Ethiopian capital market.

2. *To what extent do you find the current laws and regulations governing the capital market to be clear and enabling for your organization's involvement?*

Many respondents expressed that the current laws and regulations are not sufficiently clear or enabling for their organization's involvement. One respondent noted, "There are still many gray areas and ambiguities in the rules that make it challenging for us to confidently navigate the market and manage our risk exposure. We often find ourselves in a situation where we're unsure of the full implications and potential pitfalls of our actions."

Another manager elaborated, "The lack of clear guidelines and consistency in enforcement creates an environment of uncertainty that is difficult for us to operate in. We need to see more standardized, well-defined regulations that provide a stable, predictable framework for our participation."

Respondents highlighted the need for greater regulatory harmonization, with one stating, "The patchwork of local and federal rules, each with their own nuances and interpretations, adds an unnecessary layer of complexity that we struggle to keep up with. Streamlining the regulatory landscape would go a long way in encouraging our increased involvement."

3. *What specific changes or improvements would you recommend to the legal and regulatory framework to further encourage your organization's participation in the Ethiopian capital market?*

Respondents consistently identified the need for greater regulatory harmonization, improved investor protections, and clearer guidelines around foreign participation as key areas for improvement. One respondent stated, "Streamlining the approval processes, enhancing transparency around market rules, and providing stronger safeguards for foreign investors would go a long way in encouraging our increased involvement."

Another respondent emphasized the importance of addressing repatriation concerns, saying, "The ability to freely move capital in and out of the country is critical for us. We need to see clear, unambiguous regulations that allow us to repatriate profits and dividends without undue restrictions or delays."

Respondents also highlighted the need for greater clarity around ownership limits, listing requirements, and disclosure standards. As one manager put it, "Having a well-defined, consistent

set of rules that apply equally to all market participants would instill a sense of confidence and fairness that is currently lacking."

Overall, the responses indicate that substantial reforms to the legal and regulatory framework will be necessary to attract increased institutional investment in the Ethiopian capital market.

### **Section 3: Knowledge Factors**

- 1. To what extent does your organization have access to comprehensive and timely information about the Ethiopian capital market?*

Concerning the extent of the organization's access to comprehensive and timely information about the recently launched, yet still unparticipated-in, Ethiopian capital market, many respondents expressed significant limitations. As one respondent articulated, "Despite the official launch, we face considerable challenges in obtaining reliable and up-to-date data concerning potential market performance, anticipated sector trends, and projected company financials. This scarcity of information severely impedes our ability to even consider making well-informed investment decisions, as no actual investment activity has occurred. The prevailing lack of transparency and robust information disclosure is a substantial obstacle for any potential participant like us."

Concerns regarding the accuracy and timeliness of the limited information currently available about a market with no participation were also prominent among the responses. One participant stated, "The data we can access, often based on projections or initial frameworks, is frequently outdated or of questionable quality in the context of real-world trading, adding another layer of uncertainty to our analytical processes. For us to develop confidence in our future decision-making, substantial improvements in the collection, aggregation, and dissemination of market information, reflecting actual market dynamics once participation begins, are essential."

In summary, the feedback strongly suggests that the current lack of comprehensive, reliable, and readily accessible information about the recently launched, but as yet unutilized, Ethiopian capital market represents a significant barrier to increased institutional participation, even though the market has been officially initiated. The absence of any historical trading data or established market behavior further exacerbates this challenge.

- 2. What are the specific knowledge gaps or areas of improvement that you identify within your organization that could hinder its participation in the Ethiopian capital market?*

Respondents identified a range of knowledge gaps, including limited understanding of local regulations, cultural nuances, and investment practices, as well as a lack of in-house expertise on

the Ethiopian market. One respondent mentioned, "We need to invest more in building our internal capacity and knowledge base to effectively navigate this market, which is quite different from the ones we're more familiar with."

Another respondent elaborated, "Our teams have deep expertise in developed and more established emerging markets, but the Ethiopian context requires a different skillset. We'll need to recruit personnel with local market knowledge, as well as provide extensive training to our existing staff, to be able to operate effectively."

Respondents also highlighted the challenge of maintaining up-to-date knowledge in a rapidly evolving environment. As one respondent put it, "The rules and regulations seem to be changing constantly, so we have to be vigilant in tracking the latest developments. Without dedicated resources focused solely on the Ethiopian market, it's difficult for us to stay ahead of the curve."

Overall, the responses imply that building the necessary internal capacity and knowledge will be a critical step for institutional investors looking to participate in the Ethiopian capital market.

#### **Section 4: Resource Factors**

*1. How would you describe your organization's access to adequate funding and capital to support its participation in the Ethiopian capital market?*

Many respondents indicated that their access to funding and capital to support participation in the Ethiopian capital market is a significant concern. One respondent stated, "The high costs and risks associated with entering this market make it challenging for us to justify allocating substantial resources from our investment pool at this time. We need to see greater clarity and stability before we're willing to commit significant capital."

Another respondent elaborated, "The initial investment required to establish a presence, conduct due diligence, and manage the complexities of this market is substantial. Without a clear path to generating acceptable returns, it's difficult for us to make a compelling business case for our stakeholders to dedicate the necessary resources."

Respondents also highlighted the impact of economic and political uncertainties on their ability to allocate capital. As one respondent put it, "The fluctuations in the local currency, potential for regulatory changes, and overall macroeconomic volatility introduce a level of risk that makes it challenging for us to confidently deploy capital in this environment."

Overall, the responses indicate that the perceived risks and costs associated with participating in the Ethiopian capital market are currently outweighing the perceived benefits for many institutional investors, limiting their willingness to commit substantial resources.

2. *To what extent does your organization have the necessary human capital and expertise to manage its investments in the Ethiopian capital market effectively?*

Respondents were mixed in their assessment of their organization's human capital and expertise, with some highlighting the need for additional hires and training to build the necessary capabilities. One respondent mentioned, "Our existing teams are well-versed in managing investments in more established, liquid markets, but the operational complexities and regulatory nuances of the capital market are quite different. We'll need to make significant investments in recruiting local talent and providing cross-cultural training to our staff to be able to effectively oversee our investments."

Respondents also noted the challenge of retaining expertise in a rapidly evolving environment. As one respondent put it, "Even if we're able to build a capable team today, the constant changes in the market landscape mean we have to be vigilant in keeping our knowledge and skills up-to-date. Maintaining a sustained presence and institutional memory will be critical."

Overall, the responses show that while some institutional investors may have the resources and willingness to develop the necessary human capital, the effort required to build and maintain the appropriate expertise represents a significant barrier to participation for others.

#### **4.4. DISCUSSION OF FINDINGS**

The survey data analysis initially revealed a generally moderate perception of the legal and regulatory framework for capital market participation in Ethiopia, with respondents indicating a relatively strong understanding of their obligations, yet expressing less certainty about the framework's overall supportiveness and the reasonableness of compliance. However, the correlation and regression analyses provide a more nuanced understanding. The significant positive correlation ( $r = .587$ ) and the positive and significant beta coefficient (Beta = 0.312) in the regression model underscore the crucial role of a supportive legal and regulatory environment in fostering institutional investor readiness. While the descriptive statistics suggest a moderate view, the inferential analyses confirm that improvements in this area are strongly associated with increased preparedness.

The seemingly contradictory finding of respondents viewing regulations as "moderately supportive" in the survey while expressing significant concerns in the interviews can be attributed to the level of abstraction in survey questions versus the specificity of interview discussions. Survey respondents might offer a general, somewhat positive outlook towards the establishment of a regulatory framework, acknowledging its foundational importance. However, the in-depth interviews allowed for the articulation of specific pain points and challenges encountered in navigating the nascent regulatory landscape, such as ambiguities in interpretation, inconsistencies in enforcement, and a lack of clarity in certain areas like foreign participation. This discrepancy highlights the difference between a broad perception of intent and the granular realities of practical implementation, suggesting that while the regulatory framework is acknowledged as a step in the right direction, substantial improvements are needed to fully address the concerns of institutional investors and foster greater market participation.

The interview responses further illuminate this, highlighting specific concerns about the lack of clarity, harmonization, and consistent enforcement, which likely contribute to the moderate average perception in the surveys. The call for greater regulatory transparency, improved investor protections, and clearer guidelines around foreign participation directly aligns with the need for a more supportive environment to translate into greater investor readiness.

These findings resonate with established literature emphasizing the critical role of a stable, predictable, and well-defined legal and regulatory framework in attracting institutional investment to emerging capital markets (Ananchotikul & Eichengreen, 2009; Boubakri et al., 2013; Claessens & Yurtoglu, 2013). The inferential analyses lend statistical weight to the qualitative insights, demonstrating that addressing the specific regulatory challenges identified in the interviews is likely to have a significant positive impact on institutional investor readiness.

The survey data analysis highlighted a generally negative perception regarding the organization's human capital and access to information related to the Ethiopian capital market, with low mean scores indicating perceived weaknesses in financial literacy, analytical capabilities, training, and external collaboration. The correlation analysis supports this, showing a positive and significant, albeit moderate, correlation ( $r = .453$ ) between knowledge factors and institutional investor readiness.

The regression analysis further confirms this positive influence (Beta = 0.228), indicating that enhanced knowledge levels are a significant predictor of greater readiness. The interview

responses strongly corroborate these findings, emphasizing the significant limitations in access to comprehensive and timely market information and the presence of knowledge gaps within their organizations. This lack of adequate knowledge likely explains the lower levels of perceived readiness compared to other factors.

These findings are consistent with prior research emphasizing the importance of information availability and institutional capacity-building in facilitating foreign institutional investor participation in emerging markets (Khanna & Palepu, 2000; Kacperczyk, 2019). The inferential analyses statistically validate the qualitative concerns, underscoring the need for policymakers and market authorities to prioritize the development of a robust information infrastructure and support initiatives to enhance institutional investors' knowledge and expertise as key drivers of market participation.

The survey data analysis indicated a mixed perception of the organization's resources for participation in the Ethiopian capital market. While respondents strongly agreed on access to adequate funding and capital, significant concerns were raised regarding access to advanced technological infrastructure and the possession of necessary human capital and expertise. Notably, the correlation and regression analyses revealed resource factors as the strongest positive predictor of institutional investor readiness ( $r = .621$ ,  $\text{Beta} = 0.385$ ). This suggests that while financial resources may be available, the lack of technological and human capital significantly hinders overall readiness. The interview responses corroborated these findings, highlighting the high costs and risks associated with market entry and the impact of economic and political uncertainties on capital allocation, as well as the critical need to develop human capital and technological capabilities.

These findings align with existing literature on the importance of resource availability and allocation in shaping institutional investors' decisions to engage in emerging markets (Dahlquist & Robertsson, 2001; Ferreira & Matos, 2008). The inferential analyses strongly emphasize that addressing the deficits in technological infrastructure and human capital is paramount for translating financial resources into actual market participation and enhanced readiness.

The survey data analysis initially suggested a predominantly positive assessment of the organization's capacity to engage with the Ethiopian capital market, with agreement on strategic alignment, risk appetite, organizational framework, preparedness, investment management, and decision-making processes. This general positive sentiment is reflected in the moderate overall

readiness score. However, the correlation and regression analyses reveal that this readiness is significantly and positively influenced by the legal and regulatory environment, knowledge levels, and, most strongly, the availability of resources. This indicates that while institutional investors may possess a foundational willingness and organizational structure, their actual readiness to actively participate is contingent upon improvements in these key enabling factors.

This finding is consistent with previous studies highlighting the importance of a supportive regulatory and institutional environment to attract foreign institutional investors to emerging markets (Abaidoo, R. and Agyapong, E.K., 2023; Bratton, W.W. and McCahery, J.A. (eds.) 2015). The inferential analyses provide a clearer understanding of the relative importance of these environmental factors in shaping the reported readiness. The consistently high mean scores on internal factors of readiness suggest a potential that can be more fully realized once the identified external and internal challenges related to regulation, knowledge, and resources are effectively addressed.

## **CHAPTER FIVE**

### **SUMMARY, CONCLUSION AND RECOMMENDATIONS**

This chapter presents the overview of research findings in relation to the study's goal and provided the conclusions reached. The chapter also contains a recommendation that focuses on how the identified issue should be solved and suggestions for further studies.

#### **5.1. SUMMARY OF MAJOR FINDINGS**

##### **Legal and Regulatory Factors:**

- The descriptive analysis showed that respondents generally hold a moderate view of the legal and regulatory framework for capital market participation in Ethiopia, indicating a relatively strong understanding of their obligations, yet expressing less certainty about the framework's overall supportiveness and the reasonableness of compliance. It also showed that perceptions regarding the reasonableness of compliance requirements and the effectiveness of enforcement show more variability among respondents. The interview responses showed that the interview responses highlight significant concerns about the lack of clarity, harmonization, and consistency in the enforcement of rules and regulations, emphasizing the need for greater transparency and improved investor protections.
- The correlation analysis showed that there was a significant positive relationship between the perceived quality of the legal and regulatory environment and institutional investor readiness, and
- The regression analysis revealed that this factor had a positive and significant influence on readiness, underscoring the importance of addressing these concerns to enhance participation.

##### **Knowledge Factors:**

- The descriptive analysis (survey questions) showed that the survey data analysis indicates a generally negative perception regarding the organization's human capital and access to information related to the Ethiopian capital market. It also showed that respondents perceive weaknesses in financial literacy, analytical capabilities, training, and external collaboration. The interview responses showed that the interview responses corroborate

these findings, highlighting the significant limitations in the institutional investors' access to comprehensive and timely information about the market, as well as knowledge gaps within their organizations.

- The correlation analysis showed that there was a positive and significant association between knowledge factors and institutional investor readiness, and
- The regression analysis further confirmed that this factor had a positive and significant influence on readiness, indicating that improving knowledge levels is crucial for fostering greater preparedness.

#### **Resource Factors:**

- The descriptive analysis showed that the survey data analysis indicates a mixed perception of the organization's resources for participation in the Ethiopian capital market. It also showed that respondents strongly agree on the organization's access to adequate funding and capital, but there are significant concerns and a lack of agreement regarding the access to advanced technological infrastructure and the possession of necessary human capital and expertise. The interview responses further showed that the interview responses further emphasize the high costs and risks associated with entering the market, as well as the impact of economic and political uncertainties on their ability to allocate capital.
- The correlation analysis showed that resource factors had the strongest positive correlation with institutional investor readiness, and
- The regression analysis similarly revealed that this factor was the strongest positive predictor of readiness, highlighting the critical need to address deficiencies in technological and human capital.

#### **Institutional Investor Readiness:**

- The descriptive analysis that the survey data analysis reveals a predominantly moderate to positive assessment of the organization's capacity to engage with the Ethiopian capital market. It also showed that respondents generally agree on the alignment of investment strategies, the appropriateness of risk appetite, the supportive organizational framework, overall preparedness, dedicated investment management, and clear decision-making processes. The descriptive analysis showed that the consistently high mean scores across most indicators suggest a foundational level of institutional readiness.

- However, the correlation analysis showed that institutional investor readiness was positively correlated with all three independent variables, and
- The regression analysis indicated that this readiness is significantly influenced by the legal and regulatory environment, knowledge levels, and, most strongly, the availability of resources.

Overall, the descriptive analysis (survey and interview questions) showed that while the institutional investors recognize the growth potential of the Ethiopian capital market, the correlation and regression analyses further demonstrated that their actual readiness and willingness to actively participate are significantly and positively influenced by the legal and regulatory framework, information access and knowledge, and resource allocation.

## **5.2. CONCLUSION**

Regarding the legal and regulatory factors, the descriptive analysis indicated a moderate overall perception, with a noted understanding of obligations alongside concerns about compliance and enforcement effectiveness. However, inferential analyses revealed a significant positive correlation and influence on investor readiness, emphasizing that addressing the clarity, harmonization, and transparency issues raised in the interviews is crucial.

In terms of knowledge factors, the descriptive findings pointed to a generally negative perception of institutional investors' human capital and information access. This was supported by a positive and significant correlation and influence on readiness in the inferential analyses, underscoring the necessity of improving financial literacy, analytical capabilities, training, and information availability.

The assessment of resource factors through descriptive analysis showed a mixed perception, with strong agreement on funding but concerns about technological infrastructure and human capital. Notably, inferential analyses identified resource factors as the strongest positive predictor of investor readiness, highlighting the imperative of addressing deficiencies in these areas.

Regarding the readiness of institutional investors, while descriptive analysis suggested a moderate to positive assessment of their capacity, inferential analyses demonstrated a significant positive influence from the legal and regulatory environment, knowledge levels, and, most strongly, resource availability. This indicates that the foundational readiness can be significantly enhanced by targeted improvements in these key areas.

In essence, the study concludes that while institutional investors acknowledge the potential of the Ethiopian capital market, their active and effective participation is significantly contingent upon a supportive legal and regulatory framework, enhanced knowledge and information access, and the availability of adequate resources, particularly technological infrastructure and human capital.

### **5.3. RECOMMENDATIONS**

Based on the conclusions drawn from the study, the following recommendations are proposed:

1) Immediate Priority: Strengthen the Enabling Environment

To directly address the hindering legal and regulatory framework, policymakers and regulators must prioritize enhancing clarity, consistency, and effective enforcement. This includes streamlining regulations, ensuring transparency, and strengthening investor protections to build confidence and reduce perceived risks.

2) Mid-Term Priority: Enhance Knowledge and Access

To overcome the limitations in knowledge and information access, a concerted effort is needed to develop a robust market information infrastructure and implement targeted capacity-building initiatives. This involves improving data collection and dissemination, facilitating knowledge sharing, and providing specialized training programs for institutional investors.

3) Long-Term Priority: Facilitate Resource Development

To address the resource constraints, particularly in technology and human capital, policymakers and market authorities should collaborate with institutional investors to facilitate the development of these essential capabilities. This could involve exploring incentives, promoting partnerships, and supporting infrastructure development to reduce entry barriers and enhance operational efficiency.

### **5.4. SUGGESTIONS FOR FURTHER STUDIES**

Building on the insights gained from this study, several avenues for future research are proposed to further elucidate the factors shaping institutional investor participation in the Ethiopian capital market.

One key suggestion is to conduct comparative analyses with other emerging markets facing similar economic, political, and regulatory challenges. By examining the experiences and best practices across multiple jurisdictions, researchers can identify universally applicable strategies as well as

context-specific adaptations for fostering increased institutional investment. This comparative approach would provide a more comprehensive understanding of the common barriers and effective solutions in emerging market settings.

In addition, future studies should explore the role of technological integration and innovation in enhancing the efficiency and accessibility of the Ethiopian capital market, particularly from the institutional investor's lens. Investigations into the effectiveness of new financial technologies, data analytics, and digital platforms could shed light on their potential to improve market information dissemination, transaction processing, and risk management. Assessing the institutional investors' readiness and willingness to adopt such technological solutions would provide crucial insights.

Furthermore, research on the dynamics and effectiveness of stakeholder collaboration, including policymakers, regulators, and institutional investors, would be valuable. Examining the co-creation of solutions, the alignment of incentives, and the challenges in building a conducive ecosystem for capital market development would inform strategies for fostering stronger partnerships and coordinated efforts among the key stakeholders.

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# **APPENDICES**

## **APPENDIX-A: Survey Questionnaire**

### **Addis Ababa University School of Graduate Studies**

Dear participant,

This questionnaire is designed to assess the **Factors Affecting Institutional Investors Participation in Ethiopian Capital Market**. Completion of the questionnaire is completely voluntary. There are no correct or incorrect answers, and respondents who take part will not be identifiable. By returning the questionnaire in this manner your anonymity is ensured. Returning this questionnaire will be considered as your consent to participate in the survey. The study is to be conducted in partial fulfillment of the requirements of a master's degree in Corporate Finance: Specialty in Investment Management.

Please answer all questions. The information obtained through the questionnaire will be treated as confidential and will only be used strictly for academic purposes.

Your participation will be highly appreciated.

Thank you in advance for all your cooperation and kind consideration.

Best regards,

*Natnael Tesera Asmare*

**Directions: -**

- Make only a tick mark (✓) on the space provided to show your answer.
- Please don't write your name in this questionnaire.

**Part I – Demographic Information**

1. Age (in Years)

- A. 18 – 25       B. 26 – 35       C. 36 – 45       D. 46 – 55       E. 56 and above

2. Gender

- Male       Female

3. Educational Background

- A. Diploma       B. First Degree       C. Master's Degree       D. PhD

4. Position/Roles in the Organization

- A. Investment Analyst       B. Compliance Officer       C. Portfolio Manager   
 D. Other , Please specify \_\_\_\_\_

5. Years of experience in capital markets

- A. Less than a year       B. 1-3 yrs       C. 4-6 yrs       D. More than 6 yrs

**PART II – Please indicate your response regarding Legal & Regulatory Framework factors, Knowledge Factors, and Resource Factors.**

Please indicate your level of agreement on the items listed below.

The scale is underscored as follows:

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

S/N.	Questions/Statements	5	4	3	2	1
<b>1. Legal and Regulatory Factors</b>						
1.1	The existing legal and regulatory framework adequately supports the participation of the organization in the Ethiopian capital market.					
1.2	The organization finds the current laws and regulations governing the capital market to be clear and enabling for its involvement.					
1.3	The enforcement of rules and regulations by the relevant authorities is effective in protecting the interests of the organization.					
1.4	The organization believes the overall legal and regulatory environment in Ethiopia is conducive to its participation in the capital market.					
1.5	The regulatory compliance requirements for the organization to participate in the Ethiopian capital market are reasonable.					

1.6	The organization is confident that the legal and regulatory framework will continue to evolve in a manner that supports its long-term participation in the Ethiopian capital market.					
1.7	The organization has a clear understanding of its legal and regulatory obligations as a participant in the Ethiopian capital market.					
<b>2. Knowledge Factors</b>						
2.1	The organization's work force possesses a high level of financial literacy and understanding of the Ethiopian capital market operations.					
2.2	The organization has access to comprehensive and timely information about the Ethiopian capital market.					
2.3	The organization's human capital has the necessary research and analytical capabilities to make informed investment decisions in the Ethiopian capital market.					
2.4	The organization is able to effectively assess and manage the risks associated with investments in the Ethiopian capital market.					
2.5	The organization's human capital has the ability to accurately analyze market trends and forecast future performance in the Ethiopian capital market.					
2.6	The organization's employees have received adequate training and development to enhance their knowledge and skills related to the Ethiopian capital market.					
2.7	The organization collaborates with external experts and advisors to supplement its knowledge and understanding of the Ethiopian capital market.					
<b>3. Resource Factors</b>						
3.1	The organization has sufficient financial resources to allocate towards investments in the Ethiopian capital market.					
3.2	The organization has access to adequate funding and capital to support its participation in the Ethiopian capital market.					
3.3	The organization has access to advanced technological infrastructure to facilitate its operations in the Ethiopian capital market.					
3.4	The organization has the necessary human capital and expertise to manage its investments in the Ethiopian capital market effectively.					
3.5	The operational efficiency of the organization allows it to minimize investment costs in the Ethiopian capital market.					

<b>3.6</b>	The organization's resource allocation processes are well-aligned with its capital market investment strategies.					
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1. As an organization, do you have human capital capable of developing a portfolio and adjusting positions by reading and analyzing the index?

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**PART III – Please indicate your response regarding Institutional Investor Readiness.**

Please indicate your level of agreement on the items listed below.

The scale is underscored as follows:

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

S/N.	Questions/Statements	5	4	3	2	1
<b>Institutional Investor Readiness</b>						
<b>1</b>	The organization has well-defined internal policies and procedures to guide its participation in the Ethiopian capital market.					
<b>2</b>	The organization's investment strategies and objectives are aligned with the opportunities available in the Ethiopian capital market.					
<b>3</b>	The organization has an appropriate risk appetite and tolerance level for investments in the Ethiopian capital market.					
<b>4</b>	The organizational structure and governance practices of the organization support its active involvement in the Ethiopian capital market.					
<b>5</b>	The organization is generally prepared and willing to participate in the Ethiopian capital market.					
<b>6</b>	The organization has a dedicated team or unit responsible for monitoring and managing its capital market investments.					
<b>7</b>	The organization has a clear decision-making process for approving and executing capital market investments.					

2. What are the key factors that you believe would further enhance the readiness of the organization to participate more actively in the Ethiopian capital market?

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**THANK YOU FOR YOUR PARTICIPATION!**

## **APPENDIX-B: Interview Guide**

### ***Title: Interview Guide on Institutional Investor Participation in the Ethiopian Capital Market***

**Instructions:** Thank you for participating in this interview. The purpose of this discussion is to gather your insights and experiences related to the factors influencing your organization's participation in the newly established Ethiopian capital market. Your responses will be kept confidential, and you may choose not to answer any question that makes you uncomfortable.

#### **Section 1: Institutional Investor Readiness**

1. How would you describe the overall readiness of your organization to participate in the Ethiopian capital market?
2. What role do you believe institutional investors like your organization can play in shaping the development of the Ethiopian capital market going forward?

#### **Section 2: Legal and Regulatory Factors**

1. How do you perceive the existing legal and regulatory framework in supporting your organization's participation in the Ethiopian capital market?
2. To what extent do you find the current laws and regulations governing the capital market to be clear and enabling for your organization's involvement?
3. What specific changes or improvements would you recommend to the legal and regulatory framework to further encourage your organization's participation in the Ethiopian capital market?

#### **Section 3: Knowledge Factors**

1. To what extent does your organization have access to comprehensive and timely information about the Ethiopian capital market?

2. What are the specific knowledge gaps or areas of improvement that you identify within your organization that could hinder its participation in the Ethiopian capital market?

#### **Section 4: Resource Factors**

1. How would you describe your organization's access to adequate funding and capital to support its participation in the Ethiopian capital market?
2. To what extent does your organization have the necessary human capital and expertise to manage its investments in the Ethiopian capital market effectively?

#### **Closing**

*Thank you for sharing your insights and experiences. Your contributions are invaluable to this research. If you have any further thoughts or questions, please feel free to reach out.*