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## EMPLOYMENT IS THE MAJOR ROUTE OUT OF POVERTY - HOW DONORS CAN HELP

### Background Papers

*This document contains the set of background papers which have been drawn on to prepare the policy guidance note on Employment [see: DCD/DAC/POVNET(2009)16]. They have been prepared under the responsibility of their respective authors, and reviewed and approved by the POVNET Task Team on Employment and Labour Markets.*

Contact: Peter Bieler - Tel: +33(0)1 45 24 84 57 - Email: [peter.bieler@oecd.org](mailto:peter.bieler@oecd.org)

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## REVIEW OF DONORS' POLICIES AND PRACTICES RELATED TO EMPLOYMENT AND LABOUR MARKETS<sup>1</sup>

Laura Delponte, OECD Secretariat

### Key Messages

- Donors are pursuing different approaches and using a wide range of instruments to address employment and labour markets
- Rather little evaluative material is available on the employment impact of past interventions, showing the relatively short history of this development area.
- The lack of quality data on informal employment limits the ability to develop diagnoses of the labour market adapted to the situation in developing countries.

### Introduction

1. Creating more, better and more productive jobs is a daunting task in developing countries because labour markets have to absorb a large number of people within a short time period. In addition, a shortage of jobs can increase migration pressures, which can drain societies in developing countries of both well-educated and unskilled people. Persistently high poverty rates and the desire to achieve the Millennium Development Goals (MDGs) has created a sense of urgency resulting in developing countries and their donor partners giving more prominence to employment and labour market issues, in poverty reduction strategies and development co-operation programmes.

2. This stocktaking exercise aims to collect more evidence about the instruments that donors use to create more and better jobs and to improve employment outcomes. In summary, donors are pursuing different approaches and using a wide range of instruments. Little or no evaluative material is available on the employment impact of past interventions, although donors agree that this is an area where progress needs to be made. Furthermore, the lack of quality data on informal employment limits the ability to develop diagnoses of the labour market adapted to the situation in developing countries. This is a serious obstacle for policy formulation as the use of OECD country economic categories and concepts tends to bias the analysis towards formal and waged employment.

### I. Strategic framework

3. Although few donors have policy statements on employment, most donors recognise that creating more productive jobs is central to achieving the MDGs, in particular the target of halving income poverty. Case studies conducted jointly by the International Labour Organisation (ILO) and the Swedish International Development Co-operation Agency (Sida) in 2005 showed that poor performance in poverty reduction in fast growing economies is often associated with low employment dynamics. Strategy documents, white papers and speeches by senior aid agency staff clearly indicate that promoting better employment outcomes is key to poverty reduction. For instance, Germany's "Poverty Reduction – A Global Responsibility: Programme of Action 2015" underlines that a central element for halving poverty is

the establishment of strong economic structures which foster pro-poor growth, create scope for poverty reduction, increase employment and foster the development of the productive potential of the poor.

4. For many donors, job creation is an outcome of various sector programmes, such as education, agriculture or private sector development, rather than an objective in itself. The “informal international division of labour” - whereby the International Monetary Fund (IMF) and the World Bank focused on improving the macroeconomic environment, the ILO promoted job creation and the upgrading of working conditions through international labour standards and bilateral donors addressed supply and demand-side constraints to employment creation - has contributed to fragmenting the way donors tackle labour market issues and held back the formulation of holistic approaches. Moreover, experience with past policies promoting labour-intensive growth, especially public works programmes, has highlighted that instruments that create jobs in the short term might not bring about sustainable employment outcomes. In response, some donors are formulating conceptual and analytic frameworks to integrate employment issues better into growth diagnostics and sector programmes. For example, Sida has designed an Integrated Economic Analysis tool that brings together employment, macroeconomic and business environment analysis. In 2007 the European Commission released a Staff Working Document to promote employment through the European Union’s development co-operation.

## **II. Instruments used and institutional arrangements**

5. Since underemployment is a key issue in improving employment outcomes in developing countries, donors are increasingly concerned about productivity gains, *i.e.* job improvement, rather than job creation. Therefore, some donors emphasise the importance of skills development, to enhance the employability of the poor and to improve their chances of finding wage employment. Facilitating access to productive assets, such as land or capital, is pursued as another way of generating more productive self-employment opportunities. Recent research conducted by the French Development Agency (Afd) shows that these interventions have more sustainable employment outcomes when they are implemented together.

6. To promote employment, most donors support private sector development through a wide range of instruments, as the private sector is the major contributor to employment creation. Therefore, the ultimate objective of most business support programmes is creating more jobs through expanding existing businesses or fostering self-employment and entrepreneurship. For example, one of the objectives of Norwegian development assistance for private sector development is to create jobs that give people dignity and sustainable livelihoods.

7. Agriculture accounts for a large share of employment in developing countries and provides labour-intensive employment for the poor. Donors support a variety of interventions to increase employment in agriculture and livelihood diversification opportunities in rural areas. For instance, they encourage core agricultural activities that are based on labour-intensive operations, promote the expansion of agribusinesses, to encourage forward and backward linkages with the global agricultural value chain, and help improve access to local and international markets. Also, good agricultural research and extension could inspire sector-wide or large-scale vocational training schemes to enhance productivity and employment quality.

8. Few donors have an organisational unit or department responsible for employment and labour market issues. In addition, there is little easily accessible information about donor activities in this area available on the Internet. Consequently, expertise and specific information about these topics is spread across various units within development agencies and more can be done to improve the management of available knowledge. Within the Swiss Agency for Development and Cooperation for example, knowledge sharing, the capitalisation of experience and networking with specialised institutions are ensured through

the network “economy and employment”. This network is coordinated by one senior collaborator and include staff from different operational units at headquarters and in field offices. The European Commission and Germany’s GTZ also has an “Economic Development and Employment” section.

### **III. Ways to improve employment outcomes**

- a) An area clearly requiring improvement is the measuring of employment outcomes through indicators of the quantity and quality of jobs created. The latest generation of poverty reduction strategies pays more attention to setting employment targets but little has been done to follow through with systematic monitoring. In addition, the emergence of the ILO’s “decent work” agenda has brought more attention to the qualitative aspects of job creation, such as employment in the informal economy, the working poor and job security. These need to be included in evaluation processes as well.
- b) Donor harmonisation and co-ordination on labour market issues is not as advanced as in some other areas of donors’ interventions, such as health and education. This may be because of the cross-cutting nature of the employment theme and because of relatively few interventions. Discussions within POVNET have highlighted the need for more conceptual clarity on the employment, growth and poverty reduction nexus and on the instruments that donors and partner countries can use to create more, better and more productive jobs.
- c) Most jobs in developing countries are in the informal economy. Therefore, donors are increasingly interested in understanding better what the interplay between the formal and informal economies in developing economies is and what is the right mix of policies and institutions that would create incentives to increase formal employment. To support this objective, some donors have contributed to academic research on the causes and consequences of formality and informality. Examples include AFD country studies, the joint Institute for the Study of Labour (IZA)/World Bank research programme, and the ILO’s In-Focus programme on Informality.
- d) Few donors have significant experience in working with labour market institutions, including the promotion of social dialogue or assistance to help reform labour market laws and regulations. Traditionally, the ILO has focused on these issues. However, bilateral donors are increasingly taking account of the important role of institutions, both formal and informal, in shaping employment outcomes. For instance, through its business sector programmes, Denmark is supporting reform of several labour market institutions as well as the establishment of genuinely tripartite dispute resolution mechanisms and institutions. Other donors, such as the Netherlands and Sweden, help to build capacity in employers’ organisations and labour unions in developing countries by establishing links with similar institutions in their own country.

### **IV. Cross-cutting issues**

- a) The 2007 World Development Report “Development and the Next Generation” showed that unemployment is higher for youths than for adults and that working youths are often found in low paying jobs or unpaid family work. Promoting youth employment is thus central to many donors that support the Youth Employment Network, a joint initiative between the World Bank, the ILO and the United Nations. In addition, the World Bank has prepared an inventory of interventions that support efforts by young people to find work. It showed that the most common type of intervention is skill upgrading through training programmes. Nevertheless, some donors have developed more holistic approaches. For example, Germany seeks to improve the social and economic integration of young people through targeted interventions built on three dimensions:

*i)* increasing the employability of young people; *ii)* helping them to start a business; and *iii)* providing mediation and job matching services.

9. Donors recognise that the promotion of gender equality is central to employment strategies, as the participation rate of women in the formal labour force is lower and they are often employed in low paid and precarious jobs. The lack of sex-disaggregated employment data impedes more precise assessment of the gender gap, the monitoring of progress and the evaluation of the impact of women-focused programmes. Nevertheless, donors have developed a dual approach to promote women's access to higher quality employment. Targeted interventions, such as micro-finance schemes for women or girl emancipation programmes, are reinforced by efforts to mainstream gender issues into the broader context of socio-economic policies and development co-operation. Most donors channel their support for better employment opportunities for women through multilateral initiatives, such as the World Bank's Gender Action Plan or the Women in Informal Employment: Globalizing and Organizing (WIEGO)<sup>2</sup> research policy network.

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<sup>1</sup> This report is based on information provided by members of the DAC Network on Poverty Reduction's (POVNET) Task Team on Employment and Labour Markets.

<sup>2</sup> <http://www.wiego.org/about/>

## **THE ROLE OF EMPLOYMENT AND LABOUR MARKETS IN THE FIGHT AGAINST POVERTY**

Christoph Ernst and Janine Berg, ILO

### **Main messages**

- Employment, and the quality of employment, decent work, is crucial for poverty reduction and in achieving growth with equity and pro-poor growth. The link between economic growth, employment and poverty reduction is thus a process in which output growth induces an increase in productive and remunerative employment, which, in turn, leads to an increase in the incomes of the poor and a reduction in poverty.
- Ensuring that growth is pro-poor requires high employment-intensity of growth and a rise in productivity which also depend on institutions, policies, laws and practices that positively affect the functioning of labour markets. A well-functioning institutional environment can support the virtuous circle and, in the process, facilitate pro-poor growth.
- Informal employment remains important, persistent and is often even rising. Thus, the quality of work of poor people holding an informal job has to be improved through the rise of productivity through vocational training and education, micro and small enterprise development and access to credit. Moreover, new strategies are needed to extend social security to informal workers, and to improve their working conditions. Formal job creation has to be accelerated, exceeding labour force growth. And the transfer from informal to formal employment should be facilitated through changes in regulations and tax or incentive systems, as well as rising productivity of informal activities.

### **I. Introduction**

1. In 2006, 195 million workers were unemployed, amounting to 6.3 per cent of the world's labour force. However, the number of unemployed paled in comparison to the working poor. That same year, 1.37 billion workers — nearly half the world's workers — were considered as “working poor.” These workers are living on less than USD2 dollars per day, a sum that is insufficient to lift themselves and their families out of poverty. To make long-term inroads into unemployment and working poverty, it is essential that greater use be made of periods of high growth, in order to generate more decent and productive jobs. Reducing unemployment and working poverty by creating such jobs should be viewed as a precondition for sustained, pro-poor, economic growth.

2. In its Policy Statement on Pro-Poor Growth, the DAC states that, in order for growth to be pro-poor, poor women and men must be able to participate in, contribute to and benefit from economic growth. The most effective means of participating, contributing and benefiting is through decent and productive employment. Thus policies are needed to ensure that the pace and pattern of economic growth leads to employment opportunities, and that the poor are sufficiently empowered to avail themselves of these opportunities. The past work of POVNET has focused on the how the development of the private sector, infrastructure and agriculture can be used in the fight against poverty. Employment features prominently in all of these topics.

3. The purpose of this conceptual framework is to serve as an advocacy tool in support of making employment a focus of development assistance, as opposed to just a by-product. The document is evidence-based, drawing on the experience of countries that have successfully reduced poverty, in order to shed light on the extent and manner in which growth has led to employment, and how more and better job opportunities have been translated into a reduction in poverty. It also discusses the challenges faced in other countries still grappling with high poverty levels, and the importance of employment in these efforts.

## II. The Challenge

4. Economic growth is essential, but not sufficient to achieve the Millennium Development Goals (MDGs). Macroeconomic and structural policies that promote employment, economic inclusion, empowerment and social investment are crucial. Ensuring that growth is pro-poor requires changes in the institutions, law and practices that perpetuate poverty. Employment is an essential ingredient in the fight against poverty and in achieving growth with equity.

5. Employment is also a recognized human right. The United Nations Universal Declaration of Human Rights includes the right to work, thus recognizing that many of the other economic and social entitlements proclaimed to be human rights cannot be secured without jobs that pay. In 1964, the International Labour Conference of the ILO passed the Employment Policy Convention (No. 122), which states: “Each Member shall declare and pursue, as a major goal, an active policy designed to promote full, productive and freely chosen employment.” Support for full employment — essentially that there should be work for all who are available and seeking work — is based on the recognition that the economic and social costs of unemployment are staggering, with far-reaching consequences extending beyond the single dimension of a loss of income.

6. Employment, and the quality of employment, is crucial for poverty reduction. The ILO’s Decent Work Agenda strives for economic growth with equity through a coherent blend of social and economic goals (See box below). The Global Employment Agenda of the ILO promotes both the quantitative objective of increasing freely chosen productive employment and the qualitative dimension of employment. In developing countries, where most people cannot afford to be out of work, many who do work live on less than USD1 or USD2 a day and are known as the “working poor.” Improving the quality of employment is thus a major challenge. The Global Employment Agenda seeks to place employment at the heart of economic and social policies, so that both the quantity and the quality of employment are improved.

### *The Decent Work Agenda and Poverty Reduction*

The four elements of the Decent Work Agenda and their role in alleviating poverty:

**Employment** – the principal route out of poverty is productive work

**Rights** – without them, women and men will not be empowered to escape from poverty

**Protection** – social protection safeguards against poverty

**Dialogue** – the participation of employers’ and workers’ organizations in shaping government policy for poverty reduction is essential.

7. However, full-employment and “decent work for all” are far from being achieved in the developing world. In low-income countries, working poverty is a greater problem than unemployment, whereas in middle-income developing countries, unemployment is a concern, along with working poverty (See Table 1).

**Table 1. Unemployment and Working Poor throughout the World**

Region	Unemployment Rate, 2005	% USD1/day working poor in total employment	% USD2/day working poor in total employment
World	6.4	17.6	47.4
Developed Economies and European Union	6.8	--	--
Central and Eastern Europe (non-EU) and CIS	9.4	2.1	10.5
East Asia	3.5	12.1	44.2
SE Asia and the Pacific	6.6	11.1	56.9
South Asia	5.2	34.4	87.2
Latin America and the Caribbean	8.1	11.3	30.9
Middle East and N. Africa	12.3	2.8	34.7
Sub-Saharan Africa	9.7	55.4	86.3

Source: ILO, *Global Employment Trends Brief*, January, 2007.

8. In developing countries, particularly low-income developing countries, unemployment is a luxury that few can afford. Most low-income countries do not have unemployment insurance and although family and kinship ties remain strong, workers cannot rely on these ties to compensate for their lost earnings. Thus, self-employment and casual labour become a refuge for job losers. The situation is slightly different in middle-income developing countries, such as Brazil, Chile, and Costa Rica. Workers with secondary or higher education, particularly the more educated youths, prefer to queue for better jobs. Moreover, Brazil and Chile provide unemployment benefits to workers who lose formal jobs, thus giving some income relief to the unemployed as they search for a job and alleviating some of the need to turn to informality for compensatory earnings. But this does not imply that unemployment, as a cause of poverty, should be dismissed. In South Africa, a middle-income developing country, unemployment is estimated at 40 per cent of the labour force and is a principle cause of poverty. Indeed, employment of labour market participants was found to be the largest single contributor to the avoidance of household poverty (Mwabu and Thorbecke, 2007).<sup>3</sup>

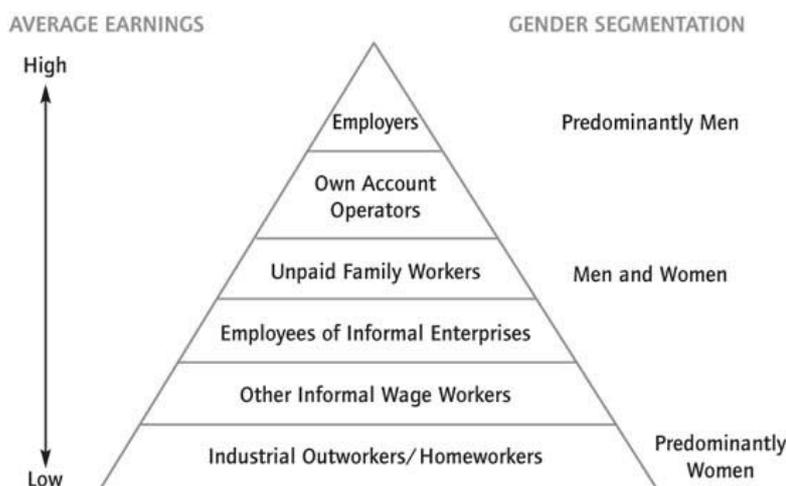
9. Another challenge for the labour markets of developing countries is *informal employment*. Contrary to the predictions of standard economic models that informal employment would disappear with economic development, informal employment remains important, persistent and, in some regions of the world, is even rising (Charmes, 2000)<sup>4</sup>. Informal employment, as defined by the 17<sup>th</sup> International Conference of Labour Statisticians in 2003, refers to the total number of informal jobs, whether carried out in formal sector enterprises, informal sector enterprises, or households<sup>5</sup>. It includes: (1) own-account workers and employers employed in their own informal sector enterprises; (2) family workers; (3) employees in informal jobs, whether employed in formal sector enterprises, informal sector enterprises, or households; (4) members of informal producers' cooperatives; and (5) own-account workers engaged in production of goods exclusively for own final use. Yet the paucity of labour market data in developing countries makes quantifying its extent difficult. If we limit the definition to micro enterprise workers, domestic workers, home workers and unremunerated family workers, it is estimated that during the 1990s, informal work in the non-agricultural sector constituted 43 per cent of employment in North Africa, 75 per cent in sub-Saharan Africa, 57 per cent in Latin America and 63 per cent in Asia (Beneria, 2001).<sup>5</sup>

10. Because of the wide spectrum of work that is considered as informal, large differences exist in the composition of the workforce, in working conditions, in earnings, as well as in the appropriate policy responses. Moreover, there is no clear cut separation between formal and informal employment. Some

informal workers may even opt out of formal structures, which is often just a sign of a decent work deficit at the low-end spectrum of formal employment. Nevertheless, the majority of informal workers will have difficulties reaching formal employment in the short or medium-term. As Figure 1 demonstrates, employers and own-account workers typically earn more than informal waged workers. Indeed, some studies indicate that their earnings are quite high, rivalling those of formally employed workers (Günther and A. Launov, 2006; Maloney, 1999; UNIFEM, 2005).<sup>6</sup> Nevertheless, self-employed workers typically do not contribute to social security systems and thus are not protected from the risks of disability and old age. Informally employed workers do not benefit from statutory protections that regulate conditions of work or from social security. Though informal workers often benefit from social assistance programmes, they do not benefit from the labour market and social protection policies that formal workers can access. The blurred line between the formal and informal sectors raises questions about the relevance and effectiveness of existing labour market, productivity and social protection policies.

11. Thus, a number of challenges exist with regard to informal employment. First, ways have to be found to improve the quality of work of poor people holding an informal job. The rise of productivity through vocational training and education, micro and small enterprise development and access to credit is a key element in raising their income. In addition, new strategies are needed to extend social security to informal workers, and to improve their working conditions. Second, formal job creation has to be accelerated, exceeding labour force growth. Major Latin-American countries, for example, have experienced a recent rise in the formal employment share of total employment. Third, the transfer from informal to formal employment should be facilitated. Changes in regulations and tax systems, incentive schemes, as well as rising productivity of informal activities, could contribute to this objective. Overall, a more holistic view of the employment and social protection agendas is needed. And it is not only the public sector, but also the private sector and trade unions, which must play a prominent role in this process.

**Figure 1: Average earnings and gender segmentation across informal employment categories**



Source: Chen, Vanek and Carr 2004.

12. Another challenge for labour markets is achieving *equality in employment opportunities for women*. Although women's participation in labour markets worldwide grew substantially in the 1980s and 1990s, women still participate less than men, are more likely to work in low productivity jobs in agriculture and services, to earn less, to be informal workers and to be unemployed. Moreover, women are estimated to constitute sixty per cent of the working poor (ILO, 2007).<sup>7</sup> *Young people* also face many challenges in the labour market. Those aged 15-24 are three times more likely to be unemployed than

adults. In 2005, the global youth unemployment rate was 13.5 per cent (ILO, 2006).<sup>8</sup> Young people are also more likely than adults to work informally.

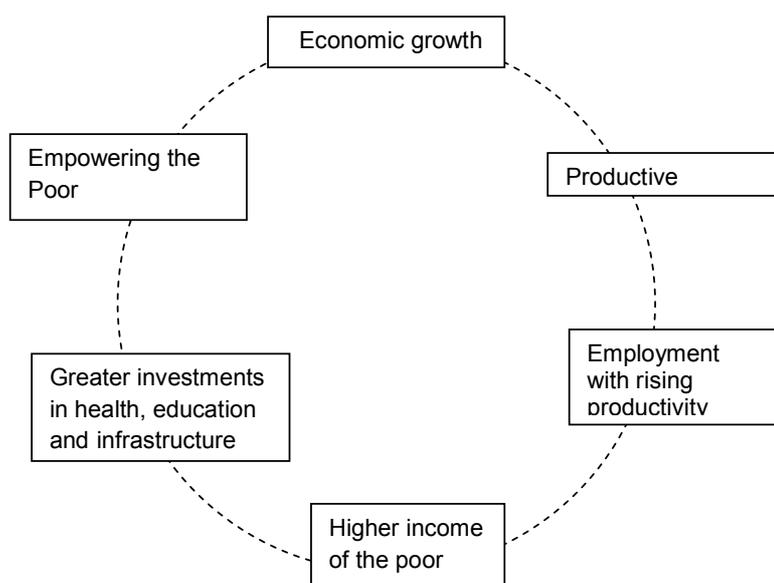
13. In addition, more than one third of the world's poor live in '*fragile states*' where the challenges of rebuilding the state and the economy are particularly acute. Because of the deteriorating economic situation and the unequal access to employment and productive assets, the poorest segments of society have been marginalised and exploited, with no access to productive assets and no voice in decision-making. Although it is beyond the scope of this paper to deal with all of the issues affecting employment and labour markets in fragile states, the need to create short-term employment as soon as conditions permit, and to invest in labour markets, has been highlighted as one of the more neglected issues in donor practice. The emphasis on governance issues and security dominate the donor agenda in fragile states. It is only recently that the international community has recognised the importance of economic reconstruction and employment as a means of contributing towards stability and state-building, as well as addressing the immediate needs of poor people in countries in which the state is not fulfilling its role. The challenges of creating employment in fragile states are dealt with in a separate hot topic paper highlighting the specific characteristics of situations in which government has failed, or is still failing, to provide citizens with basic services, security, and economic opportunities.

### **III. Evidence: Understanding the Growth-Employment-Poverty Link**

14. Although economic growth is typically thought of as the way to reduce poverty, its effectiveness in achieving this depends on the pattern of growth, essentially how particular sectors of the economy and workers benefit from growth. A high rate of economic growth, associated with a high degree of employment intensity, is a necessary condition for the reduction of poverty, but may not be sufficient. For poverty to be reduced, productivity and earnings (real wages, as well as returns from self-employment) must increase sufficiently to increase the incomes of the poor. The link between economic growth, employment and poverty reduction is thus a process in which output growth induces an increase in productive and remunerative employment, which, in turn, leads to an increase in the incomes of the poor and a reduction in poverty. The increase in incomes also finances investments in health and education that increase the productive capacity of the workforce, which improves sustainability. Success, however, will depend on the rate of economic growth, the output elasticity of demand for labour, and the ability of poor members of the labour force to respond to increasing demand for labour.

15. Ideally, there is a link between economic growth, employment and poverty reduction, which forms a virtuous circle, as Figure 2 illustrates. The stronger the links in the virtuous circle, the more likely it is that growth will be pro-poor. Although the circle does not have a defined beginning or end, the sequence can run from sustained rates of economic growth, which then, ideally, lead to sustained increases in productive capacity and generate employment opportunities, for waged and self-employed workers, irrespective of their sex, religion, ethnic or social group, or political opinion. Some of these opportunities may already exist, but they need to be up-graded, or new jobs involving higher technology and skill levels need to be created. Thus there is a need to integrate unemployed or underemployed workers into higher productive activities, so that they may obtain higher incomes. This income will allow families, businesses and society to invest in education and skill formation (for themselves or their children, thus for the future generation), as well as health, safety and other forms of social protection. These investments mitigate socioeconomic risks and empower the poor, thereby creating the necessary conditions for further investment, consumption, higher productivity and growth in the second round, and the completion of the virtuous circle of pro-poor growth (Islam, 2006).<sup>9</sup>

#### **Figure 2. Virtuous Circle of Links among Growth, Employment and Poverty Reduction**



Source: Based on Islam (2006).

16. There is, therefore, both a demand side and a supply side to achieving pro-poor growth. The variables that influence the income of the poor from the demand side include the employment-intensity of growth, shifts in the employment structure towards higher productivity sectors, greater availability of technology that boosts productivity, and the creation of assets for the poor. From the supply side, growth is best served if the poor are able to integrate into the process of economic growth and access the jobs and opportunities that are created. Enhancing education and skill development is a key aspect in this regard. Briefly, it is important that development efforts also focus on unleashing the creative and productive forces of the poor, to include them in the economic process. The focus is not simply on employment creation, and hence not on fostering labour-intensive growth as a panacea for poverty reduction, but rather on employment and productivity in a manner that increases the income of the poor efficiently, and gives them access to employment and thus to economic opportunities.

17. Many of the recent examples of pro-poor growth are in countries that have managed to enter this virtuous circle. While their success may not be easily replicable and there is much diversity in their experiences, there do appear to be some common factors behind their success and the role of employment and labour markets in making this success possible. This conceptual framework is organized around the six components of the virtuous circle: (1) economic growth; (2) productive capacity; (3) employment with rising productivity; (4) the higher income of the poor; (5) greater investments in health, education and infrastructure; and (6) increased productive capacity. Building on the work of Islam (2006) and ILO/UNDP (2007), this conceptual framework draws on the experience of countries that have made reductions in their poverty rate in recent decades, and assesses the importance of the growth-employment-poverty link in their achievements (ILO/UNDP, 2007).<sup>10</sup>

### **1. Economic growth**

18. High rates of economic growth for an extended period of at least a decade, and sometimes more, are a feature of most countries that have successfully reduced poverty. Average annual economic growth ranged from 7-9 per cent in Chile, China, India, Indonesia, Malaysia, Thailand and Vietnam. Malaysia sustained an average annual rate of 7.5 per cent for nearly three decades, from 1970 until the Asian financial crisis in 1997. Indonesia and Thailand also had long-lasting expansions of more than two decades. An annual growth rate of 7.5 per cent implies a doubling in national income in a period of ten years. It is thus not surprising that poverty was cut dramatically.

19. Macroeconomic policies are a key element in influencing economic growth on the demand side, and thus contribute to creating employment. Fiscal policy can mitigate economic downturns and employment losses. If anti-cyclical fiscal policy is used responsibly, through the implementation of a structural fiscal rule, as applied in Chile for example, and as recommended by the OECD and the IMF, investor confidence is improved. Important areas for fiscal spending that benefit job creation are on infrastructure investment, public works, and social transfers. Since the 1980s, the main concern of central banks has been fighting inflation, and the primary tool used has been the interest rate. While fighting inflation is imperative, it is also necessary that economic growth and employment creation regain their prominence as a central bank policy objective, as was the case in the 1950s and 1960s. Credit directed towards employment-intensive activities, developmental loans, public loan guarantees and improvement in coverage and administration of small-scale credit programmes may complement this policy (Heintz *et al.*, 2008)<sup>11</sup>. Another monetary variable, the exchange rate, has become the single most critical variable in determining the competitiveness of more open economies. It does not only influence the export sector, but also all tradable and even non tradable sectors. Macroeconomic policies can contribute to raise domestic productive activities and thus create new employment opportunities, but often these policies need to be sustained by structural and institutional changes to become effective.

20. Good institutions are also needed to ensure that economic growth is equitable. In many countries, high economic growth has often accompanied by a rise in inequality, but this need not be the case. Economic, wage, social and labour market policies that address distribution can ensure that growth is equitable. In Chile, for example, inequality was slightly reduced during the strong growth years of the 1990s because of a minimum wage policy and other social policies. Malaysia developed comprehensive positive discrimination policies to assure inclusive development. Income inequality was also reduced slightly in Brazil in the 2000s because the government increased social transfers and raised the minimum wage, thereby boosting the incomes of the poorest groups. However, in many other countries that have experienced economic growth, inequality increased, mitigating some of the benefits of economic growth for poverty reduction. For example, if inequality had not increased in Uganda between 1992 and 2002, the poverty rate would have been 8 percentage points lower (AFD, 2005).<sup>12</sup> Similarly, poverty reduction in China and India has been less than expected given their high rates of sustained economic growth, because growth has not been broad-based.

21. Historically, economic development has been driven by a push and pull of the labour force from the primary to the secondary sectors. Higher productivity in agriculture pushes workers off this sector and leads to them being pulled into new, more productive employment in manufacturing. Output and employment growth in the service sector come later. Although this pattern still holds for many developing countries, the service sector has gained in importance from the outset as a principal employer. Unfortunately the transition from agriculture to services has, in many cases, meant a transition from low-productivity agricultural jobs to low-productivity service jobs in the urban informal economy (ILO, 2005).<sup>13</sup> In 2006, the employment share of the service sector in total world employment, reached 40 per cent, overtaking for the first time the share of employment in agriculture, which declined to 38.7 per cent. The share of employment in manufacturing has remained steady, at 21 per cent, since the mid-1990s (ILO, 2007).<sup>14</sup>

### *Agriculture*

22. Alleviating poverty in the agriculture sector requires appropriate incentives for farmers, *i.e.* attractive prices, access to markets and effective implementation of land rights (or alternatively, the enforcement of property rights). Better income prospects and secure land rights encourage farmers to improve technology, boosting their productivity the more easily where extension and research are effective, and where farmers can access inputs and credit. Experience shows that education, health and infrastructure are further factors important for facilitating rural growth. Increased productivity will allow

the agricultural sector to shed labour for more productive and better paying work in manufacturing and services. Indonesia in the last quarter of the 20<sup>th</sup> century, China in the 1980s and Vietnam and Uganda in the 1990s are all success stories illustrating such growth and, in some cases, transition out of agriculture.

23. Thus, at the early stages of rural development, the issue in agriculture is not increased employment; major attention should be given to increased productivity, mainly a matter of vigorous demand and growth. Incidentally, the virtuous circle in Figure 2 should therefore be interpreted flexibly within the agricultural sector.

### *Manufacturing*

24. In many countries, including China, Costa Rica, Indonesia, Malaysia, Thailand and Vietnam, the development of labour-intensive export sectors has been a significant driver of economic growth. This sector was important for reducing poverty, since job creation was high, given the high output-employment elasticity of this type of manufacturing. Moreover, there were improvements in productivity as industries moved up the value chain, leading to increases in income and further reductions in poverty.

25. Asia's economic success since the 1970s has largely been based on a successful, export-led growth model; but this model is not easily replicated. In many Asian countries, certainly in Japan and Korea, and also in Malaysia and Singapore, the state has played an instrumental role in industrialization by protecting infant industries, as well as by providing subsidies on credit in these sectors. Many of these policies are not permitted under current WTO rules. Moreover, export-led growth has become "fashionable," meaning that many developing countries, not just in Asia but also in Latin America and Africa, have adopted export-led growth models. Unless the market for products is increased, countries will experience "diminishing returns to export-led growth," meaning that countries will only be able to expand their share in export markets, particularly for commodities, apparel and basic electronics, by displacing other developing countries (Blecker, 2000).<sup>15</sup> And if competitiveness is driven by unit labour costs, the benefits of this model to low-waged workers will be lessened. Nevertheless, if countries are able to use their comparative advantage to diversify into more competitive goods particularly by moving up the value chain and producing export goods that are more skill-intensive and thus quality based, then they will likely be able to sustain and enhance the benefits of export-led growth.

### *Service Sector*

26. Higher rates of world urbanization and a levelling of world manufacturing employment have meant that the service sector has come to dominate global employment. While, at 72.7 per cent, the share of employment in developed countries is much higher than in the developing world, services nevertheless constitute an important employer in many parts of the developing world. In Latin America and the Caribbean, 61.4 per cent of workers were engaged in services; in the Middle East and North Africa the figure was 47.4 per cent and in South Asia, it was 29.5 per cent in 2006, up from 25.3 per cent in 1996.

27. In some developing countries, the service sector has become a leading driver of economic growth. In India, economic growth from 1994-2005 was driven by an unprecedented expansion in service exports. India has capitalized on its large pool of educated, English-speaking people to become an important outsourcing destination for multinational corporations. Another important contributor to economic growth for many developing countries is the tourism sector. However, the service sector also contains many less skilled occupations that are important for absorbing surplus labour, but that do not typically drive economic growth; these include petty commerce and personal services.

## **2. Productive capacity**

28. The strengthened capacity of the poor to take advantage of opportunities is a main avenue for reducing income poverty and achieving pro-poor growth. A high degree of employability and labour market access for the poor is needed, in order to turn structural change into opportunities to escape poverty.

29. The presence of a well educated labour force in Costa Rica, Malaysia and India was important for attracting investment in relatively skill-intensive industries. Costa Rica and Malaysia, in particular, have based their social and economic development on inclusive policies, guaranteeing universal access to primary education and encouraging secondary education. Education is the largest item in Malaysia's federal budget. Primary education is compulsory, and both primary and secondary education is free. Malaysia's literacy rate is 93 per cent. Costa Rica instituted public and mandatory primary education at the end of the 19<sup>th</sup> century and constantly ranks as one of the highest spenders on social policy in Latin America. For these countries, it is not simply that economic growth has led to greater incomes and thus greater investment in education, skill formation and health, but also that earlier investments in education and health facilitated economic growth, so increasing opportunities for work and incomes and subsequently facilitating poverty reduction. An additional benefit of this strategy is that their gains are more likely to be sustainable, as competition is not limited to the cost of labour.

30. Appropriate education may not only be able to improve agricultural productivity, but might also ease the transition of workers from agricultural jobs to work in the secondary or tertiary sectors. Industrial jobs require a higher level of education than agricultural work. Most assembly work requires a basic education and sometimes completed secondary education as well. For example, in Bangladesh, rural unskilled workers were not hired by manufacturing firms because they lacked the skills needed for industrial work (Winters, 2002).<sup>16</sup> A well-functioning vocational development programme can also help the poor benefit from new growth opportunities. In many instances, education systems do not provide adequate preparation for informal work (the case in most sub-Saharan African countries) or for formal work (the case in South Africa, where 500,000 formal jobs remain vacant). Vocational training systems are often inadequate in size and not particularly relevant to the needs of the labour market. Improving and extending vocational training can facilitate transitions to more productive work. In addition, close cooperation and exchange of information between training institutions and companies is essential to guarantee the matching of labour supply and demand.

31. Physical capital is also important for unleashing productive capacity. Inadequate physical infrastructure, resulting in high transport costs and inefficient systems for disseminating market information, are main causes of the poor geographical integration of the economy. This also tends to result in a concentration of growth in the main cities and centrally located areas, and to aggravate spatial inequality. Investments in physical infrastructure in rural areas can improve labour productivity in rural industries, including agriculture. In Indonesia, for example, part of the reason for the growth in agricultural output during the 1970s and 1980s was because, through the Padat Karya programme, a labour-intensive infrastructure development programme, the government invested in developing rural infrastructure, including schools and health clinics, as well as in the construction of roads and irrigation systems. Thus the poor were able to benefit, not only because growth was in rural areas, but also because of their enhanced ability to participate in growth through greater productivity and better access to resources and opportunities (McKinley and Khattry).<sup>17</sup> Lacking access to credit for small and micro enterprises is another important barrier for poor workers. It hampers the rise in the productivity of their activities and the general development of their businesses. Briefly, a good combination of social investment- education and vocational training on the supply side - and productive investment - infrastructure and financing on the demand side - has to be found, in order to enhance the employment opportunities of poor workers and to empower them.

### ***3. Employment with Rising Productivity***

32. Employment with rising productivity is the critical link in the growth-employment-poverty nexus. Rising economic growth results in poverty reduction when the productivity of poor workers increases, either in their current occupation, or in new jobs or opportunities for self-employment.

33. Most countries that have experienced high rates of sustained economic growth benefit from both the creation of additional jobs, as well as rising productivity though overall productivity increases, are typically more important. For example, in Vietnam during the 1990s, the average annual employment growth rate for the economy as a whole was approximately 2.7 per cent whereas labour productivity grew by 4.8 per cent annually (Packard, 2005).<sup>18</sup> Similarly, in Indonesia during the economic boom of 1987-1996, overall growth in employment was 2.2 per cent annually whereas real wages, a proxy for labour productivity, increased by 7.2 per cent annually (Azis, 2005).<sup>19</sup> These findings are not surprising. In developing countries, most workers are employed, although the prevalent forms of employment are self-employment and casual wage employment in the non-formal segment of the labour market. Labour force surveys report these individuals as working, even if they are grossly underemployed in terms of hours worked, or income received. If economic growth leads to a rise in job opportunities in the more productive sectors of the labour market and previously underemployed workers find jobs in these more dynamic sectors, the shift in employment will not be counted as an additional job created, even though in terms of economic development and individual well-being, the transition to work in the more productive sector is very important. Similarly, strong economic growth can increase the demand for the services provided by self-employed workers, leading to an increase in their income.

34. Table 2 is a comparison of the relative importance of jobs versus incomes in 10 countries that reduced poverty successfully. For most of the countries, it appears that the increase in incomes stemming from productivity growth was more important for the reduction in poverty than the additional jobs created from economic growth. In China and Vietnam, net job creation was lower than expected because of job losses stemming from the restructuring of state-owned enterprises. For this reason, China's net job creation is reported as "not important," even though job growth in labour-intensive export sectors was quite important.

**Table 2. Sources of Poverty Reduction: Jobs or Incomes**

	Job Growth (net effect)	Increase in Incomes (productivity growth)
Brazil	0	+
Chile	+	++
China	0	++
Costa Rica	+/0	+
India	0	+
Indonesia	+	++
Malaysia	+	++
Thailand	+	++
Uganda	0	-
Vietnam	+	++

++ very important; + important; +/0 mildly important; 0 not important; - not known

Source: Based on Islam (2006).

35. Nevertheless it is important to bear in mind that Table 2 is merely a general indicator of the relative importance of jobs versus incomes, suggesting broad orders of magnitude. For different periods, the relative importance of some of these indicators may be different. For example, net job creation was very important in Malaysia in the first half of the 1990s. In general, the most important conclusion is that for most developing countries, it is not so much the additional jobs created, but the transition from low-productivity to high-productivity jobs that is most important for the reduction of poverty.

36. In a growing economy, output-employment elasticities (OEE), which denote the rate at which employment grows when output increases by one percentage point, are not the same for all sectors, nor would they change in the same direction over any given period of time. Over time, the OEE for agriculture declines and may even become negative. As the OEE for agriculture declines, labour absorption in industries and services must be rapid enough for the overall employment growth to exceed the growth of the labour force.

37. Indeed, East Asia's success in poverty reduction was characterized by high rates of growth coupled with high OEEs in manufacturing and modern services (Khan, 2007).<sup>20</sup> Although recent economic growth rates in China and India have exceeded East Asia at its peak, they have not had as much success in reducing poverty mainly because of lower OEE in the growth sectors (for example, between 1991-2003, China had an OEE in industry of 0.07 due mainly to the restructuring of state-run manufacturing enterprises). In India, the high growth sector has been IT, which is a relatively low labour-intensity industry. Similarly, Ghanaian workers have not benefited from the relatively high and steady economic growth rates experienced in the country since the mid-1980s. Growth in Ghana has been based largely on exports of low value-added cocoa and gold, which have a low employment intensity, whereas high labour absorption sectors, such as manufacturing, tourism and food crop activities, have experienced slow growth (Aryeetey and Baah-Boateng, 2007).<sup>21</sup>

38. Although labour intensity is important for reducing poverty, it matters where the intensity takes place. A recent cross-country empirical study on the role of employment intensity and productivity in reducing poverty found that increased labour intensity in manufacturing is highly correlated with poverty reduction (Gutierrez *et al.*, 2007).<sup>22</sup> Yet the opposite was true for the agricultural sector. In fact, increased labour intensity in agriculture was associated with an increase in poverty. Rather than attracting workers to new opportunities, the agricultural sector acts as a refuge for displaced workers. Therefore, policy interventions should be targeted at: (1) increasing employment in the secondary sector; (2) increasing productivity in informal activities, in particular in agriculture; (3) increasing access to secondary sector jobs.

#### **4. Higher Income of the Poor**

39. New opportunities in the labour market and in self-employment can raise the earnings of the poor, so allowing the virtuous circle to continue. Greater income leads to greater purchasing power of the poor, which stimulates the demand for goods and services, leading to additional opportunities for self-employment and waged work. With greater disposable income, poor households can make productive investments that can improve the viability of their businesses, or allow them to engage in new entrepreneurial activities.

40. A common characteristic of the poor is that they perform multiple jobs, often combining waged work with entrepreneurial activities, or sometimes undertaking several entrepreneurial activities. In Peru, 69 per cent of households living under USD 2 a day in urban areas operate a non-agricultural business. In Indonesia, Pakistan and Nicaragua approximately 50 per cent do. A large proportion of the rural poor run farms and many of the rural poor also run a non-agricultural business. And yet these workers generally perform several activities in addition to running their business, possibly because they cannot raise enough capital to run a business that would occupy them full-time. For example, a poor farmer may only be able to work the land she owns for part of the year because she lacks access to funds that would otherwise allow her to irrigate the land and make it useable for a larger part of the year (Banerjee and Duflo, 2007).<sup>23</sup>

41. The businesses of the poor operate on a remarkably small scale, usually with no paid staff and minimal assets. The smallness of scale hampers efficiency. When the incomes of the poor increase, they are able to make investments in their businesses that can improve their long-term viability and revenue potential. Moreover, these investments, if based on local inputs, can further stimulate the local economy. Similarly, when the incomes of waged workers improve, there are multiplier effects on the local economy, through additional household purchases.

#### **5. Greater Investments in Health, Education and Infrastructure**

42. With the increase in income that accompanies economic growth, governments and individuals acquire the means to finance further investments in health, education and skills development, as well as in the physical infrastructure. The additional income also allows governments to finance increased transfer payments, which reduce income poverty, as well as its other dimensions.

43. Economic growth enables countries to increase spending on education and health, which, in turn, helps economic growth. In Mozambique, total public spending doubled between 1992 and 2004, aided as well by an increase in external financial support. The investments increased the educational attainment of the labour force and were estimated to have contributed to close to 14 per cent of economic growth from 1999-2004 (Virtanen and Ehrenpreis, 2007).<sup>24</sup> Similarly, social spending in India was found to promote economic growth, as well as reduce poverty. A study of the effects of socio-economic security expenditure policies (sickness, maternity benefits, employment injury, invalidity and death compensations, medical care and subsidies for families with children) on Indian's economic performance between 1973 and 1999 for a panel of 14 Indian states found that policies that strengthened the social and economic security of the Indian population were an important endogenous variable to both the reduction of poverty and economic growth (Justino, 2007).<sup>25</sup>

44. In Brazil, social policies have played an important role in reducing poverty in the 2000s. Brazil is a relatively rich country, but has a highly inequitable distribution of income. To decrease poverty, the government has enacted a number of social transfer programmes, most significantly the *Bolsa Familia* programme, a conditional cash-transfer programme targeted at poor and extremely poor households, and also an old-age pension. The pension is tied to the level of the minimum wage, so by raising the minimum wage, which the government did, the incomes of pensioners rose, as did the incomes of low-wage workers.

Several studies have shown its positive impact on poverty and inequality reduction. Moreover, it enhanced economic growth, especially in the north-east of Brazil, where a large proportion of the poor workers live.

45. Critics of conditional cash transfer programmes allege that the programmes exert a negative affect on labour market participation. However, studies of these programmes in Brazil and South Africa show that the programmes increase the participation of adult workers in the labour market, while at the same time reducing child labour and increasing school enrolment. In Brazil, the participation rate of adults in the Bolsa Familia programme was 2.6 percentage points higher than similar non-participants, and 4.3 percentage points higher for women (Veras Soares *et al.*, 2007).<sup>26</sup> Similarly, research for South Africa shows that for the lowest-income households, social grants had a positive and significant impact on labour market participation and the probability of finding employment (Samson, 2007).<sup>27</sup>

46. Another important social and labour market policy that has benefited incomes, employment and infrastructure are public works programmes. India has a long history of using employment guarantee schemes to provide income relief to the poor and to build needed infrastructure. The employment guarantee scheme of the Indian state of Maharashtra was introduced in the 1970s and is one of the largest public work programmes in the developing world. It guarantees employment to all adults older than 18 years of age, who are willing to do unskilled manual work on piece rates. The scheme has been successful in targeting the deserving segment of the population and in building rural infrastructure (Dev, 1995).<sup>28</sup> In 2004, the Indian government announced the creation of a National Rural Employment guarantee programme (NREGA) guaranteeing 100 days of employment in public works. This programme is projected to cost 1-2 per cent of GDP.

47. Many of these social policies have important multiplier effects on the local economy. For example, a December 2004 evaluation of a cash transfer programme in Zambia covering the poorest 10 per cent of households in 143 villages and five townships found that the local economy was stimulated through the purchase of food, soap and blankets, as well as agricultural inputs (Farrington *et al.*, 2005).<sup>29</sup>

## **6. Empowering the poor**

48. In countries where the majority of people are poor, national economic growth will remain sub-optimal unless the potential of the poor majority can be unlocked through inclusive policies and social protection mechanisms. These policies are needed to help the poor manage the unexpected hardships that life brings them. Few self-employed and informal waged workers benefit from social protection policies designed to protect workers from the risk of accidents, unemployment, poor health and old age. These are just some of the most pressing risks that the poor face, but which can be mitigated through social protection. Surveys of the poor in developing countries reveal a remarkably high level of morbidity. Among the rural poor living under USD1 a day in Peru, South Africa, East Timor, Panama, and Tanzania, between 11 and 15 per cent of households report having a member either being bedridden for at least a day or requiring a doctor. In Pakistan, Indonesia and Ivory Coast, the number is between 21 and 28 per cent and in Nicaragua, Udaipur, India and Mexico (Banerjee and Duflo, 2007),<sup>30</sup> between 35 and 46 per cent.

49. When the poor come under economic stress, they often respond by eating less, or taking their children out of school. According to a household survey in Udaipur, India, in 45 per cent of the extremely poor households (living on less than USD1 a day) and in 35 per cent of households (living on less than USD2 a day), the adults had had to reduce the size of their meal at some point during the preceding year and in 12 per cent of them, children had had to reduce the size of their meal (Banerjee and Duflo, 2007).<sup>31</sup> Moreover, large expenditures on health are typically financed through borrowing, usually at very high interest rates.

50. Selling assets, depriving children of schooling and health services, or taking out high-interest loans negatively affects the future well-being of the household and can lead to permanent and debilitating levels of poverty. Studies focusing on the decision-making of poor families and individuals have shown that, in order to reduce their vulnerability to unmanageable risks, poor households often engage in low productivity and low profitability business and livelihoods. A reduction in risks faced by the poor and the availability of reliable social protection instruments can help to stimulate growth by encouraging people to engage in higher risk, higher profit activities (Voipio, 2007).<sup>32</sup>

51. And so, besides providing much needed services, social protection reduces vulnerability to risk, thus facilitating the engagement of the poor in the labour market. Producing new crops, undertaking entrepreneurial activities, investing in a business and taking advantage of opportunities in new areas all involves taking risks, which the poor are more likely to accept if the risks of accident, sickness and death are mitigated.

52. *Promoting women's engagement in the labour market.* Inequality of assets and opportunities hinders the ability of poor people to participate in, and contribute to, growth. Gender is an important dimension of inequality, as women face barriers concerning assets, access and participation in the growth process, all of which impede the progress of pro-poor growth.

53. The labour market for poor women tends to be gender-segregated, which precipitates a number of efficiency losses that can mitigate growth and compound income inequality. Competent female workers are excluded from some of the more productive activities, resulting in welfare losses for society. Gender-segregated labour markets are also associated with higher gender wage inequality, which distorts investment in human capital, prioritizing male income earners and under-capitalizing women earners. Substantial evidence suggests that occupational segregation is associated with less security in employment for women and fewer prospects for promotion. These outcomes are likely to compound the inter-generational transmission of poverty, particularly for women and girls. In order to gain a better understanding of how women and girls fare in the labour market, a gender analysis is needed, thus data must be disaggregated by sex. Labour laws against discrimination (employment, work, wage-setting) and policies to promote women's employment (e.g. affirmative action, work & family support) in general, as well as in underrepresented sectors, can aid in dismantling this unwelcome feature of labour markets.

#### **IV. Supporting the Virtuous Circle through Labour Market Institutions and Policies**

54. Ensuring that growth is pro-poor requires that the growth-employment elasticity is high, as employment is an essential ingredient in the fight against poverty. For achieving such a high elasticity, not only must growth come from the right mix of sectors, but it requires also institutions, policies, laws and practices that positively affect the functioning of labour markets. A well-functioning institutional environment can support the virtuous circle and, in the process, facilitate pro-poor growth. Indeed, as the previous discussion on the components of the virtuous circle illustrates, institutions feature prominently in the virtuous circle, including state-provided health and educational institutions, poverty alleviation programmes, labour market policies, and social security.

55. Labour market institutions affect the workings of the labour market, which, in turn, influence patterns of job creation, as well as working conditions. Labour market institutions exist in both developed and developing countries, and include not just labour laws but also informal rules and practices, as well as government policies, particularly labour market policies. The distinction between developed and developing countries lies in the degree to which labour market institutions are embedded in law, whether the law is applied in practice and the extent that labour market policies are used as a tool to pursue certain objectives. National labour laws are sometimes a 'formalization' of what already occurs informally, but they are also a remedy to correct the bargaining power disadvantage that workers have *vis-à-vis* employers.

Legal statutes (on, for example, maximum hours, vacations, minimum wages, health and safety regulations), as well as laws protecting freedom of association and collective bargaining, which are considered process rights, serve to strengthen the bargaining power of workers.

56. *Labour Market Flexibility.* Labour market institutions are instrumental in improving social justice and, as such, can be an effective tool in promoting pro-poor growth. Yet despite this instrumental role, an important debate has arisen on the effects of labour institutions on economic performance, and whether greater 'labour market flexibility' is needed. Many aspects of labour market flexibility, such as labour mobility and functional flexibility,<sup>33</sup> are desirable and worth promoting. In practical terms, however, the debates on labour market flexibility have focused on a very specific set of institutions: employment protection legislation, unemployment insurance, the regulation of working time and working arrangements, minimum wages, as well as the role of unions and collective bargaining. Many of the world's poor, particularly those living in rural areas and engaged in agriculture, are informal workers who fall outside the scope of these institutions.

57. It has been argued that protective labour institutions impede the workings of the labour market, creating market inefficiencies that lead either to unemployment, or in developing countries, to informality. This reasoning is based on an abstractly conceived theoretical labour market, defined by an upward sloping supply curve and a downward sloping demand curve for labour. Under conventional supply and demand analysis, jobs are allocated in a fair exchange between two equal parties that, unrestricted, will result in full employment. But this framework does not incorporate the recognized inequality in bargaining that prompted the creation of labour law, or the effect of social norms on the workings on the labour market or, at the macro level, the possibility that there is insufficient demand in the economy.

58. The importance of labour market institutions for facilitating employment, income growth and poverty reduction has been varied. China, for example, dismantled employment protections by introducing new labour laws facilitating hiring and firing, by eliminating the bureaucratic labour allocation system and by wage reform. These policies were important in spurring industrial growth, particularly in private town and village enterprises. In Chile, on the other hand, the strengthening of labour market institutions following the return to democracy in 1990 contributed to the rise in incomes of low-waged workers that not only improved their standard of living, but also increased aggregate demand in the economy. During the 1990s the government raised the minimum wage at an annual average rate of 8 per cent, contributing to a reduction in poverty among low-earning workers. Moreover, unemployment continued to decline throughout the decade. Nevertheless, income inequality has fallen little in recent decades and remains one of the highest in the region.

59. *The Importance of Social Dialogue in Designing Policies.* The participation of employers' and workers' organizations in designing institutions and policies to improve the smooth running of the labour market and poverty reduction is instrumental. Indeed, a working social dialogue is not only an end for democratic governance of the labour market, but also for society in general, as it improves the participation of various groups of society in decision-making. Social dialogue can contribute to the effective formulation of regulations and policies for achieving employment intensive and pro-poor growth.

60. Social dialogue requires strong independent trade unions and employers' organizations, with technical capacity and access to relevant information. It also requires political will and commitment and a respect for the fundamental rights of freedom of association and collective bargaining. The state has an important role in creating stable policies and a climate conducive for social partners to operate freely, without fear or reprisal.

61. There are many examples, in both developed and developing countries, of how social dialogue has been effectively used to improve the performance of the economy and the labour market and facilitate

quality job creation. Having an effective mechanism in place for social dialogue at the national level can be a competitive advantage for countries, particularly during times of economic restructuring or downturn. Singapore's relatively rapid adjustment to the Asian financial crisis with minimal job loss is a case in point. Rather than lay-offs or wage cuts, the solution of choice was to relieve employers of a share of their non-wage labour costs. Enterprises thereby received some relief in their labour costs, while the retention of jobs and earnings propped up aggregate demand in the economy. Similarly, national social dialogue in Barbados in the 1990s focused on surmounting economic crises while minimizing lay-offs and social hardship. The social partners and government agreed to focus on competitiveness and productivity, to accept wage freezes until corresponding productivity gains were achieved, and to retain jobs. At the macroeconomic level, tripartite social dialogue is often used for setting national wage policies, including the minimum wage, to ensure that wage increases match productivity growth in order to establish macroeconomic conditions that facilitate job growth. Also, during times of economic change or uncertainty, social dialogue can be instrumental in making job retention and job creation a priority for governments and social partners. In addition, social dialogue can also be very helpful in the implementation of labour market policies, such as vocational training.<sup>34</sup>

62. In many developing countries, however, traditional labour market institutions and social dialogue are relevant for only a limited number of workers employed in formal activities. The employment structure is different from developed countries with a dominant share of casual and self-employed workers, who are in general not reached by these traditional institutions. However, there are exceptions. Non-traditional institutions such as SEWA, the Self-Employed Women's Association in India, have emerged to respond and address the labour market concerns of self-employed women workers. Similarly, the ASA, in the semi-dry region of north-eastern Brazil, is an NGO network that supports small farmers. Another prominent example comes from Kerala, India, where the issue of social security has been a core concern of informal workers and has given rise to the institution of welfare funds as a result of social dialogue between labour unions, representing informal workers, and employers mediated by the State. The State plays a leading role in the initiation and management of welfare funds and contributions are either bipartite (workers and employers) or tripartite, also including the State. The welfare fund is modelled on the social security system and insurance coverage available to formal workers and each fund is managed by a tripartite body.

63. *Labour Market Policies.* Labour market policies (LMPs) provide income replacement and labour market integration measures to those looking for jobs, usually the unemployed, but also the underemployed and those in employment who are looking for a better job. So-called "passive" policies provide replacement income during periods of unemployment or during the job search. They correspond to social transfers that are not conditional upon joining a training or work programme, although they usually include job search provisions that are increasingly enforced and correspond to an active element in passive policies. Typical passive programmes are unemployment insurance, unemployment assistance and early retirement, which should be the ambition of all countries in the long run. Nevertheless, a broader approach to social protection, which is targeted specifically at poor workers in the informal sector, is needed in the medium-term, particularly in developing countries. It could include targeted cash benefits, free access to basic health and child care (e.g. SEWA in India), universal basic old age and disability pension, livelihood promotion, assistance in forming cooperatives, as well as improved access to assets or micro insurance schemes. The goal is to stabilize income and thus improve the income security of the working poor.

64. "Active" policies refer to labour market integration through demand or supply side measures. Hence the main thrust of active labour market policies (ALMPs) is active support for labour market integration. They are explicitly contingent upon participation in programmes that enhance labour market (re)integration. ALMPs support employment creation in two basic ways: directly by job creation measures (e.g. public works and enterprise creation, as well as hiring subsidies); and indirectly by improving employability through training, and by ensuring efficient labour exchanges that provide better labour market information and enhanced job matching. Active policies are usually targeted at specific groups

facing particular labour market integration difficulties, such as younger and older people, women and those particularly hard to place, such as the disabled. In part, ALMPs are also an answer to the growing critique that pure income replacement policies might entail disincentives to work once unemployment becomes more long-term.

65. Active as well as passive LMPs intermediate between supply and demand in the labour market. Indeed, the primary economic function assigned to LMPs is the matching of labour demand and supply. The impact of LMP intervention on labour supply and demand can vary. Such policies either contribute directly to matching (public and private employment services, job search assistance, prospecting and registering vacancies, profiling, providing labour market information), or enhancing supply (*e.g.* training and retraining), reducing supply (*e.g.* early retirement), creating demand (public works, enterprise creation and self-employment) or changing the structure of demand (*e.g.* employment subsidies), for example in favour of disadvantaged groups.

66. LMPs also have indirect positive macroeconomic effects by propping up or stabilizing aggregate demand, thereby smoothing consumption during economic downturns. There are also positive spill-over effects of infrastructure creation, for example, from public work schemes.

67. *Developing policies and institutions to benefit from migration.* Roughly three per cent of the world's population live outside their country of birth. Referring back to the virtuous circle of Figure 2, migrants look for higher productivity and thus higher wage or income employment abroad, as they have serious difficulties in finding it in the domestic labour market. Migrants from developing countries working abroad affect their home country labour markets through several channels: (1) by potentially having an impact on local wages by lowering labour supply in their home country; (2) by migration of skilled workers which can result in "brain drain;" (3) through the remittances<sup>35</sup> they send; (4) through the formation of diaspora networks; and (5) from the effects of return migration. International migration can be beneficial for poverty reduction, depending on the characteristics of these channels, as well as the policy and institutional environment that is created to support its beneficial aspects. Employment policies should take into account potential migration. To be effective, migration policies ought to be holistic and integrate the views and interests of sending and receiving countries.<sup>36</sup>

## **V. Policies to Address the Challenge of Fragile States**

68. Fragile states, many of which have emerged from conflict situations and are in danger of renewed conflict, require special efforts to compensate for the absence of a functional government, the need to redefine the 'rules of the game' and the physical and social aftermath of violent conflict or neglect of specific groups or regions in the country.

69. Employment creation should be a cornerstone of donor assistance in fragile states and should not be relegated to the backburner as an issue that can only be addressed as humanitarian assistance is being phased out and democratic governance reinstated. One of the major characteristics of fragile states is the absence of equal opportunity for gainful employment, often leading to increased fragility. Inequality is also one of the major factors leading to instability, while the effects of economic decline draw more and more people into poverty. The long-term vision for international engagement in fragile states is to help national reformers build effective, legitimate and resilient state institutions that promote sustained development. The three main and intertwined areas of intervention identified by POVNET are: (1) restoring the legitimacy of government; (2) creating employment and improving welfare; and (3) improving equity. However, short-term measures are also needed to fill the gap. Rebuilding the state, especially after a period of economic decline and instability, is a long-term effort. In the meantime, basic needs must be met and people, especially the poor but also returnees and ex-combatants, need to be reintegrated into economic activity and social reconstruction efforts.

70. Labour-intensive public works programmes, micro-credit programmes and public private partnerships to provide basic services are examples of initiatives that can be undertaken in the short-term. Nevertheless, these measures need to be complemented with longer-term initiatives aimed at rebuilding institutions to sustain economic growth and recovery. It is now also recognized that there is a huge, and largely untapped, potential to engage the domestic and international private sector in efforts aimed at economic recovery, even while more substantive efforts are being made to create an enabling environment for sustainable and equitable economic growth.

71. A consensus is emerging to direct investments in the following areas:

- Engaging governments in a political dialogue on issues of: (i) putting in place a legal and regulatory framework, in which equity of access to productive resources and employment opportunities are prioritised; (ii) ensuring that smart investments are made to assist marginalised groups and regions in gaining access to productive resources, remunerative economic activities and markets; (iii) contributing towards capacity-building of governmental and non-governmental institutions to further promote employment and labour market policies.
- Collaborating with the private sector, at both the local and the international level, to create new employment opportunities with a particular focus on marginalised groups and regions.
- Supporting trade unions and employers' organisations to put the interests of the poor on the agenda and lobby government to adopt policies and programmes that will create employment opportunities for marginalised groups and regions.
- Pro-active involvement of the donor community in promoting the decent work agenda and fair trade.

72. There are no simple recipes to deal with fragile states; in a country like Afghanistan there is sufficient scope for multinational companies to operate, whereas in a small country such as Burundi, with few resources, a more bottom-up approach involving employment opportunities within the communities has more impact. In most cases, a tailor-made solution needs to be found; this must be based on simple and rapid diagnostics and a willingness on the part of government and the international community to engage. With the increased involvement of multilateral institutions, international NGOs and some bilateral donors in fragile states, there is a growing awareness that millions of poor people are the real victims of unwilling and repressive governments, as well as neglect on the part of the international community. Recent studies have shown that gainful employment can reduce vulnerability, whereas humanitarian assistance alone not only creates dependency, but is also in itself a recipe for disaster if no action is taken to provide gainful employment and equitable access to productive resources while the 'new' government, or governing bodies, are investing in longer-term economic recovery.<sup>37</sup>

## VI. Employment as the route out of Poverty: Developing new policy approaches<sup>38</sup>

73. The development community recognizes that creating more productive jobs is central to achieving the MDGs, particularly the target of halving income poverty. Achieving full and productive employment and decent work for all, including women and young people, has now been included as an additional MDG. However, increasing employment and improving the quality of work for the poor is a challenge that can only be tackled through a package of policy interventions that address both demand and supply constraints in the labour market, and the interaction process of both sides. A range of policy interventions is needed, but for these interventions to have the greatest policy impact, it is important that they be well integrated, coordinated and monitored.

74. International donor efforts in the area of employment need to be coordinated in line with the Paris Declaration. Country involvement is critical. Indeed, a core principle of the Paris Declaration is that donor activities must be aligned with national development strategies, among them the PRSPs. Thus, integrated approaches for employment promotion need to be framed by national employment strategies, or be part of the national development strategy, and these need to be based on reliable labour market information. The design of employment promotion measures necessitates multi-stakeholder involvement, including the active involvement of the government, workers' and employers' organizations and civil society. Particular efforts may be required to ensure that the voices of informal workers and entrepreneurs, as well as those of women and ethnic minorities, are heard. To ensure the active involvement of these groups, new platforms for debate could be developed and innovative forms of involving informal workers in already existing workers' and employers' organizations promoted. Alternatively, the latter could provide technical assistance to create similar organizations in the informal sector. The Self-Employed Women's Association (SEWA) in India is a good example of a trade union coming from the informal sector. Groups such as these help to ensure that policy design reflects the concerns and desires of the country, which will support the institutionalization of policies and improve their chances of success. Improved donor cooperation will mitigate the duplication of efforts and ensure complementary approaches.

75. But recognising the importance of integrated efforts does not mean that donor agencies cannot concentrate on specific interventions within the virtuous circle, based on their specialization. Given the recognized need to increase productivity of workers in developing countries, some donors emphasise the importance of skills development to enhance the employability of the poor and improve their chances of finding wage employment and thus escape from income poverty. To the same extent, easing access to productive assets, such as land or capital, is pursued as a way of generating more productive self-employment opportunities. Recent research conducted by the French Development Agency<sup>39</sup> showed that these interventions have more sustainable employment outcomes when they are implemented together. Also, many agencies support business development programmes via policies to expand existing businesses or foster self-employment and entrepreneurship. Policies that support social protection, as well as empowerment, are complementary to these approaches as they can improve the employability of those women and men living in poverty, and help them to undertake more proactive and rewarding livelihood strategies.

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<sup>3</sup> G. Mwabu and E. Thorbecke (2007) "Poverty, Inequality and Labour Markets in sub-Saharan Africa," *Poverty in Focus*, International Poverty Centre, Brasilia, March.

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## **UNDERSTANDING THE RELATIONSHIP BETWEEN ECONOMIC GROWTH, EMPLOYMENT AND POVERTY REDUCTION**

Katy Hull

### **Key messages**

- Growth in one sector of the economy will not automatically translate into benefits for the poor: much will depend on the profile of growth (its employment- or productivity-intensity), the sectoral location of the poor, and the extent of mobility across sectors.
- For employment-intensive growth to translate into poverty reduction it must occur in a “more productive” sector, while “less productive” sectors may require productivity-intensive growth to ensure a decline in headcount poverty.
- Country-specific quantitative and qualitative analysis is required to identify constraints to job creation, productivity and mobility and to ensure that the poor are able to participate in more and better job opportunities.

### **I Introduction**

1. Whether they are subsistence farmers, salaried workers, or self-employed entrepreneurs, poor people derive most of their income from work. This basic fact means that the level of employment, the quality of jobs, and the access which the poor have to decent earnings opportunities will be crucial determinants of poverty reduction. The intuition that jobs matter for development has not been lost on the governments of low income countries and the vast majority of national development strategies look to employment generation as a major channel for poverty reduction.

2. Despite the intuitive notion that employment matters for poverty reduction, there is insufficient empirical research in this area. While there is a broad consensus that not all growth spells have the same impact on poverty, there have been relatively few attempts to systematically unpack the relationship between economic growth, employment and poverty reduction. Data deficiencies in many low income countries and the difficulty of ascribing causality to correlative relationships between changes in income and employment may each go some way to explaining the dearth of research to date.

3. What research there is both underscores the importance of jobs for poverty reduction and highlights the extent of the unfinished analytical agenda. Studies have demonstrated that the sectoral pattern of growth will affect the extent of poverty reduction: Loayza and Raddatz (2006) find that growth in unskilled intensive sectors contributes to poverty reduction; Satchi and Temple (2006) find that growth in agriculture may increase poverty while growth in the urban sectors may cause it to fall. But there remains a lack of consensus on which sectors are most important for poverty reduction or whether changes in employment or productivity will have the greatest impact. For instance, access to non-farm rural employment and informal urban employment emerged as important factors in some, but not all, of a sample of 14 countries which experienced pro-poor growth in the 1990s (World Bank 2005); and while

Coxhead and Warr (1995) find that increases in agricultural productivity reduce poverty, Fane and Warr (2002) detect only a meager impact.

4. This paper aims to bridge some of the gap between an intuitive understanding that jobs are crucial for poverty reduction and a lack of empirical research to demonstrate the nature of this relationship. Its objective is to provide policymakers and analysts with the tools by which to understand the interaction between growth, changes in both the number and the quality of jobs, and poverty reduction and to devise appropriate policy responses. Specifically, it aims to address the following three questions:

- How does the sectoral pattern of growth affect its poverty impact?
- Is employment-intensive or productivity-intensive growth more important for poverty reduction?
- What policies may facilitate the poor's participation in growth?

5. Since there is strong evidence to suggest that labour markets in developing countries are usually segmented between “more productive” and “less productive” jobs sectors, Part II provides an overview of theories on labour market segmentation. The goal is not, nor can it be, to provide a “one size fits all” model of segmented labour markets. Rather, it is to highlight some of the most common patterns of segmentation and its implications for the relationship between economic growth and poverty reduction.

6. Part III offers a three step framework for observing the relationship between economic growth, employment, and poverty reduction. The framework enables analysts to determine: first, the extent to which growth is associated with changes in employment (the quantity of jobs) or productivity (the quality of jobs); second, the relationship between these changes and poverty reduction, and; third, correlations with the broader policy and institutional environment. Part III demonstrates recent applications of each of these steps, while highlighting data challenges and the scope for future research.

7. As this paper's main objective is to bridge a gap between empirical research and policy, Part IV demonstrates how findings on the relationship between economic growth, employment and poverty reduction might inform policymaking. While appropriate policy responses will always be country-specific, Part IV draws on extensive country based analysis to demonstrate a range of potentially relevant policy options. These include measures to expand employment-intensive growth in “more productive” sectors, improve productivity of “less productive” jobs, enhance the mobility of the poor between sectors, and promote conducive policies and institutions, while paying due concern to political economy constraints.

## **II Labour market segmentation and its implications**

### ***Labour market segmentation in theory***

8. Labour markets in low and middle income countries tend to be highly segmented, with different wages and conditions of employment in each sector and limited mobility from “less productive” to “more productive” jobs. In contrast to basic neoclassical models predicting the equalization of wages, segmented labour market models predict that institutionally set wages (due, for example, to regulatory interventions or the bargaining power of workers) will ration “more productive” jobs. Since some workers cannot afford to remain unemployed, they will accept a “less productive” job in which earnings and/or conditions of employment are below the level set in the “more productive” sector. Box 1 provides a brief explanation of the various labels employed in the description of segmented labour markets.

**Box 1: “More productive” vs. “less productive” jobs, and other labels**

Models of labour market segmentation revolve around the identification of two or more distinct sectors. These sectors have received various labels. Some of the most common forms of distinction are summarized here.

**“Primary” vs. “secondary” sectors.** Dickens and Lang (1986) use the labels “primary” and “secondary” to distinguish between high-paying unionized jobs and lower-paying non-unionized jobs.

**“Insiders” vs. “outsiders.”** Knight and Yueh (2004) distinguish between “insiders” (urban dwellers) and “outsiders” (rural-to-urban migrants) in China. They find evidence that “insiders” positions remain protected against competition from “outsiders.”

**“Good” vs. “bad” jobs.** *Avirgan et al. (2005)* Use the labels “good” and “bad” jobs to distinguish between formal work and informal work in a number of developing countries, noting that earnings are consistently lower and working hours longer in the informal sector.

**“Upper-tier” vs. “easy entry” jobs.** Fields (2004) distinguishes between rationed “upper-tier” activities and almost unlimited “easy entry” activities, which cut across both the formal and informal sectors.

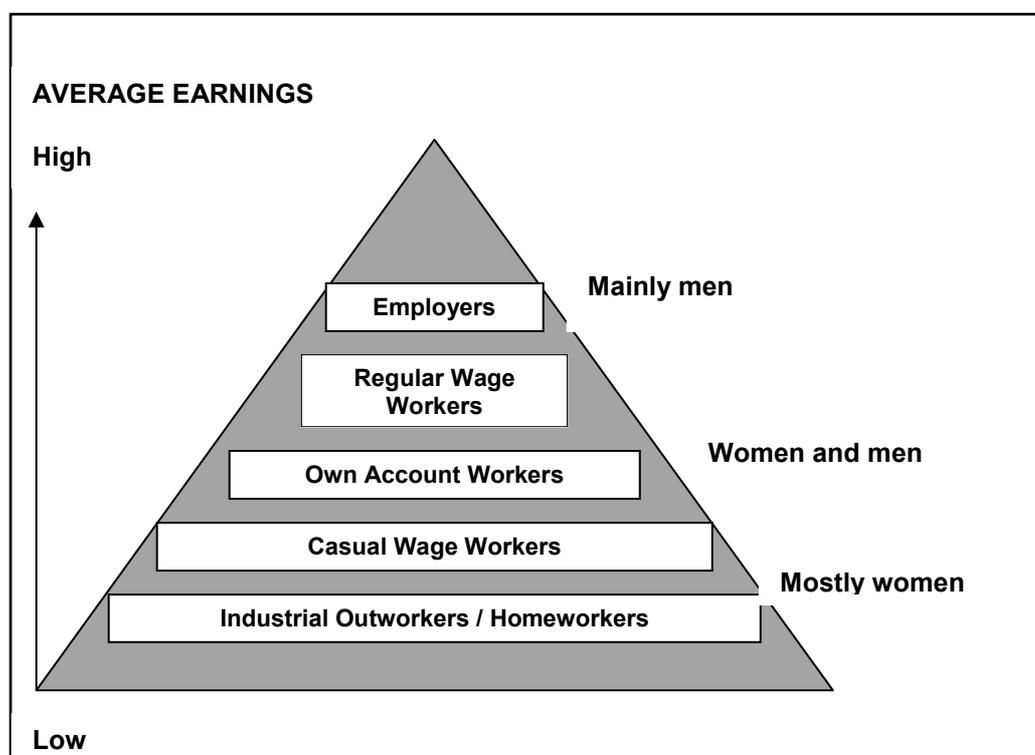
It should be noted that while this paper employs the labels “more productive” and “less productive,” this distinction, like all those summarized above, describes a single phenomenon: namely, the division of the labour market between jobs with good conditions and pay, which are limited in number, and jobs in which conditions and pay are generally much lower.

9. As one of the first to recognize the saliency of a segmented labour market model in developing countries, Lewis (1954) sought to explain “the workers on the docks, the young men who rush forward asking to carry your bag...and the like.” Lewis identified a dual labour market in which workers who were unable to obtain jobs in the formal sector took up work in a free entry, unregulated informal sector. While wages in the formal sector were kept at above market levels, those in the informal sector would fall as labour supply increased.

10. Recent revisions of the dual labour market model have challenged the notion of the informal sector as a free entry sector of last resort. Maloney’s research in Mexico (2003) suggests that some workers may choose between formality and informality on the basis of a rational cost-benefit analysis. Informal sector employers may feel compelled to offer terms and conditions of employment which are comparable to those in the formal sector so as to attract good workers and reduce turnover. Instead of representing a distortion-free sector, the informal sector will be subject to spillover effects of formal sector regulations.

11. Other responses to the standard dual model have asserted that it is insufficient to explain the “multi-faceted employment dynamics in developing economies” (Chen *et al.*, 2005). Suggesting that both the formal and informal sectors are subject to internal segmentation, these models draw attention to “upper tier” and “easy entry” activities in all sectors of the economy (Fields, 2004). They accept that both “more productive” and “less productive” jobs can exist in agriculture, in the urban formal sector, and in self-employment. Figure 1 characterizes a typical pattern of segmentation within the informal sector. Employers and wage workers occupy the “upper tier” of this sector: positions within this tier may be competitively sought after and actively preferred to jobs in the formal sector. Meanwhile, outwork and homework constitutes a free entry sector of last resort.

Figure 1: Segmentation of informal employment



Adapted from Chen *et al.* (2005)

12. Leonardi (1998) argues that while segmented labour markets are by now an “established fact,” it “remains to be proven” along what lines segmentation exists. The exact pattern of segmentation is of course context specific and cannot be dictated *a priori*. But while conceptions of dual or multiple labour markets will differ in their details, they share common features: the existence of two or more sectors with different wage setting mechanisms, with limited upward mobility for workers in the “less productive” sectors. In addition to the institutional barriers to mobility generated by the rationing of “more productive” jobs, there may be geographical barriers (for instance, poor infrastructure connecting urban and rural areas), legal barriers (such as weak enforcement of property rights), or barriers due to discrimination based on ethnicity, race or gender, which make it particularly difficult for the poor to participate in sectoral growth. Figure 1’s characterization of women as concentrated mainly in the “less productive” jobs tiers of the informal sector is all too familiar in many developing countries (Chen *et al.* 2005) and indicates that certain groups among the poor may face even greater barriers to mobility than their peers.

### ***Implications of labour market segmentation***

13. It is beyond the scope of this paper to establish the precise pattern of labour market segmentation in developing countries. Rather, the goal here is to highlight the likely implications of significant segmentation on poverty reduction (see Box 2).

### **Box 1. Implications of labour market segmentation**

Labour market segmentation has four principal implications for the relationship between economic growth and poverty reduction.

First, the overall rate of economic growth is likely to be lower under segmented conditions than in a fully integrated market, since bottlenecks inhibit the efficient flow of labour force participants between jobs.

Second, whereas the neoclassical labour market model would predict that an increase in labour demand in one sector of the economy will cause wages to rise across all sectors, labour market segmentation implies that factor returns will not equalize across sectors. In other words, growth in one sector may not have an effect on wages in other sectors of the economy. Segmentation indicates that for growth to impact the poor, it must occur in a sector in which they are located or to which they at least have access.

Third, growth that results in increased employment opportunities in “less productive” jobs sectors may not be enough to alleviate poverty. Since work in these sectors is characterized by low wages and/or poor conditions, a simple multiplication of similar opportunities will result in the expansion of underemployment and/or exploitation. On the other hand, growth which results in increased productivity in the “less productive” jobs sector may help to reduce poverty since it will help to raise wages, in effect bringing “less productive” jobs closer to the standards of “more productive” jobs.

Fourth, growth that results in an increase in the number and productivity of jobs may need to be accompanied by policies to enhance the mobility of the poor across sectors. Since barriers to movement can stem not only from the rationing of “more productive” jobs but from geography, infrastructure, and legal and cultural norms, the participation of the poor in growth will depend in part on concerted efforts to identify and remove these obstacles.

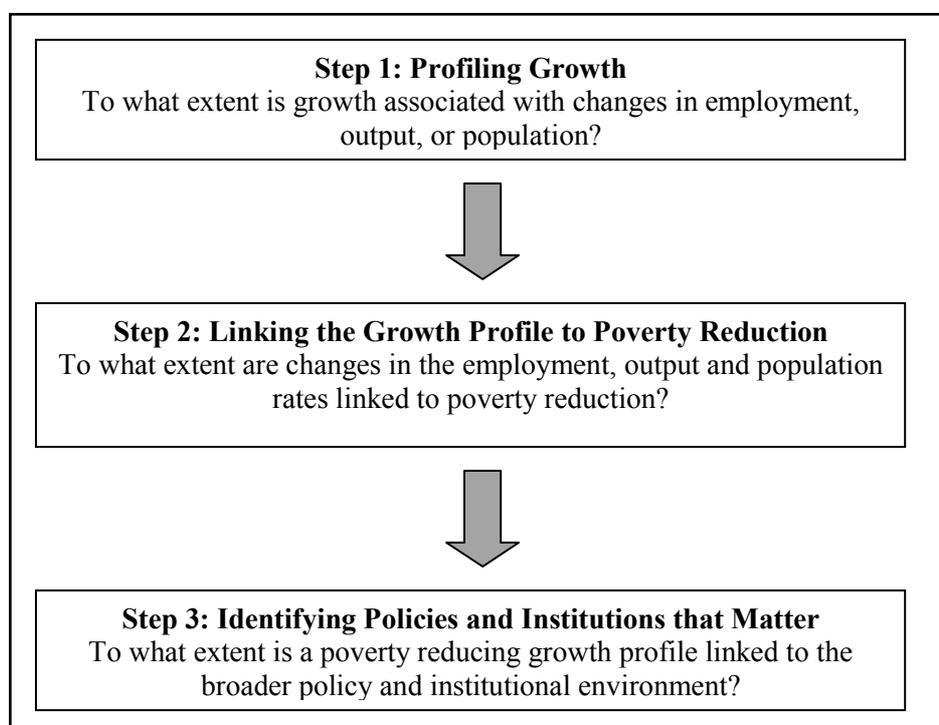
### **III A three step framework**

#### ***Objectives of the framework***

14. The objectives of the framework provided below are threefold. It aims to help analysts understand first, how the sectoral pattern of growth affects its poverty impact and second, whether employment-intensive or productivity-intensive growth is more important. Finally, the framework aims to shed light on the broader policy and institutional environment which might facilitate the poor’s participation in growth.

15. Alongside gaps in relevant data in many developing countries, the difficulty of assigning causality in the relationship between growth, employment and poverty reduction is probably a major reason for deficiencies in the current research agenda. A thorough analysis of the mechanisms by which the sectoral patterns of growth impact poverty would require a complex general equilibrium model. Such models risk stretching data beyond their limits and also pose immense challenges to analytical capacity.

16. Recognizing that the demands of general equilibrium models are often prohibitive in the context of limited data and capacity, the framework offered here is more modest. It provides analysts and policymakers with tools to observe correlations between employment generation and productivity growth, poverty reduction, and the broader institutional and policy environment. While correlations are of course not an indication of causality, this framework offers a pragmatic and feasible response to the absence of a thorough analysis of even correlative relationships in many countries. It can provide empirical input into debates on how the quantity and quality of jobs are linked to poverty. And it may help to stimulate discussion on the appropriate policies for enabling the poor’s full participation in economic growth.

**Figure 2: The three step framework**

17. The framework provides three stages of analysis. First, it decomposes economic growth into changes in both the quantity *and* quality of jobs. Second, it ascertains whether improvements in employment or productivity are most readily associated with poverty reduction, and whether this pattern changes by sector. Third, it highlights the broader policy and institutional environment which is associated with a poverty reducing pattern of growth (Figure 2).

*Step 1: Profiling growth*

18. The first step in understanding how sectoral growth affects poverty via its impact on the quantity and quality of jobs is to find a suitable methodology for profiling growth.

19. Analysis of the relationship between growth and employment has traditionally focused on the employment elasticity of growth – that is, the percentage change in employment in response to 1 percentage change in output. This measure has three notable shortcomings. First, it says nothing about the actual extent of job creation since a country that grew by 1 per cent and enjoyed a 1 per cent increase in employment would have the same employment elasticity rate as a country which had a 10 per cent growth rate accompanied by a 10 per cent increase in employment. Second, the measure does not take demographic changes into account, although growth in population often swamps increases in employment. Third, and most obviously, the employment elasticity of growth says nothing about the quality of new jobs created.

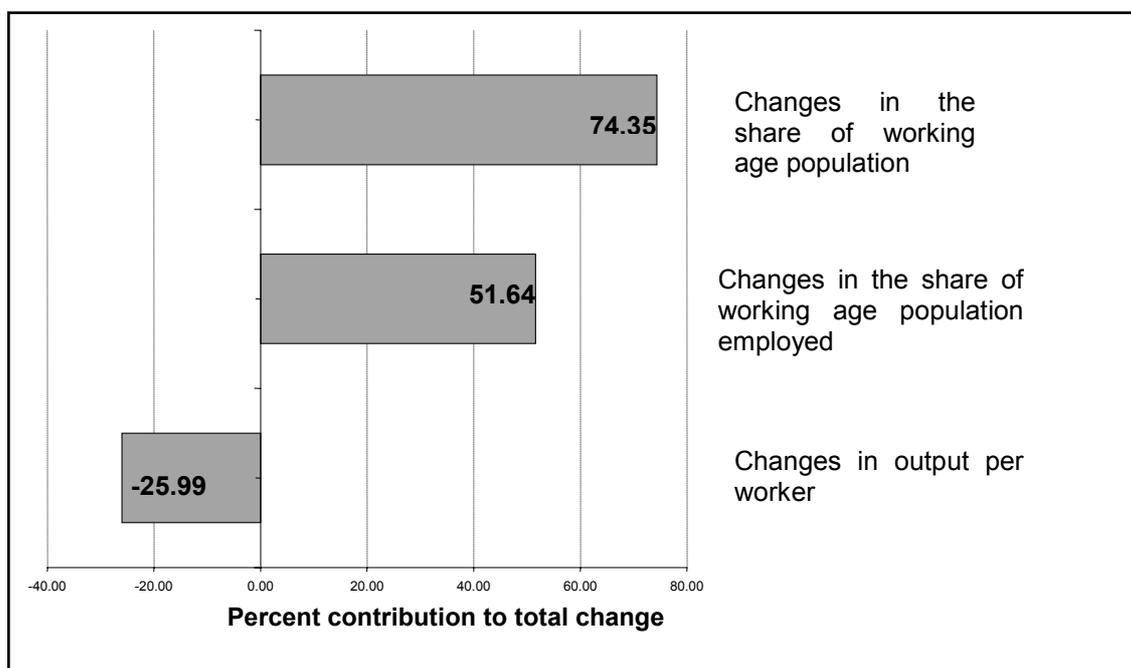
20. A simple way of understanding how growth is associated with increases in the quantity and quality of jobs is to perform a decomposition of per capita GDP growth into three components: productivity changes, employment rate changes and demographic changes. The amount of growth that can be attributed to changes in output per worker can be obtained by calculating the resulting growth in per

capita value added between two points in time under the hypothetical scenario in which employment rates and the share of the working age population remain constant, but output per worker has changed as observed. Similarly, the amount of growth attributed to changes in employment or the share of the working age population can be obtained by calculating per capita value added when the other two components are held constant.

21. Figure 3 shows the results of this growth decomposition, using the example of Nicaragua over a four year period (2001-2005), during which value added growth totalled 12 per cent. It shows that almost three-quarters (74 per cent) of the increase in growth can be linked to changes in the structure of the population. In other words, had everything else stayed the same, the reduction in the number of dependents per working age person would have generated a growth rate of 5.3 per cent (or 74 per cent of 7.12). Changes in employment were also important: accounting for over half (51 per cent), of the observed growth. This means that if productivity and the number of dependents per working age member had both remained constant, the higher rate of employment would have generated a GDP growth rate of 3.6 per cent (or 51 per cent of 7.12).

22. Unfortunately, changes in productivity acted in the opposite direction. Indeed, had population and employment levels remained constant, shrinking productivity would have had a negative impact equivalent to more than a quarter (26 per cent) of the actual observed growth rate. Put differently, had productivity not changed, observed growth would have been close to 9 per cent, but decreases in productivity meant that growth was 7.12 per cent.

**Figure 3: Aggregate employment and productivity profile of growth (Nicaragua 2001-2005)**

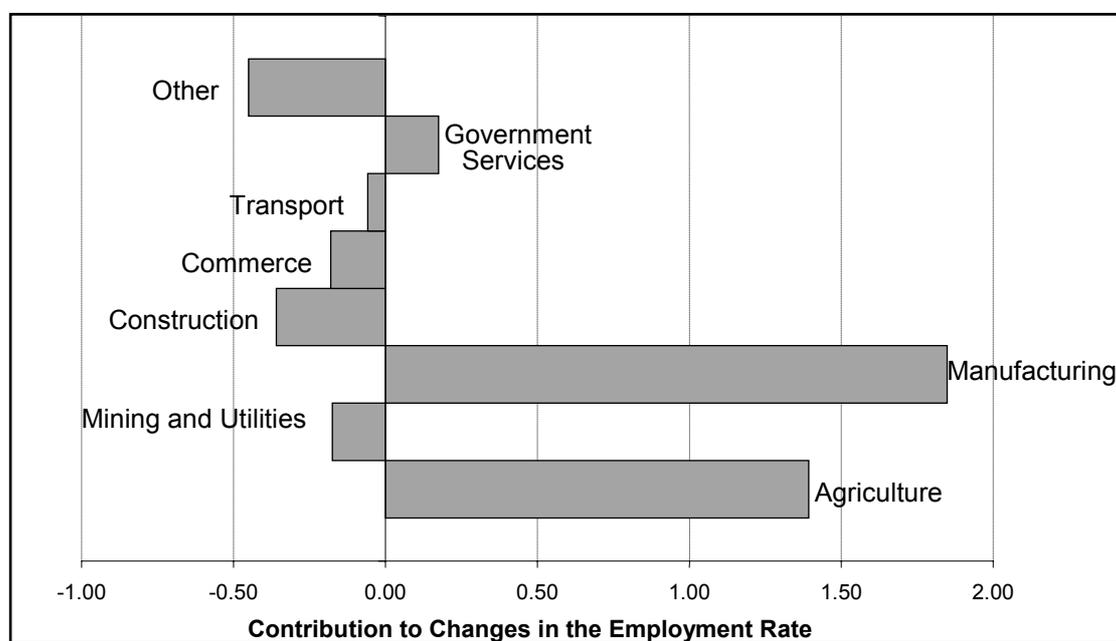


*Source:* Calculations based on data from BCN and EMNV.

23. The decomposition of growth can easily be extended to multiple sectors so as to detect any variance in the employment and/or productivity intensity of growth by sector. Figures 4 and 5 show the results of a decomposition of the employment and productivity growth rates by sector in Nicaragua. The employment rate grew by 2.19 per cent total, with increases in manufacturing and agricultural employment contributing most to this trend (Figure 4). But agriculture, manufacturing and government services all saw

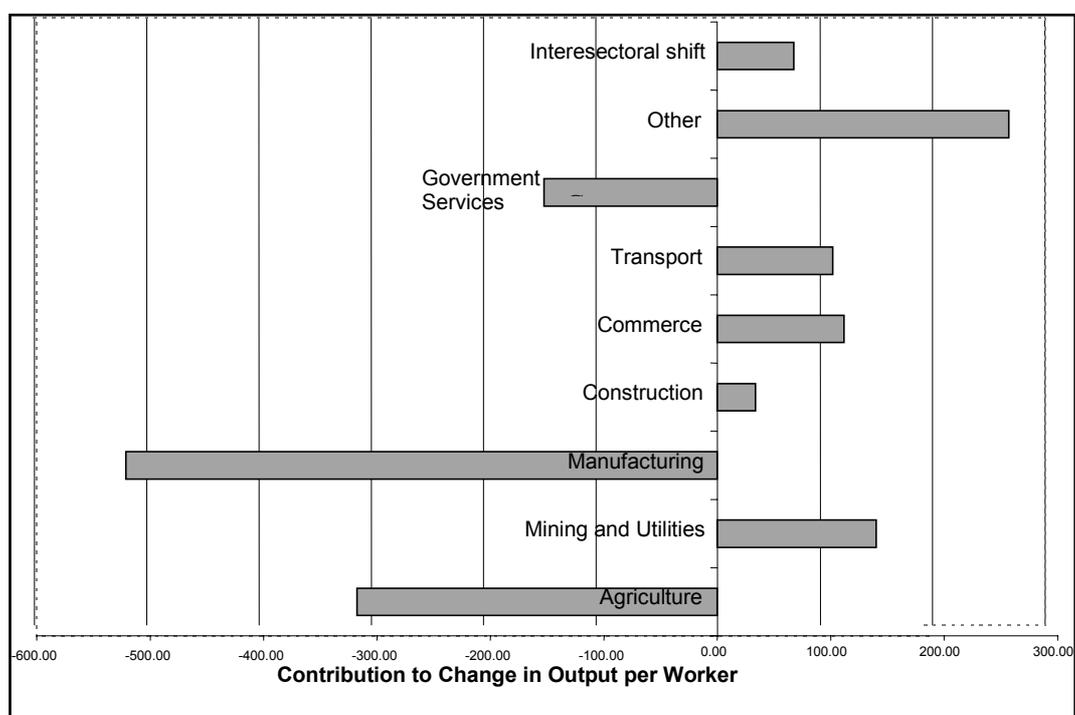
decreases in output per worker and, given their large share in total employment, this had important negative effects on aggregate output per worker (Figure 5).

**Figure 4: Contribution of each sector to changes in the employment rate (Nicaragua 2001-2005)**



Source: Calculations based on data from BCN and EMNV.

**Figure 5: Composition of each sector to change in output (Nicaragua 2001-2005)**



Source: Calculations based on data from BCN and EMNV.

24. In sum, in contrast to traditional measures of the employment elasticity of growth, this first step of the framework enables analysts to discover whether growth is most readily associated with increased employment-intensity (changes in the quantity of jobs) or increased productivity-intensity (changes in the quality of jobs), while accounting for the impact of demographic change. The easy application of this methodology to individual sectors of the economy makes it particularly valuable for understanding the relationship between growth and employment in segmented labour markets.

*Step 2: Linking the growth profile to changes in poverty*

25. The second step is to identify links between the growth profile and poverty reduction, both across the economy and by sector. This can be done by regressing each of the components of the growth profile identified in step 1 above (productivity changes, employment changes, demographic change) against percentage changes in poverty.

26. If employment-intensive growth reduces poverty, then changes in the employment rate could be expected to be significantly and negatively correlated with changes in the poverty headcount. If, on the other hand, the income of the poor rises due to increased productivity then, changing productivity will be negatively correlated with changes in the poverty headcount.

27. As in the first stage of analysis, step 2 can also be broken down by sector (See Annex 1, which also describes an alternative way for analyzing the relationship between the growth profile and poverty reduction in cases in which there are insufficient observations on headcount poverty over the requisite time period). Rather than applying *a priori* assumptions regarding which sector provides a repository of “good” or “bad” jobs, step 2 enables the analyst to identify “more productive” and “less productive” sectors, based on the observed relationship between the growth profile and poverty reduction (Figure 6).

**Figure 6: The relationship between employment-intensive and productivity-intensive growth and poverty reduction**

	<b>employment-intensive growth</b>	<b>output-intensive growth</b>
<b>“more productive” jobs sector</b>	<b>+ve</b> correlation with poverty reduction	<b>+ve</b> correlation with poverty reduction
<b>“less productive” jobs sectors</b>	<b>neutral/ -ve</b> correlation with poverty reduction	<b>+ve</b> correlation with poverty reduction

28. Applying this methodology to a sample of countries, Gutierrez *et al.* (2007) find strong evidence that the sectoral pattern of growth and its employment and productivity-intensities matter for poverty reduction. While employment-intensive growth in the secondary sector (manufacturing, construction, mining and utilities) is correlated with poverty reduction, employment-intensive growth in agriculture is correlated with increases in the poverty headcount. On the other hand, productivity-intensive growth in agriculture is significantly correlated with poverty reduction, whether through increases in sectoral productivity or through the movement of workers into other sectors. In other words, across the countries studied, the secondary sector seems to represent a repository of “more productive” jobs while agriculture is associated with lower productivity on average.

29. Within these broad findings, Gutierrez *et al.* (2007) discover a high level of heterogeneity. While manufacturing and agriculture represent, respectively, “high productivity” and “low productivity” sectors across the sample as a whole, this pattern holds less true in certain regions. For instance, in Latin America employment-intensive growth in the secondary sector is not robustly correlated with poverty reduction, indicating the likelihood of internal segmentation between “more” and “less productive” manufacturing jobs, and upper-middle income countries are found to have a different set of relationships between sectoral patterns of growth and poverty reduction than lower-income countries.

30. In sum, the second step of this three-step framework enables analysts to identify whether employment-intensive growth or productivity-intensive growth is more correlated with poverty reduction, and whether these relationships vary by sector. Analysis to date indicates a high level of heterogeneity across regions and levels of development, demonstrating scope for much deeper research.

*Step 3: Identifying the underlying conditions which matter for poverty reduction*

31. If step 2 reveals that certain sectoral patterns of growth (such as increased employment-intensity in the services sector or greater productivity-intensity in agriculture) are correlated with poverty-reduction, the policy relevance of this observation will hinge in part on identifying the broader variables associated with this pattern of growth. Step 3 enables analysts to identify whether certain policies or institutional conditions are correlated with particular growth patterns.

32. This can be done by regressing the measure of the sectoral pattern of growth against a vector of possible explanatory variables, such as education, labour market regulations, the investment climate, and trade. Explanatory variables should be taken from the beginning rather than the end of the spell since this may make it easier to detect a line of causality running from these variables to poverty reducing patterns of growth. Annex 1 provides equations to enable analysis of these relationships.

33. Cross-country analysis confirms that the broader policy and institutional environment will affect the extent to which growth reduces poverty (Gutierrez *et al.* 2007). For example, across a sample of countries, minimum wage legislation appears to significantly reduce employment-intensive growth in the secondary sector, while openness to trade appears to boost it. Education is robustly and positively associated with productivity-intensive growth in agriculture. These tentative findings demonstrate the scope for future research, since significant heterogeneity in the relationship between the broader institutional and regulatory environment and the sectoral pattern of growth could be expected between regions and countries.

*A note on data*

34. Application of the three stages of this framework of course requires data on total and sectoral GDP, poverty, population and employment, as well as policy and institutional variables. Possible sources for this data are summarized in Table 1 below. Particularly when it comes to determining institutional and policy variables, the suggestions offered in Table 1 are by no means the sole sources of data. Some notes of caution regarding use of this data and advice on overcoming its shortcomings are also offered in Box 3 below.

**Table 1: Possible sources of data**

<b>Data</b>	<b>Source</b>	<b>Notes on Coverage</b>
Aggregate GDP	World Development Indicators (World Bank)	Annual, since 1960
Sectoral GDP	U.N. National Accounts Data	Value added disaggregated into 7 sectors, since 1970
Population	U.N. Population Division	Annual, since 1950
Employment and labour force	ILO-KILM Database	Up to 20 labour indicators, since 1980
Poverty	PovCalNet (World Bank)	Based on household surveys, either income or consumption poverty, since early 1980s
Labour regulations	Rama and Artecona (2002); Sulla, <i>et al.</i> (Forthcoming).	Includes minimum wage, severance pay, union membership, strikes, since late 1940s
Investment climate	International Country Risk Guide	Includes investment profile, since 1984
Trade	Sinnot and Lopez (2003)	Measures openness to trade, 1960s onwards

**Box 3. Understanding and overcoming data limitations**

To perform all three stages of the framework described above, data on GDP, population, employment, labour force, and poverty must be available for the same two consecutive points in time, while data on broader policy and institutional variables should be available for the first time period.

Unfortunately, these demands are in some cases too high: low income countries, and particularly those in sub-Saharan Africa, often suffer from missing or inconsistent data, especially on headcount poverty and labour market outcomes. The most comprehensive data on poverty, derived from household surveys, is available from the World Bank.<sup>1</sup> But many countries have an inadequate number of surveys, while changing sample sizes and definitions pose problems for comparability. The ILO's KILM database is the most comprehensive source of information on labour force and employment rates. But it poses some problems for comparisons across countries or within countries across time. The main difficulty for cross-country comparisons is that definitions and coverage vary. In particular, some countries report values for formal employment only and other leave out sectors such as agriculture. Changes in sample and survey design pose problems for within country comparison. In addition, key observations for many sub-Saharan African countries are lacking entirely.

There are nonetheless a number of pragmatic steps which analysts can take when some of this data is inconsistent or lacking. As mentioned above, Annex 1 describes an alternative way for analyzing the relationship between the growth profile and poverty reduction in cases in which there are insufficient observations on headcount poverty over the requisite time period. As for the shortcomings in employment and labour force data, the KILM database alerts users to variations between survey design, changes in samples, and breaks in series, making it possible to control for differences in measurement and coverage. And studies for some sub-Saharan Africa countries, based on household surveys, can provide supplementary data where ILO data is inadequate.<sup>2</sup>

Gutierrez *et al.* (2007) demonstrate that analysis of the relationship between growth, employment and poverty reduction is viable in a range of developing countries, in spite of serious shortcomings in the data. The team was able to gather relevant data and perform analysis for a total of 106 growth spells in 39 developing countries, although only one-fifth of these were low income (as opposed to middle income) countries, and only 4 were in sub-Saharan Africa.

<sup>1</sup> <http://go.worldbank.org/5IJ993CJ40>

<sup>2</sup> See, for instance: World Bank (2007a) for Senegal; World Bank (2007b) for Ghana; and World Bank (2007c) for Madagascar.

#### IV) Policy implications for promoting poverty reducing economic growth

35. The three step framework described above can help to inform policy by demonstrating whether certain sectoral patterns of growth or particular policy and institutional contexts are correlated with poverty reduction. This section considers four sets of policy implications which might be generated by application of the framework, drawing widely from existing country-based analysis (Hull, 2006).<sup>40</sup> Finally, it alerts development practitioners to the political economy of labour market reforms.

##### *Promoting employment-intensive growth in “more productive” sectors*

36. As shown in Gutierrez *et al.* (2007), the sectors of the economy which constitute repositories of “more productive” jobs will vary by region and country. Steps one and two of the three step framework enables analysts to shed the assumption that a particular sector (for example, manufacturing) must automatically be equated with “good” jobs. Instead, “more productive” jobs are any jobs in which employment intensive growth is correlated with poverty reduction, whether in services, manufacturing, agriculture or even certain segments of the informal economy.

37. Once a link between poverty reduction and employment-intensive growth has been established for a particular sector, an obvious question becomes: are there any feasible policies to expand employment in this sector? For instance, country-based analysis for Argentina, Burkina Faso, Chile, Tunisia, and Ukraine, among others, has pinpointed the growth of small and medium enterprises (SMEs) as a potential source of poverty reduction.<sup>41</sup> Among the policies to expand the employment base in this sector, Burkina Faso has strengthened development and support services for SMEs. A study for Mexico recommends a strategy for targeting interventions to improve factor productivity growth in small enterprises.<sup>42</sup> Analysis for Turkey recommends policies to strengthen the links between SMEs and larger firms, so that the former benefit from economies of scale in the latter.<sup>43</sup>

38. By way of further example, the rural non-farm sector is also identified in a number of country studies as a source of potentially dynamic poverty-reducing employment in a number of countries, including Pakistan and India.<sup>44</sup> Policies to boost employment in this sector include investments in infrastructure to strengthen linkages between agriculture, off-farm opportunities, and urban markets. Analysis for Ukraine suggests policies to incentivize farms to make use of local input supply services, and analysis for Sierra Leone points to support for dynamic agro-business, agro-processing and fisheries sectors as a means of strengthening non-farm employment opportunities.<sup>45</sup>

39. In sum, wherever “more productive” jobs sectors are located, policies should direct support to potentially dynamic areas, while promoting linkage through supply chain integration, in order to strengthen demand for workers.

##### *Boosting productivity-intensive growth in “less productive” sectors*

40. While policies to expand job opportunities in “more productive” sectors are essential for poverty reduction, the majority of the working poor will remain employed in “less productive” jobs, at least in the short term. Again, since the sector in which these jobs are concentrated cannot be determined *a priori*; the first two steps of the three step framework can be helpful in identifying those sectors where an expansion of employment opportunities alone is not associated with reduction in the poverty headcount. In such sectors, policymakers must search for possibilities to boost productivity-intensive growth.

41. Agriculture is often, but not always, identified as a “less productive” sector. While it remains Cambodia’s most important employer in numerical terms, per capita value-added in agriculture has grown less than in other sectors, contributing to a widening urban-rural divide.<sup>46</sup> As in Kyrgyz Republic, flagging

levels of productivity in rural areas is often ascribed to a failure to diversify into more profitable products and agro-processing.<sup>47</sup> Strategies to boost productivity in agriculture often consist of increasing public investments in roads, irrigation, the intensification of farming methods and diversification into higher yield crops. They also look to encouraging those crops which are likely to generate commercial processing and export demand. (See for instance analysis for Bangladesh, Pakistan, Punjab, and Lesotho)<sup>48</sup>. Radwan (1995) notes that for growing productivity to impact the poor, efforts should be made to ensure that the absorption of innovative technology is not institutionally biased towards large producers, by ensuring that small-scale farmers have access to credit and extension.

42. The informal sector represents another segment which is often, although by no means always, associated with “less productive” jobs. As in Bolivia, jobs in this sector can become trapped in a bad equilibrium: while low productivity and hence low earnings means employers cannot afford to comply with regulations which are prerequisites for entering the formal sector, informality limits the potential for productivity growth.<sup>49</sup> Analysis for countries as diverse as Bosnia and Bolivia identifies the following constraints to productivity: weak access to credit; inability to tap export markets; difficulty in accessing international production chains; and the absence of economies of scale in which productivity is higher and regulatory burdens become more manageable.<sup>50</sup>

43. Recommended policies concentrate on drawing the informal sector along a continuum toward formality, by easing access to credit, enhancing the quality and organization of informal production, and facilitating relationships with formal firms. In Kenya, a Small and Medium Enterprise Development Project has helped to strengthen linkages to financial services providers and markets, enabling informal enterprises to grow and to graduate from informal to formal status.<sup>51</sup> Developing linkages with the formal sector through sub-contracting is common in the garment industry in South Asia and may be a way of ensuring that the informal sector has access to markets, raw materials and technology. Steps must be taken, however, to ensure that these arrangements are not employed as a means of circumventing core labour standards.<sup>52</sup>

44. To sum up, policies to improve the quality of “less productive” jobs must focus on enhancing incentives for diversification into more commercially viable sub-sectors (such as export-oriented agriculture or garment production), helping enterprises to escape from low productivity traps. Access to credit, technology, and infrastructure will play important roles in strengthening linkages with “more productive” sectors.

#### *Ensuring access to more and better jobs*

45. As stated in Box 2, barriers to mobility can stem from geography, infrastructure, and legal and cultural norms, as well as the rationing of “more productive” jobs. If such barriers exist, the expansion of “more productive” jobs alone will not be enough to ensure poverty reduction: policies will be required to enable the poor to move more freely from “less productive” to “more productive” sectors.

46. The first step to removing barriers to mobility is to identify them. For this purpose, the three step framework must be backed up with additional quantitative and qualitative research. Depending on country context, research could address the following questions:

- Do insecure property rights, or other institutional weaknesses, dissuade people from moving or seeking more productive employment?
- Do workers lack sufficient skills or qualification to transition into higher earning opportunities?
- Do the poor suffer from a deficit of information about job openings?

- Do significant infrastructure problems prevent easy movement?
- Are legal and/or informal norms skewed against women, youth and/or ethnic minorities in the workplace?
- Do particular groups suffer from work-related exploitation or violence?

47. Box 4 highlights just some of the barriers to labour market mobility that have been identified in country-level research.

#### Box 4. Barriers to Mobility \*\*

**Institutional.** In Pakistan, weak property rights are shown to limit the extent to which farmers are willing or able to diversify out of farming by selling or leasing their land. In Poland, housing market rigidities are identified as a significant barrier to labour market mobility.<sup>2</sup> In China, the household registration system traps temporary migrants in “less productive” sectors of the urban economy.

**Educational.** In Lesotho, education and technical training have a strong influence on workers’ chances of wage employment and the level of earning. In Honduras, a male urban worker with a post-secondary degree earns approximately 100 per cent more than a male urban worker with high school education and 170 per cent more than a male urban worker with primary school education. In Pakistan, education is an important determinant of mobility, through its effects on female labour force participation, rural-urban migration and participation in the rural non-farm sector.

**Informational.** While all countries suffer from imperfect information between “buyers” and “sellers” of employment, the problem tends to be greatest in developing countries due to the weakness of formal channels for the exchange of labour market information (such as vacancy advertising or employment offices) and the prevalence of rural and informal sectors. Barriers to information flows between potential employers and employees are found to be highest in the informal sector, in rural areas, and among women in Trinidad and Tobago (Murphy and Strobl, 2008).

**Infrastructural.** Poor transport is identified as a major constraint on the urban poor’s ability to get a job in Latin America. In Honduras and Madagascar, off-farm employment has been limited by a lack of good transportation and roads to bridge the physical distance between rural areas and urban centers. As well as directly limiting access to good jobs, living “off-road” can have indirect impacts on work-force participation through its effects on access to education, health and credit (Sender *et al.* 2005).

**Informal.** Racial discrimination, gender discrimination and discrimination related to the stigma of coming from certain neighborhoods is found to account for the prevalence of the poor in “less productive” sectors and their inability to move to “more productive” jobs in Latin America. In India, members of Scheduled Castes and Tribes are more likely to be trapped in casual labour jobs and have lower access to “more productive” off-farm employment

**Violence and exploitation.** Bonded labour, under which the worker is tied to an employer and required to work for very low or zero wages, is determined partly by religion, ethnicity and caste in Pakistan. The use of in-kind wages and wage arrears in Russia forces workers to remain attached to “less productive” jobs by hampering their ability to move (Friebel and Guriev 2000). In sub-Saharan Africa, informal sector and casual workers tend to have low organizational and bargaining capacity, making them unable to defend their interests against unscrupulous employers (Sender *et al.* 2005). One study finds that women in Mozambique who sought wage employment against the wishes of their husbands were often severely beaten (Sender *et al.* 2004).

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Drawn from: Pakistan, Idem; 2004. “Poland – Growth, employment and living standards in pre-accession Poland”; 2005. “China – Integration of National Product and Factor Markets - Economic Benefits and Policy Recommendations”; 2004. “The urban poor in Latin America”; 2006. Lesotho, idem; 2006 “Honduras – Poverty assessment: attaining poverty reduction”; 2004. “Drivers of sustainable rural growth and poverty reduction in Central America, Honduras case study”; 2005. “Madagascar – Development policy review: sustaining growth for enhanced poverty reduction”; 2006. “India – Inclusive growth and service delivery: building on India’s success”

48. Analysis to date suggests a range of policy interventions to help dismantle such obstacles to mobility:

- ***Institutional.*** In a number of cases, enhanced mobility rests on the reform of institutions associated with restricted movement of the workforce. Policy recommendations for Pakistan suggest increasing the security of property rights as a means of encouraging movement out of agriculture – enabling farmers who want to diversify into potentially more productive off-farm employment to sell or lease their land.<sup>53</sup> Research for China suggests that remnants of the household registration system be phased out and highlights the necessity of reforms of urban social policies that currently limit rural migrants’ access to benefits.<sup>54</sup> Analysis for Poland underscores the importance of policies to reduce rigidities in the housing market, alongside the provision of targeted mobility grants to enable individuals to overcome financial constraints on their mobility.<sup>55</sup>
- ***Educational.*** Education, in its various guises, is often a crucial precondition for labour market adjustment to more profitable economic activities. In Ecuador, the creation of a considerable mass of secondary educated workers is deemed necessary for enabling participation in more technologically advanced sectors.<sup>56</sup> Country-based analysis for Egypt and Kenya has called for stronger links between training institutes and private sector sources of demand, as a means of increasing market relevance of the labour force.<sup>57</sup> The historical case of Ireland demonstrates how a small economy, with a history of chronic labour migration, can develop into a prosperous niche by shifting its comparative advantage towards products and services based on skilled labour. The Irish example has been used as a reference point for other countries, such as Moldova.<sup>58</sup> In rural economies, educational improvements have been shown to increase returns to small-scale farmers because educated farmers are readier to absorb new production techniques and innovate (Radwan). Education levels are also positively associated with ability to adapt agricultural activities effectively to climate change-induced risks in sub-Saharan Africa (Maddison, 2007).
- ***Informational.*** The experience of East Asian countries demonstrates the potential role played by the expansion of employment services and search assistance, and in particular E-systems, in overcoming informational barriers in the labour market. For instance, in Malaysia employment offices in different areas are able to share information about job seekers and vacancies via networks and the internet (Betcherman *et al.* 1999). Organizations in the informal economy, such as the Self-Employed Women’s Association (SEWA) in India, can also provide potentially isolated workers with access to information about employment opportunities and markets (World Bank 2006).
- ***Infrastructural.*** The provision of reliable and affordable transport is identified as key to enabling the urban poor to reach the best opportunities in Latin America, while good rural roads and reliable electricity and water supplies are essential for accessing off-farm employment in rural areas, according to a country study for Ukraine.<sup>59</sup> In Nepal, improved transportation and communication has facilitated the convergence of agricultural and nonagricultural wages across regions in recent decades.<sup>60</sup> Infrastructure reforms can even be addressed to enhance labour market participation of specific groups. As noted in a Gender Assessment for Pakistan, investment in timesaving infrastructure is critical to encouraging women’s participation in work activities.<sup>61</sup>
- ***Overcoming discrimination, violence and exploitation.*** Responding to employment differentials across age and gender lines, research often recommends vocational training and apprenticeship programmes specifically targeted to young people (Kenya) and women (Poland).<sup>62</sup> However, due to experiences in the MENA region where, despite generally high levels of education, women’s labour force participation remains low, analysis also suggests that the increased availability of

educated women alone will not improve employment prospects in certain social and cultural environments.<sup>63</sup> Investments in education and training should be accompanied by other interventions to break a web of socio-cultural practices which prevent full-capacity participation in the labour market. Trade Unions, which in some countries have made efforts to mobilize members outside their traditional constituencies, can play an important role in strengthening the voice of marginalized groups (Sender *et al.* 2005, World Bank 2006), while donors can provide capacity-building programmes to strengthen organizations that provide workplace empowerment for discriminated groups. Governments may also need to revisit laws and affirmative action policies regarding the fundamental rights and educational and labour market opportunities of minorities.

### *Institutional and policy reforms*

49. The third step of the three step framework enables analysts to ascertain whether particular policies and institutions are positively or negatively associated with poverty-reducing patterns of growth. The results generated by this step can help to inform discussions with policymakers about the appropriate reforms to promote a broader environment conducive to growth in both the quantity and quality of jobs.

50. Country-level studies have helped to identify a host of policies and institutions which act as constraints to job creation and productivity. These include the legal and regulatory hurdles to business entry, operation and exit, and poorly designed labour market regulations. For instance, inflexible or costly hiring and firing regulations are identified as an obstacle to employment growth in Chile, India (World Bank 2005), Mexico and Zambia, among others.<sup>64</sup> Wage rigidity – indicated by the absence of a statistical relationship between employment and the real wage – can also hamper job creation. In many developing countries it has been related to the inflexibility of public sector wages (see, for instance, analysis for Uruguay, the Caribbean, and Tunisia), while binding minimum wages are also thought to increase the reservation wage.<sup>65</sup>

51. Investment Climate Assessments (ICAs) demonstrate that corruption can pose a major barrier to employment creation and firm productivity. Studies for Afghanistan and Ukraine note that intricate regulatory regimes tend not to be perceived as a major barrier by firms because they are loosely enforced. However the non-enforcement of regulations presents a problem in itself – the opportunity for arbitrary application of rules and corruption.<sup>66</sup> In Lao, “tall poppy syndrome” (by which larger or more successful firms are subject to higher levels of regulation and face a greater number of business inspections), incentivizes firms to produce at suboptimal levels, hampering productivity and labour demand.<sup>67</sup>

52. A number of country-level studies corroborate Gutierrez *et al.* (2007) cross-country finding that openness to trade is associated with a poverty reducing pattern of job creation. Anti-export biases of trade regimes are identified as hampering the productivity of jobs in Morocco and Bangladesh.<sup>68</sup> Non-tariff barriers to trade – including poor storage facilities and port infrastructure, and delays at customs – are also identified in Afghanistan, Kenya, Kyrgyz Republic and Peru.<sup>69</sup> Indeed, though a number of country studies identify tariffs as problematic, most recognize that inefficiencies in customs, complex standards regimes, and transit problems can act as greater barriers to trade (and hence the creation of “more productive” jobs) than tariffs themselves.

53. In response to the policy and institutional barriers to job creation, country-level policy advice often recommends measures to lower the costs of doing business and introduce more flexible labour market regulations. For instance, a study for Tunisia recommends lowering minimum capital requirements for starting a business, while one for the state of Orissa in India looks to simplifying the procedures for firm entry and exit.<sup>70</sup> Recent reforms in Colombia brought down the costs of firing workers as a means of encouraging employers to recruit more workers during boom periods, while in the Slovak Republic a new

Labour Code introduced the option of non-standard contracts (World Bank 2006). Strategies to alleviate wage rigidity often suggest reforming public sector compensation policies or the introduction of sub-minimums to encourage the employment of often excluded groups, such as young people.<sup>71</sup>

54. In order to ensure job security with minimal distortions in the labour market, social protection measures should be de-linked from specific jobs, where possible. As noted in the 2006 World Development Report, the “design of the optimal solution” will depend on the “institutional and administrative capacity of government and on the structural characteristics of the labour market” (World Bank 2006). In low income countries, public works programmes may be the most feasible policy response. These programmes are self-targeting (avoiding high demands on administrative capacity) and can be implemented even if levels of informality are high. If well-designed, labour-intensive public works programmes for infrastructure can also have a lasting impact on the quantity and quality of jobs by releasing binding constraints to growth (Radwan, 1995).

55. ICAs often advise measures to reduce corruption, so as to create a more predictable business environment which will be more attractive to investors, and hence a source of job-creating growth. In Zambia, a proposed anti-corruption strategies consists of action to raise the likelihood of getting caught and punished for corrupt behaviour by improving transparency and accountability mechanisms and strengthening the judiciary.<sup>72</sup> In Columbia and Cambodia, measures to reduce the opportunities for corruption consist of reducing red tape and unnecessary administrative procedures<sup>73</sup>

56. To boost employment creation following trade liberalization, country advice recommends a complementary agenda, including improvements to customs, ports and other critical infrastructure, regulatory reforms, innovation and education.<sup>74</sup> The adoption of international product standards, including sanitary and phytosanitary measures, are also identified as prerequisites for realizing the job-creating potential of tariff reductions.<sup>75</sup>

#### *Understanding the political economy of reform*

57. Reforms to policies and institutions to improve the quality and quantity of jobs can be highly sensitive from a political economy standpoint, even if they make sense from efficiency or equity perspectives. Labour market “insiders” – sometimes represented by powerful labour unions – often lobby to maintain regulations that operate in their favour, while “outsiders” – concentrated in less productive sectors – will suffer from ongoing vulnerability to the vagaries of the labour market. For policymakers, the challenges rest in finding the correct balance between job creation and job protection and forging a viable reform path. Box 5 contains some key insights into the political economy of highly sensitive reforms garnered from recent experiences in Chile, Colombia, Croatia, Poland and Slovakia, among other countries.

**Box 5. Political economy insights on successful labour market reforms \*\***

An “**agent of change**” (whether a government unit, an employer organization or a progressive trade union) is often crucial to champion controversial labour market reform.

Measures to **increase voice and accountability of the poor** may be essential to ensure that the government’s labour policy agenda is not entirely dominated by politically powerful labour market “insiders.” Democratic local governments and strong autonomous associations, such as informal sector unions, will play an important role in strengthening outsiders’ positions.

**Public information campaigns** can help to build societal consensus for reform by documenting the high costs of bad labour market policies and demonstrating the benefits of reform.

Policymakers should identify “**unlikely**” **coalitions of support** for reform. For instance labour market “outsiders” (such as informal sector workers) and employers in the independent private sector may have shared interests in supporting welfare and efficiency enhancing reforms.

**Comprehensive reforms** have a higher likelihood of success than piecemeal reforms. Reforms should cover a range of labour market policies and be linked with reforms to social production systems. Efficient product markets will help to ensure that labour market “insiders” cannot capture wages at the expense of “outsiders”.

At the same time, due attention should be paid to the **sequencing** of reforms. For instance, a recent Country Economic Memorandum for Morocco notes that there is limited potential to reduce minimum wages or alter the exchange rate regime in the short term, even though these strategies are considered optimal from the perspective of reducing labour rigidities and stimulating export-led growth. Instead, it suggests pursuing two less controversial reforms – trade liberalization and tax modernization – first.

**Losers may require compensation.** The most effective forms of compensation will simultaneously address obstacles to reentering the labour market (for instance through support for education and training or transport vouchers).

\*\*For further information see World Bank (2006); 2005. Ukraine, *Idem*; 2006. Morocco, *Idem*.

## Conclusion

58. The objective of this paper has been to contribute to the understanding of the relationship between employment and poverty reduction. Its goals have been to provide tools to assess the impact of employment-intensive and productivity-intensive growth under segmented labour market conditions, *and* to enable a transition from research to policy outcomes. Specifically, it has sought to help analysts and policy makers address three questions.

59. First, how does the sectoral pattern of growth affect its poverty impact? This question is of particular relevance under the segmented labour market conditions commonly found in developing countries. Growth in one sector of the economy will not automatically translate into benefits for the poor: much will depend on the profile of growth (its employment- or productivity-intensity), the sectoral location of the poor, and the extent of mobility across sectors.

60. Second, is employment-intensive or productivity-intensive growth more important for poverty reduction? This will depend on the quality (or productivity) of jobs in the sector in which growth occurs. Put simply, for employment-intensive growth to translate into poverty reduction it must occur in a “more productive” sector, while “less productive” sectors may require productivity-intensive growth to ensure a decline in headcount poverty. The first two steps of the framework in Part III provide tools for profiling growth (according to its employment- and productivity-intensity) and assessing its impact on poverty.

61. Finally, what policies will facilitate the poor's participation in growth? Step three of the framework suggests that a range of policies – pertaining to both the labour market directly and the policy and institutional environment more broadly – can promote a poverty-reducing sectoral pattern of growth. Country-specific quantitative and qualitative analysis is required to identify constraints to job creation, productivity and mobility. Depending on the sector in question, policymakers may wish to boost employment and/or productivity, while ensuring that the poor are able to participate in more and better job opportunities. Part IV draws on existing research to highlight policies pertaining to infrastructure, education, trade, the investment climate and human rights, among other key concerns.

40 Hull (2006) reviews World Bank Analytical and Advisory Activities (AAA) from 2004 until August 2006, identifying more than 100 pieces of AAA with a substantial focus on the topic of employment generation. This paper draws on some of the most pertinent findings of the review. Individual studies are referenced below in footnote form. All are World Bank publications unless otherwise stated.

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## INFORMALITY AND INFORMAL EMPLOYMENT

Henrik Huitfeld, SIDA and Johannes Jütting, OECD Development Centre

### Main messages

- Strengthen the knowledge base on the diverse nature of informal employment, including its links with the formal labour market, and the costs and benefits of, as well as the barriers to formalisation.
- Focus more attention on workers in informal employment to increase their productivity and earnings, and reduce the risks they face, with the aim of creating more decent jobs.
- Acknowledge the diversity of occupations and job types in informal employment and develop policy packages for the different categories of workers.

### Introduction

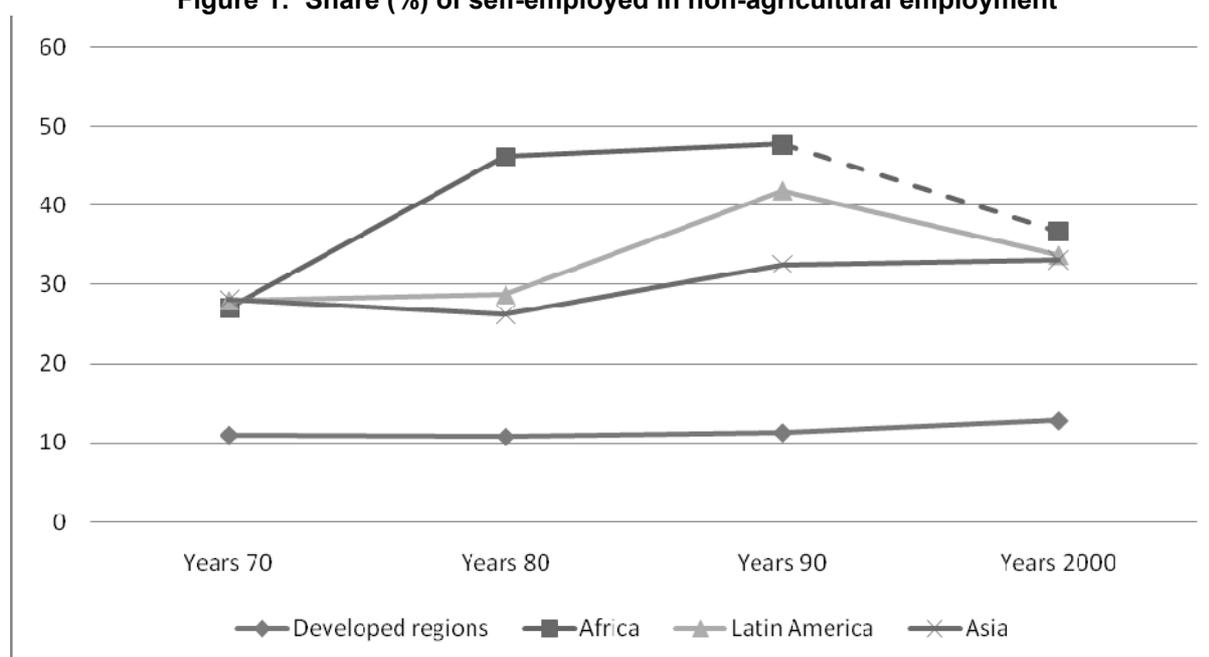
1. Informal employment in its diverse forms is gaining increasing attention within global and national development agendas. The incidence and persistence, and the causes and consequences of informal employment are increasingly being discussed and debated. In this hot topic paper, we take stock of this ongoing discussion with the aim of raising awareness among the policy community that addressing the constraints, opportunities and incentives of informal workers and enterprises is essential for achieving pro-poor growth in both middle-income and low-income developing countries.

2. Why should we care about informality or informal employment? Firstly, all over the world, the share of informal employment, that is jobs performed outside the formal structures that govern taxes, workplace regulations and social protection schemes, is very high, and increasing. On average, over half of all jobs in non-agricultural sectors in developing and emerging economies can be considered informal. Informal employment is also pervasive in a number of OECD countries, covering well over a quarter of workers outside of agriculture. In some regions, including sub-Saharan Africa and South Asia, this rate is as high as 80 per cent and, for a few countries, even higher.

3. If informal employment in agriculture is included, the share of informal employment in total employment is even higher: as high as 90 per cent in many countries in South Asia and sub-Saharan Africa (Chen *et al*, 2005). Recent international consensus emphasises the role of productive employment and decent work for all to achieve sustainable growth and poverty reduction<sup>76</sup>. A poverty reduction strategy that acknowledges the role of decent work for all will then naturally need to focus on informal employment. The informal economy contains considerable unfilled potential to generate growth and reduce poverty.

4. Secondly, informal employment is not withering away. Non-agricultural self-employment – a proxy for informal employment – has been increasing continuously in absolute and relative terms since the 1970s and across the four decades (Figure 1). It represented 22.5 per cent of total non-agricultural employment in the 1970s, 26.8 per cent in the 1980s, and 31.3 per cent in the 1990s, and it is expected to be at the same levels for the 2000s, when the data for Western and Middle Africa becomes available.

**Figure 1: Share (%) of self-employed in non-agricultural employment**



Source: OECD 2009a

5. Thirdly, the reasons for informality vary considerably among countries, occupational categories and types of enterprise within a country. For most, informal employment is the only available option and functions as a last resort for people excluded from the formal labour market. A strong link exists between informality and poverty; most of the working poor in the world work informally, either in self-employment or as wage earners. Many of these people lack basic social protection and are locked in low productivity activities, with scant opportunities for economic mobility.

6. However, being informally employed does not automatically mean being poor, of low productivity and excluded from services and social security. In many parts of the world, the informal economy also includes small-scale entrepreneurs who are not poor and have a large capacity for innovation and a large potential to grow. In addition, as has been suggested by some recent authors, quite a few working people may actively choose informality to avoid paying taxes and complying with regulations, and also to opt out of social insurance schemes and other public services that they consider low quality (Perry *et al*, 2007; Maloney, 2004; Jütting, Parlevliet and Xenigiani, 2008). However, it is debated to what extent informal employment is a “real” choice and how important this cause of informality is in different country contexts (Tokman, 2008).

## **A New Interest in Informal Employment and its Relationship to Pro-Poor Growth**

7. The renewed interest in informal employment was reflected in and further promoted by the 2002 International Labour Conference Resolution and Conclusions on Decent Work and the Informal Economy<sup>77</sup>. The resolution includes conclusions related to the definition and diagnosis of the informal economy, the main characteristics and decent work deficits of informal workers and informal economic units, and a range of actions to address these decent work deficits and to facilitate integration into the mainstream economy.

8. The term “informal economy” was considered preferable to the traditional “informal sector”<sup>78</sup>, because informal workers and economic activities do not belong to one sector of economic activity, but cut across many sectors. The informal economy refers to “*all economic activities that are, in law or practice, not covered or insufficiently covered by formal arrangements.*” Informal employment is a broader concept that also includes employment of an informal nature in formal enterprises, as well as wage and self-employment in informal enterprises and households.

9. Two important factors have contributed to the questioning of the conventional wisdom that the informal economy has little growth potential and that it disappears with economic growth.

### ***1) The persistence and increase of informal employment***

10. In many regions informality is on the rise or at least persistent. Even in environments that have benefited from sustained growth, informal employment is often rising faster than formal employment. As an example, self-employment has risen as a share of total employment in India (Ghosh *et al.*, 2007) and nearly 50 per cent of the urban workers in China have no formal contract and often work under precarious conditions. This calls into question the approach of focusing policy interventions on those who are in the formal economy. Instead, the main challenge is to increase the productivity and earnings and reduce the risks of those working informally, with the aim of creating more decent jobs and gradually formalising informal employment.

### ***2) The diversity of informal employment***

11. The mainstream economics perspective on informal employment is in the context of labour market segmentation where good formal jobs are scarce and workers outside the formal labour market are queuing for them while working involuntarily in low-productivity informal jobs. However, given the size and diversity of informal employment, we need to look in more detail at the dynamics and segmentation *within* informal employment.

12. Generally, informal employment can be classified according to major characteristics such as wage employment or self-employment, urban or rural employment, and in informal or formal enterprises. Some major regional differences can be noted among developing countries. Self-employment of various kinds is the dominant form of informal employment in sub-Saharan Africa, accounting for four-fifths of informal employment in Kenya, Ghana, Mali and Madagascar (Heintz and Valodia, 2008). In Latin America and South Asia, informal self-employment and informal wage employment each account for approximately half of the informal workforce. However, while in South Asia most informal wage employment is within informal enterprises, in Latin America almost half of the informal wage-employed work in formal establishments (Chen and Doane 2008; Tokman 2008).

13. A set of main employment categories of informal workers can be identified to take into account differences in employment relationships. These categories can provide the basis for development of appropriate broad policy interventions.

- Employer-owners of informal firms;
- Own-account workers;
- Informal employees (of formal and informal firms);
- Sub-contracted workers and wage workers for households (domestic workers);
- Wage workers with no fixed employer (casual day workers); and
- Unpaid contributing family members.

14. The main employment categories could be disaggregated further based on country-specific situations and the relevant importance of different occupational categories. For example, the Self-Employed Women's Association (SEWA), an organisation of self-employed women workers in India, divides its members into four major occupational categories: vendors and hawkers; home-based workers; labourers and service providers; and rural producers (Chen, 2006). Home-based workers and street vendors are two of the largest sub-groups of the informal workforce, with home-based workers perhaps the more numerous but street vendors the more visible. Taken together they represent an estimated 10-25 per cent of the non-agricultural workforce in developing countries (ILO 2002).

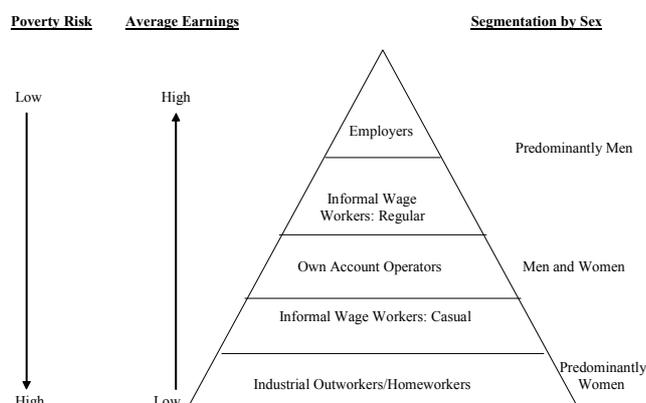
**Box 1: Street trading in Africa**

A regional review of informal street trading in Africa found that street trading accounts for a large share of new urban jobs in sub-Saharan Africa (Skinner, 2008). This growth is a result of a combination of factors, especially urbanisation, migration and economic development. The main concerns of street traders relate to the right to a place to work, and harassment by police, city officials, and retail traders. Other concerns relate to the strong position of wholesale traders and access to capital. Often traders have to borrow from the wholesale traders at very high interest rates. The strengthening of organisations of street traders and the participation of street traders in urban planning are central to addressing these concerns. Some best practices exist in policies to accommodate street traders. In Dar es Salaam, Tanzania, and Durban, South Africa, street traders have been issued licences to operate. Associations of street traders have established good relationships with city authorities and infrastructure for street traders has been established at central locations. However, many street traders are not members of any organisation.

15. The following pyramid depicts the segmentation within the informal economy by employment status and the relative earnings of different segments (Chen *et al.*, 2005, Figure 2). While micro-entrepreneurs who hire others, that is employers, can have a relatively good income, other groups such as home workers are much worse off. This figure also shows segmentation by sex. In general, men are more represented at the top of the pyramid (as micro-entrepreneurs/employers and informal employees), and women more as unpaid family workers and home workers. Categories of workers also differ significantly in terms of poverty risk, and irregularity and insecurity of work. The diverse and heterogeneous structure of informal employment calls for policy measures that are adapted to the specific situation of individual groups of employers and workers.

**Figure 2. Segmentation of the Informal Economy: By Sex, Average Earnings, and Poverty Risk**

**SEGMENTATION OF THE INFORMAL ECONOMY:  
BY SEX, AVERAGE EARNINGS, AND POVERTY RISK**



Source: Chen *et al*, 2005

**Box 2: A labour market profile: Tailoring and stitching in Nepal**

In Nepal, tailoring is carried out in local small informal shops, whereas stitching is often home based. These activities are done primarily for local clients and local markets, but are also often done for garment makers who subcontract work to local stitchers. Women dominate among garment workers, in particular among home-based workers.

Tailoring and stitching can be done either on a piece-rate basis or through self-employment; in fact, the two work methods may be combined if necessary, that is workers may have more than one employment status at a time. Piece-rate workers do not have a contract and are paid by the owner of the garment business; the self-employed may sell directly to customers or through middlemen. Earnings are low and vary substantially over different periods of the year (24-40 per cent of average income in Nepal). In Nepal, as in other countries, home based work is paid at much lower rates than the same work done outside the home, for example in factory settings.

Tailoring and stitching are caste-based activities carried out largely by the Damai (Periyar), a community so marginalised that other caste groups are very reluctant to enter the sector of tailoring and stitching. Problems with middlemen and contractors are foremost, and delayed or incomplete payments are common. Garment workers report that they need more skills training, more work, and payments on time. They also mention the need for at least a minimum wage, and access to some kind of healthcare, particularly because eye problems, back pain and other health problems affect their ability to work.

(HomeNet South Asia and the Institute of Social Studies Trust, 2006)

**The Drivers and Determinants of Informality and Informal Employment**

16. There is an important debate in the literature about what has been driving the increase in the share of informal employment observed in developing countries in the last decades. It is important to understand the drivers of informality in order to be able to design proper policy responses. The literature suggests a set of alternative explanations.

17. Firstly, informality could to a large extent be seen as a result of the type of development that fails to generate sufficient good jobs for all. This has been accentuated by low capacity in the private and public sectors to accommodate rapid population and labour force growth and has been worsened by labour market discrimination and segregation between men and women, social groups and different occupations.

18. Secondly, an increase in subcontracting driven by globalisation and economic liberalisation has led to greater diversity in the forms of informal employment. This in turn has led to a greater heterogeneity among informal workers, and an increase in the number of those with higher skills and productive capacity.

19. Thirdly, formal regulations have mostly been designed for larger enterprises and are therefore often inadequate for the needs and conditions of the growing sector of micro-enterprises. Changes in labour regulations and/or in implementation of labour regulations may also have had an impact on the share of informality in the economy.

20. Fourthly, there has been informalisation by employers of once-formal jobs as a strategy to lower labour costs and deal with competition.

21. One important related issue in this debate is whether changes in informality can be attributed to changes in employment arrangements *within* sectors, or to shifts in employment *across* sectors in the economy. This second possibility is worth examining as some economic sectors are especially prone to informal employment relations as we have seen above. An increase of the relative share of such sectors in the economy thus would lead to an overall increase in informality.

22. However, evidence from Latin America suggests that a large part of the increase can be attributed to increases *within sectors*. For example, Bosch and Maloney (2006) find that 91 per cent of the 4 per cent increase in informality in Mexican labour markets from 1991-5, as well as 90 per cent of the decline to its original level in 2001, can be attributed to changes within sectors. A similar picture arises for most other Latin American countries (Gasparini and Tornarolli, 2007). This evidence suggests that certain jobs that were previously formal have become informal over the last decade(s). Such a tendency also seems to be relevant in South Africa, where informal employment within formal enterprises is becoming an increasing source of precariousness (Altman, 2007; Skinner and Valodia, 2002)). For South Asia, Chen and Doane (2008) note that the traditional, industrial and global modes of production that coexist today are each associated with high degrees of informal employment.

### **Good and Bad Practices in Addressing Informality and Informal Employment**

23. Traditionally, measures related to informality in employment have been aimed at formalisation of informal activities. These have included measures to improve the overall business environment, to simplify business registration practices and to reduce red tape. However, often formalisation policies have had negative connotations and taken the form of stressing the illegality of informal activities and making it more difficult for informal economic actors to carry out their activities. This has included measures such as moving street vendors out from central locations, introduction of obligatory cash machines at market places, and stricter enforcement of laws and regulations. The results of these measures are questionable at best. Often, rather than reducing poverty they have contributed to increased poverty and vulnerability by pushing already vulnerable groups of people into even more difficult situations.

24. More rarely, governments have implemented measures targeted at strengthening the position, increasing the earnings and growth potential, and reducing the risks of informal workers and entrepreneurs. Supplementary to this, a large range of initiatives has been supported by international, non-governmental and private actors throughout the developing world. These include activities in many important but diverse fields such as microfinance, business development services, sub-sector development, vocational training and support to member-based organisations of informal workers. From these types of programmes, good practices can be identified that could be implemented within a more broad-based strategic framework.

The Self-Employed Women's Association (SEWA) is an organisation of poor self-employed women in India. These are women who earn a living through their own labour or small businesses. SEWA's main goal is to organise women workers in order to improve the work and living conditions of the women and their families. SEWA has a membership of over one million workers, all of whom are women in the informal economy from a range of different occupations and trades in both urban and rural areas. To help their members achieve their goals, SEWA engages in what it calls "Struggle and Development": that is, union-style collective bargaining and campaigns to raise awareness, air grievances, and demand change; and development interventions to promote alternative economic opportunities and build assets. The development interventions of SEWA include financial services (savings, loans, insurance), social services (health care, childcare, adult literacy), infrastructure (housing, sanitation, electricity, transportation), capacity building (technical skills, leadership), and enterprise development and marketing services (Bhatt, 2006; Chen, 2008).

#### **Box 4: Waste recycling in Durban**

The municipal government of Durban/eThekweni – in cooperation with organizations of informal sector workers – has established buy-back centres in the city to purchase recyclable materials such as cardboard from self-employed waste collectors. Prior to the establishment of the buy-back centres, waste-collectors often had to rely on intermediaries for market access, which reduced their terms of trade and the share of value-added they were able to realise. The establishment of such centres for marketing recyclables allowed the self-employed to sell their services more directly to the companies processing the materials collected. In this way, a targeted, municipal-level intervention was able to increase market access and to create a type of market exchange which was not prevalent before. The development of markets often provides economies of scale which reduce transactions costs. Operating individually, the informal self-employed cannot take advantage of these potential benefits. However, by consolidating the purchase and sale of recyclables by establishing marketing centres, self-employed individuals can improve access to markets, raise productivity, and improve their earnings. Cooperation between municipal government bodies and organizations of the informal self-employed was necessary to realise these collective benefits (Heintz and Valodia, 2008).

#### **Policy lessons and recommendations for donors**

25. The UN Commission for Social Development adopted a resolution in February 2008 that "emphasizes that promoting decent work aims at the overall improvement of living and working conditions for all and encourages efforts, as appropriate to the country context to address the challenge to gradually formalize economic activities in the informal sector". In addition, a new target to the Millennium Development Goals stresses the role of productive employment and decent work for all in national and international development strategies. However, even if employment has received a more prominent role in the second generation of Poverty Reduction Strategy Papers (PRSPs), a strategic approach targeted at informal employment or decent work for all is still to a large extent lacking (ILO, 2007).

26. Formalisation is a multifaceted concept. Traditionally, formalisation has been seen as incorporating informal economic activities into the existing formal regulatory frameworks, primarily business registration and taxation. However, formalisation must be seen more broadly than this and should include access to the rights and benefits associated with formality. As a formalisation policy needs to identify and address the barriers to formalisation, it also needs to take into consideration the limits to formalisation. As a consequence, specific measures and services should be targeted directly at informal workers and informal entrepreneurs. Donors could play an important role in promoting a more balanced approach to formalisation.

27. The 2002 ILO Resolution states that "the promotion of decent work for all workers, women and men, irrespective of where they work, requires a broad strategy: realizing fundamental principles and rights at work, creating greater and better employment and income opportunities, extending social protection, and promoting social dialogue". A strategic agenda for formalisation would then need to include a holistic approach to reducing the decent work deficit of both formal and informal jobs. It is vital to better integrate the employment creation and the social protection agenda of informal workers into poverty reduction and development strategic processes. This would include better integrating broad employment objectives into

macro policies (taxes, fiscal issues) and sector policies (such as labour, education/skills, infrastructure, social protection).

### *Towards a Three-Pronged Strategy*

28. Effectively addressing informality needs to start by understanding the costs and benefits for those employed within different segments of the informal economy. Where people have chosen to leave the formal sector, they need to be given incentives to rejoin it. Benefits should be linked to social contribution levels, while administrative procedures such as business and workers' registrations should be simplified. Apart from positive incentives, reducing informal employment also implies strengthening enforcement mechanisms. However, policies also need to adequately address those who have no choice but to work informally. Such people need a different approach from those who voluntarily opt out of the formal sector. Poverty-alleviation programmes can tide over people whose options for entering the labour market are limited. A better understanding of the complexity of informal employment and a more nuanced approach to addressing the specific needs of informal workers are urgently needed.

29. Informal employment comprises various phenomena that require distinct policy approaches. The recent OECD Development Centre Publication "Informal Is Normal?" therefore calls for a three-pronged strategy that should be adopted, depending on the specific situation in a country.

30. The following components can be identified:

- i) For the world's poor, working informally is often the only way to participate in the labour market. Policies should consequently try to unlock these people from their low-productivity activities, enable them to be more productive and provide them with economic opportunities on fair terms. Specific recommendations include active labour market policies, such as training and skill-development programmes, for those in informal jobs; and credit, business development services, improved technology, as well as market access and knowledge for those who operate informal enterprises.
- ii) If informal employment is a deliberate choice to avoid taxes or administrative burdens, governments should aim to establish efficient formal structures designed to encourage people to (re-)join the formal market. Countries should aim to introduce formal structures that can offer the same (or higher) levels of the flexibility and efficiency that informal channels occasionally offer. In this way, informal entrepreneurs, who frequently have strong innovation and growth potential, can more effectively contribute to the overall competitiveness of a country. Targeting those who voluntarily opt out of the formal sector also involves establishing credible enforcement mechanisms. However, many of those who have informal jobs did not voluntarily opt out of formal jobs – rather their employers in both formal and informal enterprises chose to hire them under informal contracts. Policy interventions need therefore to be carefully designed to distinguish between aspects related to employers who hire informal workers and aspects related to the informal workers themselves.
- iii) In many low-income countries, finally, informal employment is mainly a consequence of insufficient job creation in the formal economy. "Informal Is Normal?" thus also recognises the need for a general push for more employment opportunities within the formal sector. Governments should support small businesses to comply with formal requirements and encourage large companies to create formal employment opportunities.

31. A broad strategy and policy package for a gradual formalisation of informal activities would include policy measures within four major areas and may include sets of measures designed for country-specific situations and carefully adjusted for different categories of informal workers:

- i) Adapting regulations to the conditions and needs of informal entrepreneurs and workers, and providing incentives to facilitate registration and legal recognition.
- ii) Empowering informal workers through promoting organizations of informal workers and representation of informal workers in policy-making and rule-setting bodies.
- iii) Increasing the earnings and growth potential of informal workers, for example through vocational training.
- iv) Reducing the risks of informal workers and broadening access to social protection.

32. A set of broad preliminary policy recommendations for donors could be outlined at this stage, in addition to promoting macro-economic policies that encourage labour-intensive growth and to support the implementation of the policy agenda outlined above.

- i) Strengthening the knowledge base on the diverse nature of the informal labour market, including the interaction with the formal labour market. Identification of binding constraints for formalisation.
- ii) Supporting the inclusion of decent work for all into development and poverty reduction strategic processes.
- iii) Mainstreaming employment issues for informal workers into programmes in private sector development, infrastructure, agriculture and other related fields.
- iv) Supporting capacity-building for organisations of informal entrepreneurs and workers, and trade unions of informal workers. Strengthening the participation of these organisations in the strategic planning processes.

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<sup>76</sup> In 2007 the UN Secretary-General introduced a new target under Millennium Development Goal 1: to achieve full and productive employment and decent work for all, including women and young people.

<sup>77</sup> Resolution and conclusions concerning decent work and the informal economy, adopted on 19 June 2002, International Labour Conference, 90th Session, Geneva, 2002, (<http://www.ilo.org/public/english/standards/relm/ilc/ilc90/pdf/pr-25.pdf>).

<sup>78</sup> The term “informal sector” was coined by a British anthropologist, Keith Hart, in his study of the economic activities of rural migrants to Accra, Ghana in the early 1970s and was popularised and promoted by the ILO World Employment Mission to Kenya in its 1973 report.

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## VOCATIONAL TRAINING AND THE INFORMAL ECONOMY

Armand Rioust de Largentaye, AFD

### Main Messages

- Vocational training should respond to the needs of the informal economy and be inclusive, involving all relevant stakeholders
- Employment concerns should lead to strengthened links between education and vocational training.
- Vocational training should be part of a strategy to put countries on the paths of sustainable development, adequate mechanisms need to be designed that are sustainable, tailored to each situation and ensure shared responsibility between stakeholders.

1. This paper reviews six aspects of vocational training, an important policy instrument for enhancing employment. These aspects were discussed in the POVNET task team on Employment and Labour Markets during 2007 and 2008.<sup>79</sup> Boxes give excerpts from case studies discussed. Recommendations for donors appear at the end of the paper.

2. Before reviewing the six aspects, it is worth recalling that vocational training is but one instrument for employment generation and, as such, should be kept in perspective. Whereas vocational training can develop appropriate skills and thereby improve labour supply and the “employability” of the work force, demand for labour depends on incentives for investment, including prices, the exchange rate and generally, the business climate in the country.

3. In Africa, macro-economic shocks have drastically undermined employment. The deflationary structural adjustments made before the 1994 devaluation of the CFA franc had severe effects on the wage sector, with today 95% of employment in Benin and 90% in Cameroon and Senegal in the informal economy. In 2008, the world financial and economic crisis is again a major threat for employment in developing countries as well as in the developed world.

4. The **first** and arguably the most important aspect points to the fact that vocational training should respond to the needs of the informal economy and be inclusive because in developing countries people work and trade predominantly in the informal economy. During the 1990s, informal work in the non-agricultural sector represented:

- 43 per cent of employment in North Africa,
- 57 per cent in Latin America,
- 63 per cent in Asia and
- 75 per cent in sub-Saharan Africa.

5. Including traditional agriculture, the percentages were even higher. In sub-Saharan Africa, as already mentioned, percentages stood at 95% in Benin and 90% in Cameroon, Ethiopia and Senegal.

6. Two thirds of the people of sub-Saharan Africa, which total close to 800 million, are less than 25 years old, compared to 30% in Europe. Field studies show large youth cohorts entering the labour market. In South Africa, every year there are 826,000 school leavers and in Benin 200,000. In Morocco, just outside sub-Saharan Africa, the figure is 400,000. Whereas equivalent figures for annual labour demand are not readily available, the formal economy is clearly unable to provide employment in such massive quantities. Most school leavers, especially early school leavers, find an earning in the informal economy. With little access to formal vocational training, the vast majority resorts to make-shift mechanisms in the informal economy (on-the-job training, self-training or traditional apprenticeships).

7. Many technical vocational education and training systems fail because they focus on the needs of the formal economy. Contrary to a common tendency distinguishing the “formal economy” from the “informal economy” and developing different approaches for each of these “sectors”, an early concern of South Africa after the end of apartheid was to develop an inclusive approach to the labour market (Box 1).

**Box 1: Approaches to the labour market in South Africa.**

In South Africa, an inclusive labour market system and a single regulatory framework incorporating the entire labour market with the extension of protective measures to all workers in both formal and informal employment were established in 1998 under the Skills Development Act. The Act institutes:

- the National Skills Authority (NSA), representing the public authorities and the social partners, and advising the Department of Labour,
- the skills development levy, which raises 1% of the total payroll,
- the Sector Education and Training Authorities (SETAs), made up of employers and employee representatives, and covering 23 sectors: finance, banking, textiles, chemicals, agriculture, etc..

SETAs receive 80% of the skills development levy and develop training in enterprises and programmes to improve critical skills for the labour market. With the remaining 20% of the levy, the National Skills Fund (NSF) serves the unemployed and people in the informal economy.

Gender considerations are part of the concern for inclusiveness (Box 2).

**Box 2: Vocational training for women in the Indian sub-continent.**

In the slums of Delhi and Bangalore, the Decent Employment for Women (DEW) project, funded by USDOL and executed by ILO, trained 4,500 women between 2001 and 2004, after carrying out a training needs assessment. The project helped women find employment and markets for their products. An impact study showed that trained women were satisfied by increased household income. Lessons learned include:

- the special attention, time and effort required to change attitudes of trainers from formal training institutions,
- the gradual impact on the social status of women resulting from increased skills.

The Community-based training project (CBT, 2003-2005) in Bangladesh (funded by UNDP, executed by ILO) is a similar project carried out in rural areas. By 2005, over 1,000 women had completed their training which included confidence-building, technical and business skills. The project comprised a careful assessment of economic and market opportunities as well as training needs.

In Mali, the effort to address the needs of the real economy has led to support a “dual” training system (Box 3).

**Box 3: Dual training aims at addressing real needs in Mali.**

Formally introduced in Mali in 1997, dual training (*apprentissage alterné* or dual) is a training system which combines work supervised by a trained artisan (80% of the training time) and formal courses in a training centre (20%). Evaluations confirm that the dual system improves skills significantly and contributes to social inclusion and to improved employment. The private sector is now routinely involved with the Ministry of Employment in the design of programmes and in the quantification of training needs for the dual system.

A similar system is being pursued in Benin (Box 4).

**Box 4: Benin strives to make vocational training more relevant to the needs of the youth and of the informal economy.**

Benin recently reformed its vocational training policy to adjust technical and professional education (*enseignement technique et professionnel*, ETFP) to urban labour demand. The reform develops practical training in the form of dual apprenticeship (« *apprentissage dual* ») which alternates theoretical training with practical apprenticeship. A professional certificate of qualification (*certificat de qualification professionnelle*, CQP) is awarded after 600 hours of training in an education center, delivered every week for one day during a three year apprenticeship including five days of work per week in a business or artisanal workshop.

For the first time in 2006, 292 apprentices were awarded the CQP. In time, the reform will provide 3,000 CQPs per year. Nine options are or will be available : masonry, electricity, plumbing, surface preparation, cycle mechanics, carpentry, refrigeration & air conditioning, sewing & clothing and hair-dressing. The reform will also create a work qualification certificate (*Certificat de qualification de métier*, CQM) to recognize artisanal skills. The demand for this certificate is estimated at 15,000 candidates.

8. **Second**, employment concerns should lead to strengthened links between education and vocational training. While the Millennium Development Goals have focused the attention of international donors on education, links to vocational training need to be strengthened to provide youth with effective access to labour markets and include them in the productive economy with decent jobs.

9. West African countries such as Benin, Togo, Senegal and Mali are restructuring technical vocational education and training (TVET) systems to incorporate traditional apprenticeships, including certification mechanisms (Box 4), while South Africa and Ethiopia are opening their TVET systems to informal economy needs. Morocco is now explicitly addressing needs for the informal economy through its Ministry of Education (Box 5).

**Box 5: Morocco: the Ministry of Education takes on informal education.**

The Moroccan Ministry of Education recently created a Department of Informal Education to address the needs of 2 to 3.5 million school drop-outs aged – to 15. Professional insertion initiatives deal with several dozen thousand young people. The new Department also sponsors adult literacy programmes, half the workers in the informal economy having never been to school.

10. In the case of agriculture, the link that needs attention is the one between farmers and agricultural research, rather than education. Whether or not traditional agriculture is considered an informal activity,<sup>80</sup> agriculture generally offers considerable scope for improving output and income through proper training of farmers. Where small scale enterprises prevail, as in traditional agriculture, the challenge is to increase productivity and reduce vulnerability, rather than to create employment.<sup>81</sup> Hence, vocational training in agriculture is mainly pursued through extension services, which need to be properly connected to research, market intelligence and professional organisations, and to provide for adequate training of trainers.

11. **Third**, vocational training should include all relevant stakeholders. To re-establish the connection between technical education and vocational training on the one hand, and the needs of the labour market on the other, experience in South Africa (Box 1) and experiments in Morocco, Benin and Cameroon (Box 6) underscore the need to associate social partners (employers and employees) in technical vocational education and training (TVET) systems for the identification of jobs and the development of appropriate training strategies and methods.

**Box 6: Involving stakeholders in Cameroon.**

The White Book published by the Chamber of Commerce of Cameroon (*Chambre de commerce, de l'industrie, des mines et de l'artisanat*, CCIMA) in 2006 ("*Projet politique de la CCIMA pour l'artisanat du Cameroun 2005-2010*") makes a number of policy proposals to support apprenticeship, including dual training (*formations en alternance*), which alternates theoretical training with practical apprenticeship. Dual training is currently provided by GIPA, a craftsmen group of about 100 artisans in Yaounde. With German support (DED, *Deutscher Entwicklungsdienst*), GIPA works on vocational training in the urban sector and on engaging craftsmen in the training effort.

12. **Fourth**, mechanisms need to be designed that are sustainable, tailored to each situation and ensure shared responsibility between stakeholders (households, employees, enterprises and the State). Box 1 referred to the funding mechanism in South Africa.

13. **Fifth**, vocational training should be part of a strategy to put countries on the paths of sustainable development. In Morocco, for example, vocational training is coordinated with initiatives supporting the transition out of the informal economy. In addition to a number of public initiatives in vocational training, Al Amana, a private association supported by Vita, an NGO, and USAID, manages a portfolio of 260,000 micro-credits, mainly in the informal economy. Furthermore, training policies should target sectors with promising employment prospects, as in South Africa (Box 7).

**Box 7: South Africa seeks out employment opportunities.** In 2003, a Growth and Development Summit organized by the South African Government and the social partners (employers and employees), agreed to deploy all possible means to create jobs. Accordingly, the partners agreed to:

- invest more in sectors offering good job creation opportunities such as textiles, the food industry, call centres and crafts,
- improve the quality of infrastructure in transport, energy, communications, research and development, and, more generally, the business environment,
- create job opportunities in the informal economy through public works, care programmes (care for the aged and people in poor health, care for young children, school feeding), and labour-intensive environmental protection programmes (at least 130,000 jobs were created in public works in 2005),
- provide appropriate skills and better access to the job market for school leavers.

14. **Sixth**, country reviews show that vocational training systems are generally inadequate in size and inadequately relevant to the needs of the labour markets in poor countries. In many poor countries, experiments and TVET reforms are recent and generally remain small-scale. The challenge is to scale-up after the pilot phases.

**Box 8: The challenge of scaling up dual training in Mali.** The scope of the dual training system in Mali remains small, with about one thousand apprentices graduating every year, as compared to the 300,000 or so entering the labour market. Scaling-up requires:

- the extension of the system to a variety of activities;

- a better control of costs, which currently vary between 60 and 1,000 euros per trainee per annum; and
- a proper training certification system.

### **Recommendations**

15. The POVNET task team on Employment and Labour Markets concluded with the following recommendations for donors.

#### **Recognise the role and place of the informal economy**

- Use informal training systems. Such widespread systems should be carefully assessed when reforming education and vocational training.
- Use informal professional organisations to structure training demand.
- Recognize the ability of workers in the informal economy who have experience in training and improving job skills; use them as skilled trainers or experts in vocational training programmes.
- Support schemes to improve notoriously poor statistics and knowledge on the informal economy.

#### **Improve the design of vocational training programmes**

- Improve informal apprenticeship practices gradually. Best practices engage all partners concerned.
- Train adults as well as youth. Efforts to improve the quality of youth training can also benefit adult literacy and vocational training in the informal economy.
- Develop pre-employment schemes to reduce social and educational wastage. Pre-employment schemes help early school-leavers build on their education and improve employment options.
- Develop balanced funding mechanisms to make training systems sustainable. Properly designed, such systems involve the range of public and private partners.
- Support the move beyond training towards social inclusion and job creation. Means to provide such support can be intellectual (tutoring, monitoring...), practical (tool kits...) or financial (micro-credit).

#### **Emphasize education**

- Continue focusing on basic education. The attention given by donors to secondary education should not affect the need to focus on basic education. Hardly 50% of students currently complete their basic education in sub-Saharan Africa and workers in the informal economy generally have low levels of education. Gaping needs for quality improvements in basic education remain.

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<sup>79</sup> POVNET is the Development Assistance Committee network on poverty reduction

<sup>80</sup> Opinions may vary though statistical studies generally consider that informal enterprises are enterprises that cannot be distinguished from households and that don't keep accounts. See references : OECD Development Centre

<sup>81</sup> *Promoting Pro-Poor Growth: Agriculture*, OECD 2006.

## YOUTH EMPLOYMENT

Claudia Coenjaerts, Christoph Ernst, Mariangels Fortuny, Diego Rei, ILO

Markus Pilgrim, Youth Employment Network (YEN)

### Main messages

- The youth face specific barriers in the labour market; their unemployment rate is significantly higher and their employment and working conditions are worse than those of their elders, which leads to high economic and social costs for their society. Special attention must, therefore, be paid to integrating the youth better into the labour market, even more so given that their number is so high.
- Support for the youth should mainly be based on existing employment policies, complemented, where necessary, by targeted interventions and when implemented, its impact on other age groups must be taken into consideration.
- Often a supply demand mismatch lies at the root of the weak labour market integration of the youth; this is a situation that could be resolved by adopting integrated approaches that consider both sides of the labour market effectively and involve all sectors of society, including the youth, in the decision-making process

### I. Introduction

1. Youth employment has grown in prominence on national and global development agendas. The youth employment challenge has its own dimensions and confronts countries worldwide regardless of their stage of socio-economic development. The underlying problems are the large number of young people entering the labour markets every year, the lack of employment opportunities in particular in poor economies and post-conflict countries, and the low quality of education and training without a proper link to the labour markets. This paper tries to outline the dimension of the problem, the reasons why to intervene, and the possibilities of improving youth employment.

2. What are the recent global labour market trends and challenges with regard to youth?

- Today's world contains an estimated 1.2 billion young people aged between 15 and 24 years (an increase of 17 per cent compared to 1995), that is 24.7 per cent of the world's working-age population.<sup>82</sup> About 87 per cent of them live in developing economies.<sup>83</sup>
- As the youth population grew faster than both the total population and youth employment, the share of the youth who are employed in the youth population declined from 49.2 to 44.5 per cent between 1997 and 2007 and the total number of unemployed increased from 63 million to 71 million between 1997 and 2007, in particular in sub-Saharan Africa (from 8 to 10 million).<sup>84</sup>
- Worldwide, youth unemployment is high, with a global average of 11.9 per cent in 2007, *i.e.* almost three times higher than the adult unemployment rate<sup>85</sup>. Moreover, young people made up

43.7 per cent of the world's total unemployed population despite accounting for only 25 per cent of the working population. However, unemployment is only part of the problem.

- More than one-third of young people in the world are unemployed, have completely given up looking for a job (discouraged) or are working but still living below the USD2-a-day poverty line (the working poor<sup>86</sup>). There are an estimated 125 million young working poor at the USD1 threshold, which in 2005 corresponded to 20 per cent of employed young people.
- Overall, there is no significant difference between the sexes when it comes to young people's search for work. The unemployment rate for female youth is, at 12.5 per cent, only slightly higher than the male rate of 12.2 per cent.<sup>87</sup> Nevertheless, differences can be stronger in specific countries<sup>88</sup> and regions due to economic and cultural reasons and may justify gender-specific interventions. Moreover, young women are engaged more in unpaid (family, personal, reproductive) work, which affects their participation in paid productive activities.

## **II. Why special attention to youth?**

3. In view of the youth employment challenge, many governments are investing considerably in youth employment programmes, which complement general poverty reduction and employment policies. Questions arise as to what justifies these youth-specific interventions and why it is not sufficient to focus on promoting a favourable investment and business climate.

4. The following main arguments have been put forward to justify youth-specific interventions:

- Young people face specific challenges in accessing the labour market and this lowers their chances of finding decent employment. The main difficulties are: (a) a higher chance of losing their jobs during economic downturns ("last in, first out"<sup>89</sup>); (b) specific barriers to entry, often stemming from lack of experience;<sup>90</sup> and (c) path dependence: early unemployment increases the likelihood of subsequent unemployment.<sup>91</sup>
- Underutilized young people incur significant economic costs<sup>92</sup> as the national workforce is not being used to its full potential. Moreover, young people are, in general, more dynamic, often have a higher educational level than their parents. It is also mainly young people who opt for migration if they cannot find adequate employment in their own country. Underutilization of young people in the labour market can trigger a vicious circle of intergenerational poverty and social exclusion.
- Often, lack of employment opportunities may result in social conflicts, such as violence and juvenile delinquency, which, in turn, incur high social costs. Moreover, post-conflict countries have predominantly young populations without a decent job, many of them deprived of education, having grown up in violent societies and often having been combatants themselves.

## **III. How to promote youth employment?**

### ***Labour demand***

5. Resolving the problem of youth unemployment and under-employment requires, on the one hand, growth of salaried employment in the formal economy. This leads to more jobs for young people and encourages the transition from the informal to the formal economy. On the other hand, the quality of employment (e.g. productivity, working conditions) in the informal economy, where the majority of young people work, should be improved.

6. Job creation depends primarily on economic growth, which itself depends on investment, but also on the international context. A stable macroeconomic environment which boosts investment – both private and public – and thus growth, is fundamental to the creation of new formal jobs for all groups of workers, but is of particular benefit to young people, who suffer most from economic downturns because of their short job tenure and lack of experience (“last in, first out”).

7. Sectoral policies, in particular, can promote job creation in the medium to long term, provided they are well designed and targeted to sectors with high potential for employment growth. Well-targeted policies can promote private initiatives in traditionally “youth-friendly” sectors such as tourism, catering, information and communications technology (ICT),<sup>93</sup> basic and social services, including health, as well as in the sports sector.<sup>94</sup> In developing countries, 75 per cent of the youth living in poverty are found in rural areas. Rural youth is more likely to have started work in childhood. They are the favourite victims of human trafficking and sexual exploitation and are more vulnerable to being recruited by militant extremist groups. Most urban poverty, in turn, is the result of rural deprivation and resulting distress urban migration.<sup>95</sup> Therefore, special attention should be given to the agricultural sector by moving away from subsistence agriculture, and introducing commercialization and productivity improvements through technological changes and infrastructure support. The international trade and aid policy should also be taken into consideration in this context.

8. Youth in general shows a strong interest in the conservation of our planet. Environmental management also has an interesting employment potential. A successful example is a youth employment project in the Indian State of Goa. A mix of interventions based on individual motivation, use of best practices, public–private partnerships and legislative measures has resulted in the last three years in more than 2,000 jobs for young people in waste management and recycling, with opportunities for further expansion.

**Training West African youth in a growth sector:  
Corporate social responsibility and information technology**

**Background**

In 2000, Cisco, a US-based IT company, launched its Least Developed Countries (LDC) Initiative, replicating Cisco networking academies in LDCs. The Networking Academy Program is a comprehensive 560-hour course designed to provide students with the skills that will enable them to design, build and maintain computer networks. At the end of the curriculum, students can choose to pass a Cisco-certified examination.

In partnership with international donors, Cisco set out to provide Internet-based learning and IT skills training in half of the world’s 50 least developed countries. In West Africa alone, 125 networking academies have been established in 11 countries. Currently, over 9,200 students are enrolled throughout West Africa. More than 60 per cent of students are between 25 and 34 years old.

**Outcome and impact so far**

A survey of the LDC Initiative conducted in six countries shows that two-thirds of respondents found IT jobs after completing the programme and that 10 per cent started their own business. Currently, 31 per cent of students graduating from the courses are women, exceeding the target of 30 per cent.

**Lessons learned**

- The programme is successful because it covers the demands of a growing sector. The

IT industry estimates that sub-Saharan Africa will have 400,000 vacancies in this sector in a few years' time due to a lack of qualified specialists. Closing such skills gaps is probably the quickest way to combat youth unemployment.

- The cooperation between a private company and public donors leads to wide outreach and demand-driven training programmes.
- Fees being charged for the courses improve the sustainability of the academies. However, they might inhibit the access of poor youth, although reduced rates are offered for unemployed.
- Limited access to electricity and fast Internet is a hindrance to the Initiative's expansion, especially in rural areas.

*Source:* "Building the Case for Business Collaboration on Youth Employment. Good Practices from West Africa" (forthcoming [www.ilo.org/yen](http://www.ilo.org/yen)).

9. The public sector can also influence youth employment directly through public spending. Employment-intensive investments, such as in infrastructure or construction, will create employment opportunities in sectors dominated by young people. In 1989, with the support of the African Development Bank and the World Bank, the Senegalese Government set up a USD33 million public works programme for young workers in labour-intensive activities such as construction, rehabilitation and maintenance of public services. These activities were subcontracted to small and medium-sized enterprises. In total, 350,000 temporary jobs and even 6,000 permanent jobs have been created per year through 3,226 projects. Strong political support, clear objectives and continuous development assistance have been the key elements for success. On the negative side, the programme has not provided training for young participants and has targeted mainly urban areas (UNECA, 2005).

10. Nevertheless, it is the private sector that is the main driver for growth and job creation. Entrepreneurship is a driving force for initiating business ideas, mobilizing human, financial and physical resources for establishing and expanding enterprises and creating jobs. Entrepreneurship is another way of unleashing the economic potential of young people. The promise of youth entrepreneurship can be maximized through programmes and strategies that address the barriers to doing business. Young people face particular challenges because they lack appropriate skills and experience, are less creditworthy, and have more difficulty in accessing business networks and sources of information. A burdensome business environment is difficult for all, but as youth have generally less knowledge and experience of business regulations and related legal and institutional frameworks, this constraint can discourage them from venturing into a business career and so increase the risk of business failure.

11. Societies that appreciate entrepreneurship, and thus promote its values and norms, can create a dynamic and vibrant class of young entrepreneurs. Empirical evidence shows that educating young minds in enterprising behaviour and boosting their confidence for calculated risk-taking, increases the incidence of entrepreneurship being adopted as a career option. The successful development of youth business hinges upon good access to well-integrated services such as management training, business mentoring programmes, financial services, support in gaining access markets and networking opportunities. Enhancing their capacity in association building and policy advocacy can address this disadvantaged position. Young women entrepreneurs face additional hurdles, as in many cultures they are influenced to be even more risk averse, while their roles in the family and society keep them from tapping opportunities in business development. This also means that they are more likely to be in the informal economy and less likely to be entrepreneurs employing others.

## **Youth entrepreneurship: The case of Shell LiveWIRE International**

### **Background**

Shell LiveWIRE was initiated in Glasgow, United Kingdom, in 1982, as a programme to encourage the young to develop their own businesses. Today, it is a global community initiative which considers self-employment as a viable and desirable career option. The programme is active in 25 countries across the globe, including: Argentina, Brunei Darussalam, China, Hungary, Ireland, Iran (Islamic Republic of), Mauritius, Nigeria, Oman, Pakistan, Romania, Singapore, South Africa and Sri Lanka.

LiveWIRE involves a combination of information, training, counselling and mentorship for over one million young people annually. Each national programme receives significant support from the Shell oil company and a range of corporate sponsors, often combined with government assistance.

### **Outcome and impact so far**

Since 2000, over four million young people have been in contact with the LiveWIRE programme. Currently, one million young people are in touch with the programme each year worldwide and 200,000 young people undertake some form of training.

Results may vary across countries. Specific stocktaking for the United Kingdom indicates that, since 1982, 600,000 young people have explored the idea of starting their own business; approximately 16 per cent of all enquiries led to a business start-up; as a result, three to four jobs are created by each business start-up; and 65 per cent of new start-ups are still trading four years later.

A similar exercise carried out in Oman showed that the "Intilaaqah Oman" programme currently trains and supports over 5,500 young people each year. Thirty-seven per cent of participants over the last 12 years still run an enterprise, and nearly all the remaining participants are in private or public sector employment or further studies. In Oman, 54 per cent of participants are young women, which shows the gender sensitiveness of the programme. Ninety-five per cent of Intilaaqah-supported businesses are in the formal sector, and most generate an income far greater than what is possible in the public sector.

### **Lessons learned**

There are some intrinsic factors of success in the LiveWIRE programme, such as:

- **Open accessibility:** It is available to all, irrespective of socio-economic status, such as educational level or gender. The only eligibility qualification is an interest and motivation in pursuing the enterprise option.
- **Standardization of programme elements and processes:** The impressive and successful reproduction of LiveWIRE as a youth enterprise initiative across the globe is in part due to a well-tested formula for youth entrepreneurial development. New countries embracing the model have been able to "leapfrog" on others' experiences and extensive product development.
- **Attention to national identity and cultural sensitivity and collaboration with local partners:** Whilst there are common elements and values, in each country LiveWIRE reflects the culture, needs and the resource opportunities of that country. Prior to the establishment of a programme in any country, in-depth country research is carried out to identify local needs, opportunities and critical business development issues.

*Source:* Kenyon, 2008.

12. Higher volatility and lack of work experience are strong reasons why entrepreneurs often shy away from hiring young people. Wage subsidies<sup>96</sup> and/or reduction in payroll taxes for enterprises that hire inexperienced young workers seem to be the best options to counterbalance these concerns of employers and, therefore, increase the demand for young workers.

### **Labour supply**

13. On the supply side, a well-linked educational and training system (*e.g.* the “dual system” combining school-based education with work-based training and apprenticeship, recently introduced in various African countries) and closer cooperation between this system and the private sector facilitate a smoother transition from school to work. Often, the educational system does not provide the appropriate labour force needed by the domestic market. This mismatch may generate a lengthy process to get a good job in the domestic market. Therefore, young people’s employment opportunities are often limited to the informal economy, which may lead to frustration, or even make them opt for migration (*e.g.* the “educated unemployed”), while there are unfilled vacancies in other technical jobs in the country.

14. Education and vocational training should be designed around the informal economy, where most young working people are found in developing countries. Often, vocational training has to be complemented by remedial education, as many young workers in the informal economy may have dropped out of the educational system at an early stage. Young people may have begun working prematurely, while still children, through economic necessity (*e.g.* AIDS orphans in some African countries may have become heads of households and breadwinners) or cultural constraints. As a result, they lack basic skills, including literacy and numeracy.

15. Nevertheless, these young informal workers acquire technical skills in informal activities but, as these skills are often not recognized officially, they face difficulties to have access to better jobs. Recognition and certification of skills acquired through informal channels are key elements in this regard. In addition, young people often do not know which profession to join and where to look for a job. Special youth labour market information and employment services, as well as early career guidance, may facilitate their entry into the labour market and help avoid a mismatch between youth labour supply and demand.

16. With regard to labour market institutions, in particular employment protection legislation (EPL) and minimum wages, it has been argued that these increase youth unemployment by making labour too expensive. And yet, recent evaluations do not provide a clear indication of the impact of these measures on young workers. In fact, some recent studies have even challenged this.<sup>97</sup> Moreover, many young people in developing countries work in the informal economy, where EPL and minimum wages have a rather limited impact. The question is not whether or not to regulate, but what kind and what level of regulations are appropriate to get the best forms of protection for young people without inhibiting firms from hiring.

## **Republic of Congo: Vocational training and the value of assessment**

### **Background**

ONEMO, an experienced national employment agency operating under the Ministry of Labour, was selected to execute a vocational training programme for young people formerly associated with armed forces and groups and assist them with employment placement and self-employment. From the beginning, ONEMO was convinced that the future for these young people would be in farming and had already started a series of preparations for agricultural training. Nevertheless, to their great surprise, most young men elected to participate in skills development programmes in construction-related occupations, such as masonry, welding and electricity, whereas women preferred tailoring (14) or hair-cutting (15). As a result, time and resources were wasted on the preparation of agricultural training and preparations for construction training started late into the process.

### **Outcome and impact so far**

Finally, ONEMO managed to put together a six- to nine-month training programme in cooperation with the Coeducational Technical School based in Owando, followed by a three- to four-month internship with building companies established in this area. After successful training and internship, most young men (26) found a job in construction companies working with the Owando municipality, which benefited from a promising local economic development initiative.

### **Lessons learned**

- Assessing market opportunities and understanding the expectations of young people are crucial to programme planning. A major difficulty initially was the lack of market opportunities assessment and of a pre-registration beneficiary survey prior to vocational training and guidance.
- Fortunately, the municipality initiative represented a real market opportunity, corresponded in great part to the capacities and aspirations of the youth and had received enough prior media coverage to grab their attention.
- Even though in this case interests and expectations matched market opportunities, often young people face constraints to making realistic decisions as they may lack reliable information sources.

*Source:* ILO, 2007.

## **The need for an integrated and participatory approach**

17. Experience shows that youth employment programmes and policies aimed at refining labour market dynamics often result in interventions that are fragmented, too narrow or isolated and do not fully take into account the general economic, institutional and social framework. Inconsistencies may arise in terms of the content of the interventions, their level, geographical location and target beneficiaries. Moreover, supply-side measures tend to outweigh demand-side measures. Anecdotal examples of improvable interventions include skills training programmes not backed by an appropriate demand for skills in the labour market, or entrepreneurship training without any possibility of gaining appropriate

access to credit. It is, therefore, indispensable, in the domain of youth employment, to dispose of an overarching, integrated strategy for growth and job creation. This strategy covers labour demand (job opportunities) and supply (employability), as well as the mediation or matching process, combined with well-targeted and structured interventions. A life-cycle approach to youth employment is also highly useful as it recognizes that what happens at one stage is affected by, and in turn affects, opportunities at other stages.<sup>98</sup> For example, premature entry into the labour market as a child lessens the chances for better employment in adulthood because of their lack of education.

18. Youth employment policies must be embraced by the broader context of a country's employment and growth policy, considering possible crowding-out effects on other age groups. Productive employment and decent work for young people requires sustained, determined and concerted action by a wide number of actors. As they cannot stand on their own, youth employment interventions must be linked to broader development frameworks. Coherence and coordination between relevant government agencies and other national and international (*e.g.* donor community) stakeholders is crucial. While not necessarily the only mechanism, the use of national action plans (NAPs) for youth employment can be useful to facilitating this. To be successful, however, these plans should have strong and sustained political commitment and be based on broad participation. In this context, it is important that youth also participate actively in the decision-making process, as they know best what they want and what they can offer. The participation of young people in membership-based organizations and their engagement in decision-making processes affecting their employment and working conditions is crucial to fostering social inclusion and advance democratization. Young people are often under-represented in these processes. A good example is the consultation of youth in PRSPs in Ghana, Honduras, Indonesia and Uganda.<sup>99</sup>

## **National action plans on youth employment as a tool for policy advice**

### **Background**

In 2002, the Youth Employment Network (YEN), an interagency partnership of the UN, ILO, and World Bank, introduced the lead country process on youth employment as a tool to raise awareness on this important topic. One key precondition for being accepted as a lead country by YEN is to commit to the preparation and implementation of a national action plan (NAP) on youth employment. The NAP provides a coherent set of policies and programmes to improve youth employment and should be integrated in national development policies and budgets. YEN offers technical assistance for drafting a NAP through its network.

### **Outcome and impact so far**

YEN started with five lead countries in 2002, and today 18 countries have volunteered as lead countries committed to formulating NAPs. Of these 18 countries, seven are at the development stage; four have no current activity; one has drafted the document; and six are at the implementation stage. Only one country is currently embarking on an evaluation of its NAP. YEN's work led to UN resolutions encouraging member States to prepare NAPs and submit them to the UN Secretariat for analysis and follow-up in 2005. In total, 41 NAPs were submitted. NAPs are also implemented even outside the YEN framework.

### **Lessons learned**

- NAPs are a strong advocacy tool to put youth employment on national development agendas.
- So far, there are no clear minimum requirements to be fulfilled for becoming a lead country and for adopting NAPs. The risk is that NAPs remain just lip-service in the face of a pressing problem, without real commitment to implement.
- Little is known about outcomes and impacts of NAPs, solid monitoring and evaluation plans and their underlying indicators are usually missing in NAPs. YEN therefore recently initiated a benchmarking initiative on youth employment policies aimed at establishing a regular peer review process among lead countries on their performance in youth employment. Future support has to focus on providing technical assistance on how to measure this performance.

*Source: [www.ilo.org/yen](http://www.ilo.org/yen)*

## **IV. Conclusion**

19. The energy, skills and aspirations of young people are invaluable assets that no country can afford to squander. Helping young people to realize their full potential by gaining access to productive employment and decent work is, therefore, a pre-condition for poverty eradication, sustainable development and lasting peace. Youth employment programmes can provide useful support to young people who are facing specific barriers in the labour market. Their underutilization has economic and psychological costs and may cause social conflict. Nevertheless, youth programmes have to be designed with caution to avoid crowding-out effects on other groups of workers.

20. Even though little evidence exists on existing youth employment initiatives, the following policy recommendations for the donor community can be put forward:

- i) Donors should support country-led efforts in various policies that are contributing to an improved labour market situation for the youth. Genuinely national commitment for the promotion of youth employment requires the strong involvement of large sectors of society: Firstly, a greater participation of the youth within their own organizations or as representatives in other organizations, and also of key social actors such as CSOs, trade unions and the private sector, as well as closer cooperation with, and among, Ministries and other public institutions.
- ii) Youth employment issues could often best be resolved with already existing employment policies, which could be adjusted to youth-specific needs such as youth entrepreneurship, remedial education and vocational training. Targeted interventions could, however, be useful under specific circumstances. Nevertheless, it is important to take into consideration the possible crowding-out effects on other age groups.
- iii) Often a mismatch between the demand for young workers and the supply, the availability of appropriately skilled workers, has been at the roots of their weak integration into the labour market. Supply-side interventions are most effective when they meet current demand on the labour market, for example, for skills development in high-growth sectors. An integrated approach (e.g. national action plans on youth employment), where not just the Ministry of Employment/Labour, but also other key Ministries, address the issue of youth employment, could be helpful in this regard.

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82 ILO, 2008a and c.

83 UN, 2007, Statistical Annex.

84 ILO, 2008c.

85 ILO, 2008c.

86 ILO, 2006.

87 ILO, 2008b.

88 In particular Latin America and the Caribbean, the Middle East and North Africa, ILO, 2005.

89 See O'Higgins, 2001, and Godfrey, 2003.

90 These specific barriers are: (i) lack of labour market information and job search experience; (ii) aspirations of youth and their parents which do not match the realities in the labour market; (iii) lack of experience and capital for self-employment; and (iv) lack of diversified working experience.

91 See Clark and Summers, 1982; Freeman and Wise, 1982.

92 Employment difficulties experienced by young people also causes psychological problems, even though this issue is not at the core of this paper. They may suffer from reduced self-esteem, discouragement leading to drug and alcohol abuse and related health problems

93 Some countries in South-East Asia, such as Hong Kong (China), India, Republic of Korea and Malaysia, particularly benefited, at all levels of the value chain, by concentrating public investments in this sector (Curtain, 2002).

94 As noted in the 2003 report of the United Nations Inter-Agency Task Force on Sport for Development and Peace entitled "Sport for development and peace: Towards achieving the Millennium Development Goals", the sector was valued at USD36 billion worldwide in 1999 and predicted to expand by 3 to 5 per cent annually. The sector generates employment in the manufacture of sports goods, sports-related services, infrastructure development and sports events, along with related opportunities linked to spectators, sponsors, vendors and the media.

- 95 ILO, 2005.  
96 World Bank, 2007.  
97 Freeman, 2005; Cazes and Nesporova, 2003; Godfrey, 2003.  
98 ILO, 2005.  
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## PROMOTING EMPLOYMENT FOR WOMEN AS A STRATEGY FOR POVERTY REDUCTION

Elsebeth Krogh, and Thomas Nikolaj Hansen (cowi consult), Susanne Wendt and Morten Elkjaer, (Danish Ministry of Foreign Affairs)

### Main messages

- Place women's economic empowerment prominently on the agenda in high-level policy dialogue with Governments
- Engage with and support government authorities, employers' organisations and trade unions to promote gender sensitive labour market reforms and reduce the costs of doing business to facilitate women's entry.
- Support organisations that promote women entrepreneurs in informal and formal economy and non-state actors in sensitising governments to the need for tackling cultural and social barriers.
- Facilitate increase in supply of gender-sensitive business development opportunities and increase and diversify access to finance for women, including microfinance.

### Why is employment important for poverty reduction

1. Employment is often described as the most important link between economic growth and poverty reduction. Providing income earning opportunities through wage employment or self employment for poor women and men is crucial to raising incomes and overcome poverty. However, currently women across the developing world enjoy limited access to fair and decent work compared to men.

2. Two main arguments are presented in current debates on women and economic empowerment. The *right-based argument* focuses on increasing women's job opportunities and their freedom to work in security and dignity. The *economic argument* emphasises women's economic capacities and potential contribution to economic growth. The economic argument draws on the fact that women tend to reinvest their income in improved nutrition, health and education for household members, thus increasing living standards and reducing 'non-income poverty' in the long term. The Decent Work agenda of the ILO supports both arguments in combining the poverty reduction agenda with the fundamental right to work in freedom through the four pillars: Opportunities, Rights, Protection, and Voice.

3. Gender discrimination at the labour market has a significant cost. For Asia it has been estimated that gender discrimination costs up to USD80bn a year due to restriction on women's labour market participation and access to schooling (UNESCAP, 2007;). Furthermore, as documented by Costa and Silva in a study of selected Latin American countries, removing gender-based barriers to the labour market would lead to a significant reduction in the poverty rate (Costa and Silva, 2008).

4. The purpose of this paper is to identify issues keeping women in developing countries out of decent employment and point to strategies that donors may consider when designing interventions for improving women's employment opportunities.

### Facts about women and employment - Three Imbalances

5. Women's participation in paid, non-agricultural employment has continued to increase slowly. But women are still more likely than men to access low-paid, low-productivity and vulnerable jobs with no basic rights, social protection nor voice. According to a recent ILO report, the status of women at the labour markets throughout the world has not substantially narrowed gender gaps in the workplace (ILO, 2008).

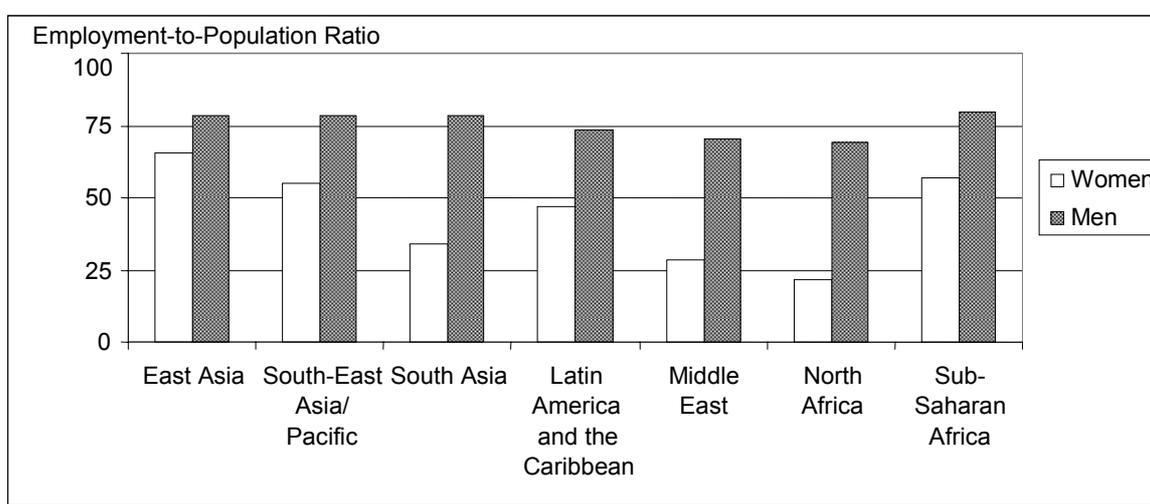
6. Women's economic empowerment currently faces three major challenges: women are less likely to have a paid job; women's jobs are more likely to be concentrated in the informal economy<sup>100</sup> and in low value-added sectors; and in low-paid jobs characterized by poor working conditions.

### Women face a significant gender gap in employment - especially in South Asia, the Middle East and North Africa

7. The gap between female and male employment worldwide is still significant. According to ILO estimates, the share of employed people in the world's working age population (the employment-to-population ratio) was 49.1 per cent for women and 74.3 per cent for men in 2007 (ILO, 2008).

8. The difference in the female and male share of employed people in the working age population is above 40 percentage point in South Asia, the Middle East and North Africa. At the other end of the spectrum, the gaps are below 20 percentage point in East Asia. As documented in a recent cross-country study of 18 sub-Saharan countries, countries with the highest male employment ratio also tend to have the lowest gender gap (Kolev and Sirven, 2007).

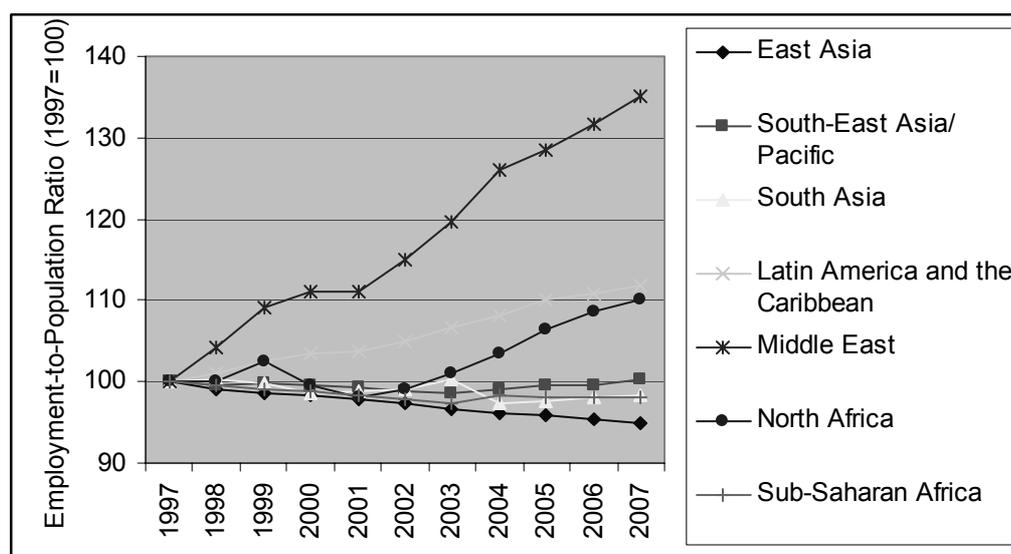
**Table 1 - Employment-to-Population Ratio (2007 preliminary estimates)**



Source: ILO, 2008

9. Closing the gap? The Middle East has managed to increase the female employment-to-population ratio by more than 35 per cent during the period from 1997 to 2007. The ratio has also increased by almost 10 per cent in North Africa and Latin America and the Caribbean, while some regions have even seen a slight decrease, notably sub-Saharan Africa, South Asia, and East Asia (ILO, 2008).

**Table 2- Female Employment-to-Population Ratio (1997-2007; 1997=100)**



Source: ILO, 2008

### Women are under-represented in the formal economy and in high value-added sectors

10. In developing countries six out of ten women work in the informal economy often as self-employed. Many of these women are domestic workers or informal factory workers, while others are unpaid workers in family enterprises and family farms. The poorer the region, the greater the likelihood that women work in the informal economy as unpaid contributing family members or low-income own-account workers.

11. Agriculture is the primary sector of women's employment. Women constitute 41 per cent of the total employment in the agricultural sector. The regions with the highest proportion of women in the agriculture sector are East and South East Asia, the Middle East and sub-Saharan Africa (ILO, 2008).

12. In South Asia, Northern Africa, and Middle East women only constitute one in five of waged workers employed in the non-agricultural sectors (United Nations, 2007). It should be noted however, that some non-agriculture sectors are dominated by female workers. For example in Bangladesh, two out of three workers in the export-oriented garment industry are women (World Bank, 2000). In regions such as Latin America, the Caribbean, and in South-East Asia women constitute close to or above 40 per cent of workers in the non-agricultural sector (United Nations, 2007: 12). Furthermore, the public sector tends to employ more women compared to the private sector, but women in the public sector tend to work in low paid jobs in social sectors such as education and health.

### Women face a decent work deficit

13. The ILO Decent Work Agenda advocates for productive opportunities with a fair wage, rights and recognition, personal development, fairness and gender equality (ILO.org). Many women working in both the formal and informal sector have a substantial "decent work deficit":

14. Women's earnings are well below those of their male colleagues. Kolen and Sirven's cross-country study of sub-Saharan African economies finds a significant gender pay gap: The average female-to-male weekly income gap ranged between 23 per cent (Burkina Faso) to 79 per cent (Ghana), while women in Malawi earned slightly more than men (2007:12). According to UNIFEM, gender differentials in hourly earnings are common and apply to most types of employment, especially among own-account

workers, while the gender ratio is more balanced for employees in the public sector (2005: 49). The gender pay gap can to a large extent be explained by lower level of education and by the fact that women are more likely to work in informal jobs. Controlling for the level of education, Kolen and Sirven find that among workers with no education men earn almost three times more than women, while the gap is nearly closed with respect to workers with tertiary education (2007; 16-17).

15. Women's work related to domestic obligations in the family and unpaid contribution to family-run businesses is largely invisible in the statistics and of low status. Important efforts to document this type of work have been done by UNIFEM - including the unpacking of the term 'unpaid care work' which refers to the provision of services within households, for other households and community members. Although often not recognised as such, it is 'work' meaning that 'the activity has a cost in terms of time and energy and arises out of a social or contractual obligation, such as marriage or less formal social relationships' (UNIFEM, 2005).

16. Women are often engaged in employment with high degrees of insecurity. Lack of recognition of women's work is often reflected in discrimination against women in regard to access to the labour market and working conditions once women are part of the labour market (wage differentiation, benefits, maternity leave, promotion) and skewed pension laws once women leave the labour market. For example, female workers in the garment industry in Bangladesh have typically been employed to "exploit the comparative advantages of their disadvantages, like the low price of their labour, their lower bargaining power and their docility" (World Bank, 2000). In areas with high prevalence of female-headed households due to *e.g.* out-migration of men, poor women can be forced into the sex industry and be exposed to HIV/AIDS and violence.

### **Key factors at play - and possible solutions**

17. Even though gender patterns of employment are caused by a variety of factors, which differ by *e.g.* region, sector and type of employment, there are a number of structural causes of a more general nature. These include social and cultural barriers to women's employment, and the extent to which political and legal frameworks are conducive for women's employment. Key issues and proposed solutions in relation to the three main gender imbalances identified in the previous section are presented below, building on experiences from different parts of the world.

#### **Factors behind the gender gap - barriers to women's employment**

18. The general gender gap is explained by multiple factors. The most important among these factors are social and cultural patterns keeping women out of the labour market as well as a tendency of government authorities to invest too little attention and resources in promotion of women's employment:

19. Women are "time poor". Due to the gender division of labour in the family prevailing in many countries, women's responsibility for unpaid household labour leaves only few hours daily for engaging in work outside the household (UNIFEM, 2005). The situation is further aggravated in cases where women are the sole head of household. Women's ability to free up time depends to a great extent on the availability of services and infrastructure such as potable water, good access roads etc.

20. Cultural beliefs and norms may keep women out of the labour market. In many cultures there is little or no acceptance of women taking up employment - in society, in families, among employers and even among women themselves. In many rural areas of Afghanistan for example, women do not have permission to leave their house, let alone take a job outside the household (IRIN, 2007). In sub-Saharan Africa early marriage is common and often seen as a key factor why women fail to access the labour market. The OECD database on Gender, Institutions and Development confirms this by looking at a

broader set of factors related to discrimination against women (OECD, 2008a). Using a combined measure for family code, physical integrity, civil liberties and ownership right, the OECD finds that discriminatory institutions have a direct impact on women's economic development (OECD, 2006). Finally, it should be noted that customary norms and lack of access to information often prevent women for claiming their rights and exploiting opportunities.

21. Women lack the basic education to effectively participate. Girls are still excluded from education more often than boys, particularly in West and South Asia (United Nations, 2007) and more so for secondary education, vocational, and tertiary education. This education gap has implications for the ability of girls and women to access economic opportunities later in life. The rapid increase in women's labour force participation rate noted in the Middle East over the past decade has coincided with massive investments in education (ILO, 2008).

22. Finally, many governments have failed to demonstrate explicit leadership and political will to supporting employment for women. Often promotion of women's participation is vested with resource-poor ministries. For example in Ghana, where the Ministry responsible for gender issues, the Ministry of Women and Children's Affairs, remains "severely under-resourced, and is left to draw on a network of gender desk officers consisting mostly of junior officers with little capacity to influence decision-making" (IFC, 2007). Likewise, Poverty Reduction Strategy Papers typically make reference to the importance of gender mainstreaming, but often fails to set specific targets for outputs and outcomes or make specific budget allocations to advance these priorities.

### **Recommendations and good practice - reducing employment gender gaps**

23. No simple solutions are available to reduce employment gender gaps, especially in regions where the gaps are deeply rooted in norms, cultural and social practices and further consolidated by poor infrastructure and service delivery. It has been recognized however, that economic growth that increases demand for labour has the potential for having a real impact on women's employment. Donors can contribute towards reducing gender gaps by cooperating with government authorities, the private sector and civil society to strengthen the supply of and demand for policies and programmes favouring women's access to the labour market.

24. *Place women's economic empowerment more prominently on the agenda in high-level policy dialogue with Governments and in implementation instruments related to the Paris Declaration and the MDGs.* A more prominent gender focus in poverty reduction strategies and private sector development strategies will set an example for the society at large and facilitate a stronger resource allocation to this area.

25. *Support non-state actors in sensitising governments to the need for tackling cultural and social barriers.* Private sector organisations, business chambers and NGOs could be supported to strengthen the demand for gender sensitive laws regarding inheritance and ownership, and conduct awareness raising programmes on women's rights to decent employment etc. Another modality is to support networking and facilitate organisation among women. Simple awareness raising programmes targeting women have in many cases triggered positive effects on women's participation in economic development.

26. In Guatemala for example the World Bank has carried out a land titling project to make women aware of their legal rights including the right to register land. As a result, women's land ownership has increased to 45 per cent in the project areas - compared to 8 per cent for the country as a whole (IFC.org).

27. *Facilitate girls' access to primary and secondary school enrolment and attendance.* While primary and secondary schooling not necessarily is an entry ticket to the labour market *per se*, it remains a

fundamental building block for interventions such as awareness raising programmes, vocational training etc. Moreover, increasing girls' level of education will contribute to decreasing the pay gap between men and women. Persuasion, advocacy and awareness raising will often be required, in combination with stipends or other financial support to motivate families to send their daughters to school, even though in most cases, education systems do not discriminate between boys and girls in terms of access.

28. In Bangladesh the World Bank supported Bangladesh Female Secondary School Assistance Program, led to a secondary school enrolment increase from 1.1m to 3.9m girls through the provision of tuition stipends (World Bank, 2007d).

### **Factors keeping women in low value added sectors**

29. Women's tendency to work in low value-added sectors is, as outlined below, due to the existence of legislative and regulatory barriers as well as women's lack of skills and access to finance and business development services. However, many of the social and cultural factors discussed in the previous section also influence which type of employment women get involved in. For example, as documented by the OECD, the percentage of women participating in the paid non-agricultural labour market is generally higher in countries where women get married relatively late in their life cycle. (OECD,2006). Likewise, in a recent study, OECD notes that single women are more likely to be employed in the formal economy, while women with children are more likely to be employed in the informal economy (OECD, 2008b).

30. The costs of doing business often prevent many self-employed women from getting into business. To facilitate entrepreneurship among women, a considerable effort is required to streamline procedures for business registration and licensing, export permits, procedures for payments of taxes etc. Female entrepreneurs further have to struggle with the fact that legislation and tradition in some cases prevent their access to (and control of) productive resources, notably land.

31. The supply of gender sensitive business development services and finance is inadequate. To promote female entrepreneurs, gender sensitive business development services such as training, support to development of business plans and availability of business incubators catering to women are required. While microfinance is clearly a promising instrument for mobilising micro-scale entrepreneurs, it is still difficult for women to graduate to the next level and access loans from commercial banks (World Bank, 2007e; f).

32. Women in low value added sectors lack skills to access other sector. As evidenced by countries such as Singapore, Taiwan, and Malaysia an increase in vocational training is a precondition for countries to make the transition from low to high-value added production (World Bank, 2007a: 162)

### **Recommendations and good practice - increasing women's employment in high value-added sectors**

33. To increase the share of women in high value added sectors within the formal as well as the informal sector immediate impacts may be achieved through simplification of legislative frameworks. In regard to medium and long term strategies, donors are encouraged to finance further research on the structural reasons why the majority of women are engaged in the informal sector. Finally, donors should work with government authorities, training institutions, private companies, NGOs and commercial banks to increase women's participation in non-agricultural sectors.

34. *Support organisations that promote women entrepreneurs in informal and formal economy with capacity development and basic infrastructure.*

35. *Reduce the costs of doing business to facilitate women's entry by removing barriers for business registration, business licensing, acquisition of land etc. To ensure that future policies and regulations take*

such issues into consideration, some countries are conducting Regulatory Impact Assessments with specific emphasis on gender aspects on a pilot basis.

36. Recently, Lesotho made land registration easier for women by allowing married women to transfer land without their husband's signature. Moreover, many developed economies such as Australia, Canada and New Zealand have demonstrated that introducing simple measures for business registration may have a significant, positive impact on the number of women registering their own businesses - a finding that has been confirmed by a pilot project in Entebbe, Uganda. The pilot project, which has been granted an international investors award, succeeded in reducing the time spent by Ugandan businesses in obtaining licenses by 90 per cent while revenue went up by 40 per cent. The pilot triggered a wave of first time applications from women. (World Bank, 2006b: 42).

37. *Facilitate increase in supply of gender-sensitive business development opportunities.* In order to expand the range of employment opportunities for women, skills and capacity development such as technical skills in agriculture, private sector etc. may be introduced. Specific initiatives in skills development may also address gender disparities in education and training, e.g. vocational training. Institutionalisation of incubators specially targeted towards women could be an area with significant scope for development of public-private partnerships.

38. In China, the Tianjin Women's Business Incubator was set up to benefit female micro and small-scale enterprises. Through a USD2m investment from the Chinese Government, UNDP, AusAID, and the All China Women's Federation, the scheme benefitted almost 50 women-owned businesses - and as a result close to 3000 jobs were created (IFC.org).

39. In Tanzania, TUCTA (Trade Union Confederation of Tanzania) is implementing a programme to improve the rights of women market vendors which includes collective bargaining with the municipalities to provide a safer working environment and prevent sexual harassment from customers, promote management training, provide business premises at affordable rents, improve knowledge of legal rights etc.

40. *Increase and diversify access to finance for women, including microfinance.* Microfinance has clearly proven to be an effective tool in facilitating women's access to credit. Supporting development of new financial products, such as longer term loans, could assist women in expanding their businesses.

41. The micro-finance sector in Africa is relatively weak in coverage and performance compared to other regions. While the number of micro-finance institutions has evolved as steadily as other regions, the MFIs in Africa have not reached out to as many people as in Asia or Latin America. By the end of 2006, MFIs in Africa were reaching around 11 per cent of the poorest households in the region, compared to 68 per cent in Asia and 20 per cent in Latin America.

42. While typical micro-finance schemes may not reach the poorest of the poor, experience from a Bangladeshi programme - Challenging the Frontiers of Poverty Reduction (CFPR) - has shown that women can also be economically empowered through small grants offered in combination with skills development, health services, and general awareness training (BRAC and Aga Khan Foundation, 2006).

43. Looking towards the better resourced women, the real challenge is to create incentives for commercial banks to offer credit to women graduating from micro-finance schemes. This is an issue currently being explored by the Global Banking Alliance for Women (gbaforwomen.org).

### **Factors keeping women in low quality employment**

44. In many countries, informal sector jobs are synonymous with female employment and associated with low status and poor working conditions. Consequently the factors keeping women in the informal

sector also imply that women continue to face poor working conditions. In addition, as outlined below, women may continue to face poor working conditions due to flaws in labour market legislation. Poor compliance of labour market legislations at the work place and weak enforcement mechanisms may also contribute to keeping women (and men for that matter) in jobs with poor working conditions:

45. Many women are not guaranteed decent work conditions due to flawed labour market legislation. Working conditions with direct impact on women, such as equal wage, maternity leave, and pension are in many cases not properly addressed. For examples in the case of Uganda, the labour laws date back to colonial times and do not address issues such as discrimination, sexual harassment, and maternity leave and pay (World Bank, 2006b).

46. In many instances workplaces do not consider gender aspects in working conditions and organisation. Many employers, especially small and medium sized enterprises lack the knowledge, skills and motivation to put in place working conditions that are attractive to women. This includes measures such as flexibility in working hours and place of work, accessible means of transport, affordable quality child care facilities, bath and toilet facilities and access to training and education. Occupational safety and health (OSH) is another concern for female workers. According to a recent IFC study, international experiences indicate that OSH regulation based on prescriptive and enforced regulation does not significantly reduce the rate of accidents - and the administrative cost of such regimes are very high (World Bank, 2007b: 92). On the other hand, experience from trade unions shows that OSH is a good entry point for dialogue as it can lead to a win-win situation in terms of improved working conditions for workers and improved productivity for employers.

#### **Recommendations and good practice - reducing women's decent work deficit**

47. All steps designed to increase women's integration into the formal labour market will by and large have a positive impact on women's working conditions. In addition to the steps proposed in the previous section, women's working conditions may be further improved by adopting and implementing adequate labour market legislations.:

48. Engage with government authorities, employers' organisations and trade unions to promote gender sensitive labour market reforms. Promoting labour market policies, legal changes, compliance with ILO conventions and good corporate practices can improve access and working conditions for women through tri-partite processes and strengthening capacity of the tripartite organisations to promote gender equality in the labour market. A useful starting point could be to identify obstacles to women's decent employment.

49. In 2004 Tanzania adopted a new employment and labour relations act which prohibits discrimination in the workplace on the basis of gender, sex, marital status, disability and pregnancy. It requires employers to put in place, report on, and register with the Labour Commissioner plans to promote equal opportunities. It also introduces maternity leave and contains provisions protecting a mother's right to breastfeed and to be protected from engaging in hazardous employment (World Bank, 2007b). When advocating for labour standards it is important to strike the right balance between labour protection and job security, on the one side, and the need for employers to have flexibility, on the other side.

50. In 2003, after a 15 year struggle, domestic workers in South Africa were finally brought under the Unemployment Insurance Act covering employed workers. This requires employers to register their domestic workers and pay a monthly levy to a Fund. Workers also contribute. The Fund covers unemployment, maternity, sickness and death. Enforcement of the law is a problem, but there is evidence emerging of positive results in some areas. Statistics from the official disputes resolution body, the Commission for Conciliation, Mediation and Arbitration (CCMA), show fairly extensive usage of the

disputes resolution machinery by the domestic sector. Latest statistics (April-December 2003) show that 12 per cent of all referrals were from this sector, second only to the retail sector. The majority of cases referred are about dismissals – 85 per cent between 1999 to 2003.

51. Through a combination of union campaigns and negotiations in a statutory tripartite (plus community) forum, workers rights and protections have been extended to a large numbers of vulnerable women workers in South Africa. This includes the right to organise, bargain collectively, access the dispute resolution processes and be protected from dismissal. It includes minimum conditions of employment such as leave, sick leave, maternity leave (although unpaid), overtime pay, prevention of discrimination, affirmative action and access to skills development. It applies not only to workers with full time employment and a single employer, but also to part-time workers and those with multiple employers. Recently, minimum wages were legislated through sectoral determinations for domestic and agricultural workers. Such determinations are made for “vulnerable” workers, where collective bargaining forums are not in place.

### **The Way Forward - Partnership**

52. In order to become effective, the solutions proposed above need to be adapted to specific contexts, involving actors relevant to the specific situation. It is possible, however to outline some general recommendations. Governments, the donor community and the private sector should seek to increase market demand and economic opportunities through increased investments targeted at labour-intensive industries and labour-surplus areas, supportive trade policies that protect these industries, as well as provide more and better linkages between formal firms, informal firms and informal workers.

53. A specific focus should be on reforming the financial and other economic institutions that affect working women, including reforms in the regulatory environment, to include one-stop registration and progressive fee structures. In the policy environment to address biases that favour formal firms/workers over informal firms/workers and men over women. Financial institutions should introduce simplified borrowing and collateral requirements and extend savings and insurance products, and urban policies and planning needs to include information enterprises and workers in the allocation of urban space, resources and contracts.

54. Organizations of working poor women into membership-based organisations, such as unions, cooperatives, and other associations accountable to their members and representation of these organizations in relevant policy-making and rule-setting institutions are important to ensure women’s voice in decision-making processes. To ensure visibility of women’s employment, there need to be an official recognition of the economic contribution of working women through improved labour force and other economic statistics. Additionally, working women should be recognized as economic agents and their membership-based organizations should be considered as legitimate representative institutions. These are all essential enabling conditions for economic empowerment of women.

55. Finally, the guiding principle for any donor should be partnership with national drivers of change, including government authorities, private sector representatives, employers’ organisations, trade unions, NGOs and other development partners. Gender equality and women’s empowerment are also being promoted in relation to *aid effectiveness*, as seen in *e.g.* the April 2007 Dublin workshop on development effectiveness in practice (OECD, 2007c). Any strategy should be well founded in national development strategies and have ownership from the most important change agents. In consequence, the first step is to carry out joint analyses to identify needs, opportunities, threats and key drivers of change.

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<sup>100</sup> Informality is not *per se* a problem, it is a way of being and working for the vast majority of the working poor, especially women. The real problems lie with the institutions that make it difficult for informal enterprises to register, deny them the benefits of formality if they do encourage informal wage employment, and thereby deny legal protection to millions of workers.

## MIGRATION AND EMPLOYMENT

Jeff Dayton-Johnson (OECD Development Centre), Antje Pfeiffer (GTZ),  
Kirsten Schuettler (GTZ), Johanna Schwinn (Consultant)

### Main messages

- Policies toward international migration and employment in developing countries must be more coherent, given the many interactions between the two phenomena. But more coherent policies require a much better understanding of the links and impacts between mobility, jobs and development.
- More coherent policies should be pursued by means of stronger partnerships between origin and destination countries – with special attention to brain-drain and circular-migration issues.
- Remittances will contribute more to job creation if policies help create stronger incentives to save and invest in migrants' home countries – including, notably, in community-development projects.

### 1. Summary

1. Social, economic, political and environmental problems are root causes for migration. Regarding the labour market, migration is a symptom of imbalances in sending countries, such as high rates of unemployment and underemployment among low-skilled workers, low wages for skilled workers, and unmet demand for education and acquisition of skills.

2. International migration can help reduce poverty and raise economic growth rates in the migrants' countries of origin. First, an increase of remittances is generally associated with a reduction of overall poverty. Second, circular migration plays an important role. Economic analyses show that an increase in circular migration between developing and developed countries could produce gains of USD 150 billion per year, which would equally benefit developed and developing countries.

3. While the link between migration and economic development receives special attention, the particular dynamics of migration and its effects on the labour markets of sending countries are still poorly understood due to the lack of reliable data. However, initial empirical evidence shows that the labour markets in sending countries adjust to emigration in different ways, depending on the scale and type of migration and the country's general socioeconomic state.

4. The effects of migration on employment have many facets. The migration of low-skilled workers might result in rising wages or a relaxation of the local labour market in areas with high rates of emigration and an oversupply of labour. The outflow of skilled workers deprives developing countries of their human capital and results in brain drain with serious consequences on the delivery of key services like education or health care, and on economic productivity. In contrast, overseas work experience might provide opportunities to improve skills and further knowledge, while others whose qualifications are not recognised in their receiving country may see their skills diminish while abroad, making return difficult.

5. To grasp the variety and complexity of these relationships, more data must be collected and appropriate tools developed to detect and analyse the effects of migration on labour markets and employment. Considering the manifold links between migration and employment, migration policy has to be coherent and complement policy fields of education and vocational training, economic promotion and the labour market, all of which should be aware of the situation of (potential) migrants.

6. The option of re-entry of migrants into developed markets on renewable short-term contracts, flexible working arrangements and the protection of fundamental rights provide positive incentives for circular migration. To restrict and prevent the migration of professionals from sectors affected by brain drain, 'ethical recruitment' practices and measures to improve working conditions and infrastructure for high-skilled personnel in developing countries should be tied in with the acquisition of professionals from sectors exposed to brain drain.

7. On-the-job training and skill acquisition schemes affecting migrants' employability and knowledge transfer can also supplement circular migration. Additional training programmes in sending countries provide incentives for professionals to stay and thus help cushion the loss of expertise. Diaspora networks play an important role in reducing the costs of brain drain by fostering cooperation and the conveyance of knowledge and skills as well as collective and business investment.

8. The migrants' families often use remittances primarily to finance their livelihoods, rather than to invest productively. Some job creation will occur through the local multiplier effects of spending remittances for consumption and to secure livelihoods. This increases local employment while the saving of remittances can counterbalance local insurance system deficiencies. Given the limited scale of the positive employment and multiplier effects of remittances, some policies seek to encourage the use of remittances for more productive investments. This however requires more effective incentives for productive and employment-oriented investments in the economy, the reduction of transfer fees and better access to financial institutions. A further tool is government co-funding of diaspora-driven non-profit investments.

## **2. The relevance of migration to employment and labour markets**

9. In 2005, around 190 million people (3% of the world's population comprising almost equal proportions of men and women) lived outside their country of birth. This proportion has remained relatively stable for several decades. The imbalance of active populations between developed and developing countries will however increase. The World Bank projects that by 2010 the active economic population of developed countries will increase by 50 million people compared to an increase of 733 million people in developing countries.

10. There is increasing political focus on the consequences of international migration for economic and social progress in the migrants' countries of origin. For instance, in September 2006 the United Nations held the first High Level Dialogue on International Migration and Development. This led to the creation of a Global Forum for Migration and Development (GFMD). The GFMD first met in July 2007 in Belgium and the second meeting took place in the Philippines in October 2008. Furthermore, several multilateral organisations (such as OECD, ILO and World Bank), the European Union and many bilateral donors ascribe higher importance to migration issues in their research and policy agendas.

11. It is increasingly accepted that international migration can help reduce poverty and contribute to economic growth in the migrants' countries of origin. According to a World Bank study an average increase of 10% of emigrants in the total population of a developing country is associated with a 1.6 percentage point reduction in poverty (using an international poverty line of USD 1 per day). Moreover economic analyses show that an increase in temporary migration in developed countries, including low

qualified migrants, could produce gains amounting to USD 150 billion each year, equally shared between developed and developing countries. Meanwhile, a 10% increase in the share of remittances in Gross Domestic Product (GDP) is associated with a reduction of poverty by 1.2%. However if migration leads to a significant loss of skilled labour to more developed economies (brain drain), international migration might have negative impacts on sending countries.

12. The connection between migration and employment, as a dimension in the link between international migration and economic development is therefore important for poverty reduction, and of interest to policy-makers in migrant-sending and migrant-receiving countries. One major reason for migration is the earnings gap between the host and the home country; hence most of the migrants leave their home countries for more remunerative work. Studies by the International Labour Organization (ILO) show that workers in high-income countries earn a median wage that is almost five times the level of that in low-income countries, adjusted for differences in purchasing power. However the earnings of migrants in their host countries are lower than those of native workers as migrants often lack the necessary qualifications and knowledge of the local language.

13. Another important reason for mobility is education and the acquisition of skills which are also related to employment and labour markets. Migrants come from all educational levels. Educated migrants have better prospects for the advance of skills and knowledge. The improvement of skills and the accumulation of financial capital from working abroad or by activities of the diaspora could have positive effects on the labour market like increased employability and the capacity to start a business in the country of origin. Yet these effects might be hampered when the upgrade in qualification does not match local needs or when economic and political conditions remain unattractive for investments.

14. International migration furthermore has effects on the labour market outcomes for many potential migrants or non-migrants in developing countries. These effects need to be better understood by decision-makers. Empirical studies on the link between migration and employment in developing countries do not show a clear picture and most of the theories are not quite satisfactory. However, social contexts in developing countries play an important role in establishing theories, which could be tested empirically and used for policy recommendations.

15. Mobility, whether temporary or permanent, has also always been used as an adaptive measure in times of environmental stress. Experts affirm that environmental deterioration exacerbated by climate change and the recurrence of natural hazards is likely to increase migration. However it is hard to attain detailed and reliable data on this issue since it is difficult to measure the extent to which climate change influences people's decision to move. Furthermore, migration can hardly ever be related to environmental degradation alone (Boko *et al.*, 2007).

16. The purpose of this hot topic paper is to explore the links between international migration and employment and labour markets in developing countries. It also provides concrete recommendations for governments of developing countries and development assistance agencies. While it is difficult to draw a line, this paper attempts to focus on the channel of labour markets and employment instead of systematically surveying the many effects of migration on development. It also does not address the effects of international migration on the labour markets of migrant-receiving countries of the OECD and elsewhere.

17. If people from a developing country participate in the global labour mobility system, labour markets and employment in that country will be affected through several channels. Five such channels are considered here:

*(a) Emigration, wages and economic adjustment*

- (b) Brain drain and labour markets*
- (c) Effects of remittances on labour markets*
- (d) Diaspora networks and labour markets*
- (e) Return migration and employment*

18. Chapter 3 briefly explains the labour market consequences of each of these mechanisms. Chapter 4 highlights important gaps in our knowledge about these five mechanisms that hamper effective action by practitioners and policy makers. Chapter 5 presents selected implementation experiences as examples of good and bad practices while a list of additional experiences can be found in the annex. The paper concludes with some general recommendations for policy makers and development agencies.

### **3. Main facts and figures and current knowledge about the issue**

19. This chapter sketches the principal channels through which international migration affects employment and labour markets in developing countries. Some of these are related to the actions of the migrants themselves, including sending remittances and other activities of the diaspora (notably forging trade and investment links between countries of origin and destination). The migrants' return – whether temporary or permanent – can likewise generate benefits in their home countries' labour markets. Labour migration might have a negative impact on economic development when high-skilled migration leads to a substantial loss of human capital (brain drain) in strategic sectors like health care.

#### **Gender aspects of migration**

Women and girls have long accounted for a large proportion of all international migration. While the EU reflects the global trend of increased 'feminisation of international migration' (Lucas 2005) with a portion of 52.4%, the proportion of female migration to the US is below 45% for most migrant groups.

Women's participation in migration differs among migrant groups and receiving countries. For example, within the Japanese or Filipino migrant groups in the US more than 60% are women, whereas in the Gulf States only about one-fifth of the South Asian non-national population are female. However the role of women in migration should not only be seen in the context of their situation in host countries, but also the responsibility they shoulder when only male family members migrate.

#### *(a) Emigration, wages and economic adjustment*

20. In many, if not most, low-income countries open unemployment is relatively rare. This is partly due to the absence of adequate social safety nets that make it impossible to be 'unemployed' as defined by OECD countries. Generally most of the open unemployment in developing countries can be found in urban regions. In rural agricultural areas it is mostly hidden, as a subsistence economy functions as a kind of social safety net against poverty albeit a vulnerable and unproductive one.

21. Generally labour markets in many developing countries are marked by low wages and high rates of unemployment and underemployment among the low skilled. In contrast, studies mostly deal with the impact of high-skilled worker migration, which is expected to most affect the further development of sending countries.

22. When wages rise with economic development in sending countries this often leads to higher migration rates, as people need minimum assets to “afford” migration. If economic growth continues to be high in sending countries and income differences approximate, regional disparities will be significantly reduced and migration will decrease in the further course of development. This development is often described as a “migration hump”. While this is important to decision-makers at policy level and in development cooperation, there is scarce empirical evidence to support this theory.

23. The impact of emigration in an environment of low wages and underemployment is complex. On the one hand, studies present unskilled migration as generating huge gains for migrants, their families and their country and is seen as a component of development policy. Unskilled migration may be an instrument to relax the labour market in the sending country and induce large amounts of remittances. Conversely, it is the emigration of skilled workers that deprives developing countries of one of their scarcest resources - human capital - thus hampering the progress of more productive industries and services.

24. For many reasons wages might not rise with emigration. The evidence from a number of countries (for example Sri Lanka) suggests that high emigration rates are not necessarily associated with rising wages or even declining unemployment (OECD, 2007). The first question is whether labour supply is reduced by emigration. Some of those who are left behind and have not been working before could enter the labour market (like women, older persons, the underemployed and the hidden unemployed). In the long run emigrant workers could be replaced by technology, by more skilled workers or by migrants from other regions of the country itself or from neighbouring states.

25. Additionally if an economy is well integrated in the global economy, wages may not change because traded goods can substitute reduced output. In some cases wages might even fall if for example, emigration numbers are so high that demand and output fall.

26. Over time, an economy undergoing significant emigration will adjust with consequences for labour markets. Historically many high emigration countries witnessed the mechanisation of agriculture following emigration. This was an adjustment to the reduced availability of low-skilled labour to work the fields. Generally, production techniques will change to use combinations of various levels of skilled labour and other factors of production (land, machinery and natural resources). This will change the wage structures and job characteristics.

27. Nevertheless emigration is sometimes accompanied by rising wages in some sectors in the country of origin. Evidence from Pakistan, Philippines, Mexico, Malawi, Mozambique and other economies supports this (OECD, 2007). Whether wages rise or unemployment or underemployment levels fall, this is good news for poorer workers who do not migrate. These wage-unemployment effects are potentially powerful ways for migration to reduce poverty via the labour market, even for non-migrants. They are not always discernible at the national level; wages will rise or underemployment will fall only in those local labour markets affected by high rates of emigration. Of course in the short term if wages rise, this will increase the cost for employers. The long-term effect of rising wages depends upon how the economy adjusts to emigration.

*(b) Brain drain and labour markets*

28. With regard to the skill levels of migrants, the numbers differ between migration to Europe and North America (OECD and non-OECD countries). The majority of migrants to Europe are low skilled, while most migrants to North America possess higher qualifications (45%). Most of the low-skilled migrants who come to OECD member countries are originally from Latin America and the Caribbean, Asia, Eastern Europe and to a lesser extent, Africa.

29. Skilled migration can result in brain drain, (a decrease in human capital stock), which requires long-term efforts to be balanced by education and training. Brain drain can cripple the delivery of key services, especially in education or health care. It is estimated that 65 000 African-born physicians and 70 000 African-born professional nurses were working in a developed country in 2000. They accounted for one-fifth of African doctors and one-tenth of African nurses in the world (Michael *et al.*, 2007). With the exodus of teachers, nurses, doctors and engineers the focus tends to be on the consequences for service delivery, which may be the most important consequence related to poverty reduction. Brain drain nevertheless has at least two labour market aspects which policy-makers should focus on.

30. First, one of the reasons why skilled workers emigrate is because they are dissatisfied with labour market options at home. This is not solely a matter of pay differentials between rich and poor countries, although those differences in earnings certainly influence skilled migrants. For example, evidence from Africa suggests that many emigrants trained as health care workers were not working in that sector at the time of their departure. They had emigrated from the health care sector before they emigrated from their countries. Their decision to leave the sector in which they were trained reflects dissatisfaction with working conditions, infrastructure and pay. To retain these skilled workers these labour market conditions must be addressed.

31. The second labour market effect might be called the "keystone worker" effect. This is slightly technical and deals with the interaction of high-skilled and low-skilled workers. The emigration of skilled workers might affect labour markets if work organisation or production technology for goods and services require a certain number of skilled workers in combination with low-skilled workers. If a key worker in a firm leaves, this could reduce the productivity of his former co-workers. They are "keystone" workers; without them some firms might reduce their scale of operations or fold. Eventually, the economy might re-adjust. This however will take time during which many low-skilled workers might see their working conditions (for example, nurses in an overstretched clinic where all the doctors have left) or earnings diminish.

32. Not all movements of high-skilled emigrants from developing to developed countries cause brain drain. It depends on the social, political and economic situation of the sending country how emigration has an impact on its labour market. If we take a look at remittances made by Filipino doctors, it seems that they more than compensate for the cost paid by the state for their education. The consequences of remittances on the sending country's labour market are discussed in the next chapter.

*(c) Effects of remittances on the labour market*

33. In 2006, the officially recorded remittances sent by migrants to developing countries amounted to nearly USD 200 billion, doubling over the last five years. If unrecorded flows are added to this, the total amount of remittances to developing countries is likely to be larger than foreign direct investment (FDI) and more than twice as large as official development assistance (ODA). However remittances and aid do not generally flow to the same developing countries. While sub-Saharan Africa receives more than USD 25 billion annually in aid, it receives only about USD 8 billion in remittances. Conversely countries that receive high remittance volumes (many of them middle-income countries) receive scant aid namely, Mexico, China and India.

34. Most policy interventions related to remittances have addressed two concerns: reducing the cost of transfers and attempting to channel these flows into a wider array of uses. Neither of these is directly related to labour markets though they may have an impact on employment.

35. Surveys on the use of remittances in many countries suggest that the migrants' families use these resources primarily to finance consumption instead of investment. For poor households consumption can

certainly improve their quality of life. Moreover many categories of consumption are in fact investments in these households' futures and their human capital: for example, spending on health care, education, and consumer durables like refrigerators. The spending of remittances generally – whether for consumption or investment – will generate some job creation through local multiplier effects.

36. Remittances as a means for insurance purposes and private investment capital for people who cannot afford to migrate should not be overlooked. By serving as insurance for their families, migrants make up for the lack, or inadequacy of, local insurance systems in areas where incomes are highly variable, diseases are more common and severe, or where political, economic and/or social instability is greater. They also allow families to engage in activities that entail more risk but are potentially more profitable. This is especially the case in poor countries where capital market imperfections reduce the options available to members of low-income classes. The decline in the level of risk exposure, after the sending of remittances, may allow the household to undertake a risky – but profitable – investment project, thus contributing to economic growth. Here remittances will be relatively more productive in a distorted economic environment. This also means that altogether the share allocated to investment is relatively low. However as this is the reality in most developing countries it should be noted that migration and remittances can be associated with new insurance and investment possibilities for those who stayed home.

37. Who sends more remittances – high-skilled or low-skilled migrants? The existing literature on this point is not fully clear. However the volume of flows seems to be a function of the average skill levels of migrants, as noted above. Remittances from less qualified migrants reduce poverty more than those from high-skilled migrants. This is especially if the high-skilled migrants settle abroad permanently with their families. However in the case of the mainly educated and urban middle class Afghan diaspora in high-income countries, we see high commitment for many years. This could partly be due to its organisational strength and the persisting problems back home. Moreover the size of remittance flows depends on the duration of the migrant's stay: under this hypothesis, shorter-term migrants maintain a stronger link to the home economy and therefore send more money home, while second generation migrants tend to have weaker ties to their family back home.

38. Finally, remittance receipts have encouraged many households to reduce their labour supply and use remittances as a substitute for farm earnings. They are better off not working given the low productivity of other available options. From a macroeconomic perspective, policy makers might want to consider the effects of this reduction in available labour supply. In most cases if better paying and more productive work were available for these members of migrants' families, they might prefer to work in addition to receiving remittances.

*(d) Diaspora networks and labour markets*

39. In countries with a longer migration experience, diaspora networks (with low and highly qualified workers) may act as conduits of transnational linkages. These links include business investment – in both directions – between their home and host country. FDI and outsourcing of production financed by the overseas diaspora can generate employment prospects that might benefit the poor in the long run. Diaspora members also purchase land or houses in their country of origin, finance construction of schools, clinics or roads in their home villages and donate money for income-generating development projects. Moreover, diaspora networks between host and home countries can play a major role in sharing their skills, experience and knowledge with those who have remained at home.

40. There are mixed employment impacts of the diaspora networks' activities. China has benefited from ethnic Chinese entrepreneurs overseas who invested on a large scale within Chinese regions creating many jobs and expanding export performance. It is estimated that nearly half of the USD 41 billion FDI China received in 2000 came from its diaspora. The Indian software industry benefited from a well placed

diaspora in the US reducing reputation barriers to trade. It is easier to recruit additional skilled workers and it improves the general business relationship between US and Indian software firms. So the Chinese and Indian diasporas clearly have had a positive economic impact – including employment generation – on their respective home countries whereas the economically successful and well-organised Armenian diaspora has contributed less to developing its home country. The differences in these outcomes partly reflect the different attitudes of the local elite toward their counterparts in the diaspora: the domestic Armenian political and business elite have pushed for economic liberalisation and privatisation while keeping the major reform benefits mainly for themselves. The Chinese and Indian elite meanwhile have been more accommodating of investment finance from the diaspora.

41. Some policies have sought to encourage the use of the diaspora's resources for investments such as firm start-ups or community development. Their success will depend on the character of investments, though there are reasons to suspect that the overall impacts on employment will be modest. Start-up enterprises, many of which will be small scale, might primarily generate jobs for other family members. Community infrastructure investment is likely to be more labour intensive but such efforts will often call upon community members to donate their labour. Development projects initiated by migrants also contribute to the creation of income-generating activities on a small scale. The impact of diaspora involvement on the local level can nevertheless be important.

42. In situations where the overseas community is large or notably wealthy, the diaspora may retain significant influence on politics in their home country through absentee voting or lobbying. This indirect political influence may sometimes impact economic development. The consequences of these interventions are mixed. If it leads to violence or civil war the local economy is harmed. Several post-war countries however emphasise the migrants' contribution to local development and stabilisation. The Afghan diaspora in the USA and Europe for example, exerts great influence on political reforms and has played a significant role in private sector development. Successful attempts to promote democratisation to accelerate economic development often depend on the willingness of the ruling elite in the country of origin to interact with the diaspora. Liberia's government for example actively encourages remittances and volunteering of migrants for concrete development outcomes and even held a forum on diaspora engagement in 2008.<sup>101</sup>

*(e) Return migration and employment*

43. The return of expatriates to their home country supports economic development and job creation when returnees bring capital and knowledge back with them. Studies suggest that return migrants often have better employment possibilities than those who stayed home. They are also more often self-employed thus potentially contributing to employment generation and economic growth. Meanwhile other migrants have seen their skills diminish while abroad and have problems re-integrating into their home country's labour market. This is the experience of skilled migrants whose qualifications are not recognised when they migrate. After a period of working in a low-skilled job, they may find upon their return home that they are unable to find employment even in the field in which they were employed. Central and Eastern Europe provide many such unfortunate examples (OECD, 2007). A general difficulty arises in interpreting the evidence for this link. The re-entry often involves a process of searching for the best opportunities in the domestic labour market. Until now, it is unclear how long returnees have to search for a new job. There is also a big difference between the home countries of returnees regarding the need for social networks to find new jobs.

44. Temporary and circular migration share the benefits expected from return migration especially regarding skill and capital accumulation and their use upon return. Return on a regular or occasional basis may encourage brisker economic activity. Migrants are more likely to return if the investment and employment climates improve. Policies that foster strong R&D environments and infrastructure are

attractive, particularly to high-skilled workers (although low-skilled workers might also be lured back home by improved employment opportunities).

#### 4. Key issues and debates

45. Practitioners and policy makers need better information to reap the gains and limit the risks of international migration of workers in the developing world. This chapter highlights some of the gaps in understanding the links between migration and employment. Case study research of specific migration experiences provides critical answers.

46. Compared to OECD countries, definitions used in developing countries are often unclear. Statistics of unemployment or remittances for example, are handled differently in OECD and in developing countries. There is also knowledge and data lag because of irregular migration. The same applies to definitions of unemployment and underemployment.

##### *(a) Emigration, wages and economic adjustment*

47. More statistical data and analysis is needed to better understand the impacts of migration on employment. We need to understand better the regional and country specific backgrounds of migrants, information on the size of high or low-skilled emigration, the length of stay, the migrants' skill level, educational and economic background, their employment status before emigration, and whether they worked in the formal or informal sector. This information helps determine what happens when circular migrants return. For example, do they enter or re-enter the informal economy?

48. Assessing specific effects that occur in a given labour market are of particular interest to policy-makers. The size of unemployment and underemployment and emigration varies among countries as do the impacts of migration regarding wage and relaxation of the labour market. One question is whether, and how, governments should facilitate internal labour mobility to adjust to emigration flows. This depends on how employers actively adjust to emigration pressures like labour scarcity and/or higher wages. Do they go into new areas of activity, invest in new techniques or move to new regions in the country? Policy-makers and employers alike need to determine the kind of skills and training initiatives needed for potential migrants and remaining workers in an economy strongly affected by emigration. Such measures also need to be part of the discussion on brain drain.

##### *(b) Brain drain and labour markets*

49. To curb brain drain, countries need to know which sectors often lose highly-skilled workers. The departure of professionals influences the performance and capacity of a country in many ways (for example, in service delivery and productivity). One point that is overlooked is the incidence of sector emigration prior to actual physical emigration. If such correlations were studied, the findings would strongly influence the interpretation of the social costs of the brain drain. They would also bring us closer to understanding the labour market situation and to recognising which incentives or employment programmes are needed to retain highly qualified migrants.

50. Another case in point is the interrelation between education and migration: it needs to be analysed for each country whether highly skilled people leave their country to receive further education or whether education is a vehicle to exit a country with a lagging economy.

51. A number of studies propose the concepts of circular and temporary migration as potential tools to forestall the definitive loss of human capital. These concepts will need to consider that a temporary intention often leads to permanent stay. Overall, it is not clearly known the extent to which temporary migrants acquire new skills and financial assets and their impacts on employment. The countries of origin

should analyse what highly skilled migrants think about such migration schemes and their potential to motivate return.

*(c) Effects of remittances on the labour-market*

52. Remittances are one of the top themes of the positive effects of migration. However there is still no coherent definition of remittances or methods to measure their flow. Data on the share of remittances in GDP vary among different providers. Furthermore, many migrants use unofficial ways of transfer and the amount of such unregistered remittances can only be estimated.

53. The recipient households are most likely to use the transferred money for consumption and insurance compensation and to a lesser extent, for investment. To know the size of the multiplier effects arising from this, it is necessary to carefully map the job-creating potential of household spending in various categories (current consumption, household improvements, consumer durables, education, health and community investment). Apart from difficulties in measuring multiplier effects, sustainability depends on whether the increased demand for goods can be met by local production or requires imports.

54. Finally, more evidence is needed on the extent and the areas in which remittances contribute to the creation of enterprises and have effects on employment. Are start-ups financed by remittances usually part of the formal or informal sector? Do they have a wider employment scope beyond the family working unit and what should be done to encourage this?

*(d) Diaspora networks and labour markets*

55. For sending countries it is of vital interest to not only tap the financial resources but also the human capital migrants acquire while abroad. In the past there have been several initiatives in this direction in the form of skills and information exchange networks (see chapter 5). However it is unclear how to effectively leverage the migrants' expertise for a country's development. The countries of origin also need to know whether there are members within the diaspora matching professional vacancies back home. Opportunities to fill positions with diaspora members, particularly those with skills that are scarce in the country of origin, could be tapped through these networks.

*(e) Return migration and employment*

56. Knowledge on the magnitude of return flows is not easily obtained partly because return can be both permanent and temporary.

57. A prime concern lies with the potential benefits return migrants bring to employment and the labour market. Where return migrants can raise sufficient capital, evidence suggests that they are more often self-employed compared to non-migrants (Mattoo and Amin, 2007). To measure the effects on the labour market it is important to examine whether migrant entrepreneurs can afford to employ non-family members as well (Wahba, 2003). Furthermore, research needs to look at which political, social and economic factors encourage return and company foundation.

58. Little is known about the returning migrants' experiences of re-entry into the labour market. Leading questions are, for example, in which sectors they are mostly employed and whether jobs are formal or informal. Another interesting point is to see if the new work relates to the job they were doing abroad and to what extent returnees can apply and benefit from the knowledge and experience they gained abroad.

## 5. Examples of good and bad practice

### a) *Emigration, wages and economic adjustment*

#### *The Canadian Seasonal Agricultural Worker Programme (SAWP)*

59. A number of programmes aim at regulating the supply of labour for seasonal agricultural migration starting with the demands of the receiving country. The Canadian Seasonal Agricultural Worker Programme (SAWP) is widely viewed as a best practice model running for over forty years to facilitate labour migration between Canada and a number of Caribbean countries and Mexico. Key strengths include the involvement of all stakeholders in the process and close supervision of selection and evaluation, the protection of fundamental migrant rights and fair wages.

60. When employers have reported their request for labour, recruitment agencies in participating countries carry out the selection and screening of foreign workers. Costs arising from transportation, visa requirements, housing and health insurance coverage are partly borne by the employer. There is however a limit up to which costs may be deducted from a worker's paycheck. The wage is calculated according to the guidelines set on minimal wage and the wage for such agricultural work paid to Canadians. Migrants' rights and obligations are outlined in the contract but there are some flaws in their realisation. Given that contract renewal depends on the employer's approval, migrants may choose not to make full use of their rights in case of illness or long working hours. Furthermore, legal provisions and pressure from employers in some places make it difficult for migrant workers to organise in agricultural unions.

61. For labour migrants, the programme has proved effective since it opens access to seasonal migration and income remittances, without recruitment fees and the risks of unauthorised migration. Once in the labour pool, there are relatively good chances of being re-employed the next season, which might also be an explanation for the low rate of overstayers. More importantly, temporary migration with prospects of re-employment provides a relatively stable and predictable level of income and resources that may potentially be invested into productive activities back home.

#### *The Philippines Overseas Employment Administration (POEA) and the Overseas Workers Welfare Administration (OWWA)*

62. The Philippines has an interesting example of a government-driven policy to promote temporary labour migration which is regulated and implemented by the Philippines Overseas Employment Administration (POEA) and the Overseas Workers Welfare Administration (OWWA). According to the POEA, the main office serves an average of 3 000 potential migrants on a daily basis. The two government agencies provide services to facilitate overseas employment, including overseas work placement and the establishment of contracts, preparatory courses on social and work conditions abroad, and medical insurance and pension plans. They also maintain databases on skills and foreign employers hiring Filipino workers.

63. The provision of a credit card that allows cheaper and easier sending of remittances via private banks is another incentive to encourage labour migration through official channels and to reap the benefits. Repatriation assistance is provided to encourage return and there are a number of re-integration schemes like counselling, skills training, educational assistance, preferential access to business loans and investment advice.

64. Despite these efforts rates for undocumented and permanent migration are high and impacts on employment in the Philippines are mixed. Remittances and skills are rarely invested into business start-ups and employment at home. Additionally, a culture of migration seems to arise since return is only temporary and viewed as waiting time between the last and the next deployment abroad. Social costs in terms of

family unity and income inequality between migration-affected households and non-migrant families also increase. Migration is increasingly viewed as a tool for social mobility, with potential implications for education becoming a vehicle for migration and brain drain.

65. Clearly, the Philippine government has managed to formulate a consistent and ambitious labour migration policy providing a wide range of services to facilitate and encourage temporary migration. However there is a need to better leverage the benefits expected from migration for the country's employment and economic development (O'Neil, 2004).

#### *H-2A Temporary Agricultural Worker Programme*

66. To meet the critical shortage of domestic agricultural workers the US government launched the H-2A programme for seasonal labour. The reception and use of the programme by American growers has been very modest due to complex administrative requirements, delays and costs. Farmers complain that they have to cover workers' housing, transportation, visas and other fees, which in the end makes the programme uncompetitive to undocumented farm workers who make the major share in agricultural jobs. One criticism is the slow processing of requests that often result in the serious undersupply of workers at harvest season. The H-2A programme also shows that complex bureaucratic procedures, for example regarding applications for re-entry or for multiple 'unnamed' farm workers, are unattractive (Los Angeles Times, 2007).

67. In the beginning of 2008, the US Department of Homeland Security which is also involved in managing the programme proposed several modifications to streamline the hiring process under the H-2A programme in a systematic and timely fashion.<sup>102</sup>

#### ***b) Brain drain and labour markets***

##### *TOKTEN UNDP Programme in Lebanon*

68. The Lebanese people have been emigrating from their country since the 19th century. The outbreak of the war in 1975 caused a huge outflow of migrants. This massive emigration wave during the war included a high proportion of highly qualified persons. The incentives for Lebanese to emigrate remain high, particularly in view of the prevailing economic slowdown and high unemployment. In the absence of official statistics, estimates vary and the figure of outflows of more than 100,000 persons per year at the end of the 1990s is cited as conservative. Men constituted the majority of people who migrated during this period (85%), and emigration affected the skilled and better-educated segment of the population more.

69. The TOKTEN programme was launched in Lebanon to mobilise successful emigrants to undertake short-term consultancies in their countries of origin, with UN support. It added a dimension of technical cooperation that contributes to reducing the negative effects of brain drain. This programme supports positive contribution through the circulation of know-how and transfer of funds from abroad to the countries of origin, including the dissemination of skills and experience of diaspora members. The programme has set up a database of Lebanese professionals in various fields of specialisation and established links with Lebanese associations abroad as well as with university research centres.

#### ***c) Effects of remittances on the labour market***

##### *GeldtransFAIR.de*

70. The GeldtransFAIR website was developed to allow migrants in Germany to better compare the various services for money transfers to their countries of origin. It provides migrants with information on services offered by banks and other money transfer institutions. This makes the remittance market more

transparent and increases competition. The goal is to shorten the time taken for transfers and to reduce fees. This way, money transfer via formal channels will become more attractive and more money will be sent safely to the migrants' families.

71. Initially the website focused on money transfers from Germany to Albania, Ghana, Morocco, Serbia, Turkey and Vietnam. Today the website offers information on 26 countries regarding prices and the time required to complete a transfer with different providers (banks and money transfer operators), ways to transfer money (electronic or cash transfers) and other aspects of sending money abroad.

72. The German website was developed under the provisions of a joint project between the Frankfurt School of Finance & Management and the German Technical Cooperation (GTZ), commissioned by the German Federal Ministry for Economic Cooperation and Development (BMZ). The website was launched in November 2007 ([www.geldtransfair.de](http://www.geldtransfair.de)). Several other European countries (for example France, Netherlands, Norway, Spain and the United Kingdom) have developed similar websites.

*The connection between remittances and financial services and the development of specific financial products*

73. The Mexican government promotes the coalition of rural credit cooperatives and savings banks that are affiliated to a transfer network comprising 20 money transfer companies. This allows receiving households in rural areas to open up savings accounts and to better access micro-credit schemes, thus improving their 'financial literacy'. Moreover the additional funds in the rural banking system provide more resources for micro-credit.

74. The Ecuadorian Banco Solidario has developed special financial products and services for migrants and their families. The programme 'My family, my country, my return' offers loans to settle debts and to finance small businesses from abroad as well as home loans and foreign currency accounts. Another key element is the bank's arrangement with three major banks in Spain and one in Italy that allow migrants to access micro-credits in the host country and to send remittances at special rates. The Bank also works with cooperatives in rural Ecuador to ensure that families in the villages can obtain remittances.

75. There are special saving products where migrants place investments at a fixed interest rate during their time being abroad while the capital is used to finance micro-credits in their home country. The Economic Resource Centre for Overseas Filipinos (ERCOF) in the Philippines promotes one such example.

*Migration and local and regional economic development in Honduras (BMZ/GTZ-IOM cooperation)*

76. In early 2007 following first initiatives on remittances GTZ launched the "Transnational Bridge" pilot project in cooperation with the International Organisation for Migration (IOM) in the region of Intibucá (Honduras). This was within the scope of a programme on income and employment promotion commissioned by BMZ. Besides a study that underscored the relevance of migration to the sustainable development of the local economy, the Honduran partners' enthusiasm led to activities promoting the integration of migrants into local development.

77. Among others, the activities concentrated on the formalisation of financial transfers through the bancarisation of migrants and their families. Another key element was the consultation process to the Honduran government regarding the introduction of a pilot programme promoting collective remittances by migrant associations for infrastructure investments in Intibucá.

**d) Diaspora Networks**

*South African Network of Skills Abroad (SANSA)*

78. One way to deal with “brain drain” is through the so-called diaspora option. This strategy is attractive to developing countries that cannot afford to offer the salaries and other incentives needed to attract their highly skilled expatriates home. The aim is to encourage highly skilled expatriates to contribute their experience to the development of their home country without necessarily returning home. As a strategy to limit the effects of brain drain and make use of the presumably lost human capital, governments, organisations and members of the diaspora cooperate in networks. Such networks may focus on particular skills, knowledge or branches but they are all united by the goal to systematically use the expatriate experts, scientists and engineers for development at home.

79. The South African Network of Skills Abroad (SANSA) demonstrates what can be achieved with such an approach. As a virtual Community of Practice, SANSA’s main objective is to facilitate the development and utilisation of networks for knowledge sharing, learning and transfer between their members and the wider South African community. As of March 2002, SANSA had 2,259 members (58 % were South African citizens), in more than 60 different countries. While the SANSA network has not generated many projects (in May 2003), there have been some exciting developments. For example, the SANSA database is now linked to the NEXUS database which contains information on current and completed research projects in South Africa, research organisations, professional associations, profiles of researchers in South Africa and forthcoming conferences. The SANSA database is also useful for research purposes, such as a study by the World Health Organisation on the migration of skilled health personnel in South Africa.

80. Besides knowledge networks where mostly high-skilled members of the diaspora share and transfer expertise and skills for the benefit of their home countries (see elaboration in sections 3d and 5b), there is another type of diaspora commitment organised in networks. Migrants pool financial and sometimes material resources to fund collective non-profit initiatives and improve the living standard in home countries. Members often originate from the same geographical region (hometown associations) and maintain strong ties with families back home.

*GTZ pilot programme commissioned by BMZ for projects of migrant associations in their countries of origin*

81. Commissioned by BMZ the GTZ sector programme Migration and Development has been supporting diaspora association projects in developing countries since mid-2007.

**Example:** Employment perspectives through vocational training for young people in Senegal

82. The project’s goal was to expand the capacities of a vocational training centre in the migrants’ region of origin, Waoundé, so that more youths could have the chance for a sound craftsman apprenticeship. The region has high emigration rates due to increasing aridity that reduces agricultural perspectives. However, there is a need for qualified craftsmen.

83. The migrant association’s project that was co-financed by GTZ increased the number of apprentices from 40 in the school year 2006/2007 to 110 the following year. The Senegalese Ministry of Education doubled the number of teaching staff following the expansion of the school centre’s equipment. A third apprenticeship programme now supplements the training course. Besides wood and metal processing, electrical engineering is taught as well. Today the vocational school centre attracts qualified teaching staff. Local enterprises cooperate with the centre by making use of its machines.

***e) Return migration****Hsinchu Science Park, Taiwan*

84. The Hsinchu Science Park, a government-led initiative established in December 1980, is a successful effort to bring scientists and researchers home. The government has invested USD 1,679 million in park infrastructure and facilities. The Park had 115,477 employees by the end of 2004, including over 4,500 Taiwanese scholars who returned from abroad. These returnees directly contributed to the park's success by establishing 116 companies in the park (384 companies in total). They have also been involved in further development by introducing technologies and management skills.

*Returning Experts Programme, BMZ (Germany)*

85. The Returning Experts Programme commissioned by the Federal Ministry for Economic Cooperation and Development (BMZ) and implemented by the Centre for International Migration (CIM) advises and supports junior and senior experts wishing to return to their country of origin. Through professional re-integration and technical networking of returning professionals, the programme advances the sustainable transfer of know-how in sectors relevant to development. This helps counter brain drain and may have further positive effects on employment.

86. Advisory and placement services are offered to potential returnees and also to employers in developing and emergent countries who need employees with special qualifications. In 2007, about 5,000 potential returnees made use of the advisory services in Germany. This proves there is demand for, and potential in effectively applying the returning experts' know-how and skills towards achieving their country's development goals. There is temporary financial support for positions that are important to the development goals but whose 'normal' domestic pay is not attractive enough to expert returnees.

87. The current directive only supports the permanent return of experts. As such the potential of well-integrated, professionally experienced foreign experts is not optimally used for development cooperation. There are views that the programme should be open to circular migration processes and should be further developed in a country-specific manner.

**Example:** Returning Experts as Starting Points for Bilateral Economic Relations in Morocco

88. After completing his studies in computer science Abderrahmane El Kacemi worked as a software engineer with German companies for six years. However, in the long-term he saw his future in Morocco. During a counselling session at CIM he got to know about the returning experts programme and about the core theme in German development cooperation in Morocco "*Mise à Niveau*" which promotes the country's economic competitiveness. On his own initiative El Kacemi found a position in Morocco with a producer of plastic tubes. With his international professional experience the returnee now prepares medium-sized businesses for the planned EU-Mediterranean free trade area. By deploying new quality standards, automatised controlling instruments and training co-workers in IT, El Kacemi strengthens the company's innovative power. Based on his knowledge of the market and his connection to Germany the company has German clients and is buying an entire line of machines from a German company. Through the advisor for returning experts, he is involved in economic-related events of the Foreign Chamber of Commerce and of development cooperation.

## 6. Policy recommendations for donors

### *General policy recommendations*

89. It has been shown that migration and employment deserve stronger integration into development policy issues. In OECD countries migration should not only be seen as an internal policy challenge but as a means to complete development policy. Developing countries can use the potential of migration to increase the employment effects of their developing process while trying to control the challenges of migration.

90. To achieve more efficient migration and employment policies, relevant statistics in developing countries need to be improved. This essentially means developing tools to identify the effects of migration on labour markets and employment. It also concerns data collection, statistical capacity building, effective harmonisation and data sharing across countries in these policy fields.

91. More accurate and reliable data is also a prerequisite for employment strategies which could cover developing and developed countries, especially those that are closely interlinked by migration flows and whose labour markets show dependencies to different extents. Here, bilateral agreements would seem more likely to succeed as they tackle the relevant issues compared to regional or multilateral agreements. This can also include partnership agreements between trade unions in the countries of origin and destination (see box and annex 2). This way policy coherence between the sending and receiving countries can be improved with potential gains on each side.

**Example:** Partnership agreement on migrant labour between trade union organisations in Malaysia (MTUC)<sup>103</sup> and Indonesia (ITUC)<sup>104</sup>

There are thousands of Indonesian migrant workers in Malaysia. Most of them are women performing domestic service work. Migrant workers are often exploited by recruiting agents and employers, and have to endure poor working and living conditions. By and large, they remain outside the trade union movement. Although the law does not prevent them from explicitly joining a trade union, most of the contracts offered by agencies establish clauses stating that workers cannot unionise. If they do, they risk being sent back or fired. Besides, cross border migration is likely to increase in the near future. The partnership agreement on migrant labour between the Malaysian Trade Union Congress (MTUC) and the Indonesian Trade Union Congress (ITUC/KSPI) is an important part of bilateral cooperation in South-East Asia. To harmonise working and living conditions, it is also necessary to inform the workers of the positive contributions of migrant labour towards the development of both receiving and sending countries. One of the reasons for the agreement is to contribute to this harmonisation. It also aims to explore trade union solidarity and to strengthen cooperation between both organisations by regularly exchanging information on the situation of both labour markets, by exchanging experts on different issues and by taking immediate actions and finding solutions to migration problems. Moreover, the agreement aims to improve participation and consultation of the social partners at all levels and to establish better cooperation with the employers' organisations. The cooperation between the MTUC and the ITUC will include mutual visits, bilateral talks and consultations on these issues, seminars and conferences on specific topics concerning migrant labour and exchange of knowledge, experience and experts between trade unions at all levels.

92. Areas where multilateral cooperation might also succeed and where it is indispensable include the exchange of information and analyses on migration and employment policies and country experiences as well as the development and implementation of a code of conduct at EU-level for the ethical recruitment of high-skilled migrants.

93. Policy coherence also plays an important role when coordinating migration and employment policies at national level within a country. In cases of open economies these policies should not be conceived without taking into account trading and migration partners. They should also be consistent with the country's other national policies. This mainly concerns the coordination of (vocational) education policy, labour market and economic promotion policy regarding the target group of potential migrants. This can, among others, counterbalance the negative effects of brain drain.

### ***Regarding brain drain***

94. Although a limited but positive rate of skilled migration is very likely to be beneficial for both sending and receiving countries, many poor regions such as sub-Saharan Africa and Central America are well above that 'optimal' threshold. A number of steps should be considered to manage flows of highly skilled migrants more effectively and limit the negative impacts on sending countries. Sectors affected by brain drain should be identified and monitored, and there should be an effective regime to enforce ethical recruitment especially among doctors and nurses.

95. Development assistance to replenish key workers must be closely linked to recruitment efforts. The capacity of the brain drain-affected health and education sectors in developing countries to replenish or retain workers can be substantially improved through donor commitment in strengthening service delivery systems, continuous training of personnel and better working conditions. For example, temporary recruitment of personnel can be combined with on-the-job training programmes and skill-replenishment schemes.

96. In areas with a high emigration rate, labour market conditions and remuneration are decisive factors. The success of aid-for-migration policies depend on the volume of aid, how effectively it is utilised, the quality of jobs created and the commitments from both governments. Finally, if migration is to be managed successfully, there must be a comprehensive programme to educate or create awareness among citizens of sending countries about the benefits and the challenges of migration, especially irregular migration.

### ***Regarding remittances***

97. On an aggregate empirical level, skilled migrants remit less, so that the negative impact of brain drain on the sending countries cannot be counterbalanced by higher remittances. This does not mean that remittances by skilled migrants are negligible. This is especially if the proportion of temporary migrants increases, as the volume of remittances is negatively related with the duration of migration. Also, a low percentage of skilled migrants' income might be reasonably high in absolute terms.

98. Generally remittances have a strong impact on poverty reduction and economic activity, with an indirect impact on employment. Governments can offer incentives to increase the volume of remittances and to influence their allocation in home countries. It should be emphasised however that attempts to do so without recognising the primacy of individual choice have failed repeatedly. Success is based on relations of trust and on the networks forged both abroad and in the migrants' home countries. There is no substitute for sound macroeconomic policy, good governance, a reliable banking system, respect for property rights and a strategy aimed at fostering trade and attracting FDI. Migrants are not responsible for development and remittances are no substitutes for aid or FDI flows.

99. Policy makers can seek to facilitate transfers, for example by reducing their cost, and by increasing access to financial institutions in rural and remote areas. They can also encourage the creation of new financial instruments to favour economic initiatives. Similarly, foreign aid can be used to co-finance collective investments undertaken by migrants in their home countries.

**Example: Tres Por Uno in Mexico**

Bearing in mind the danger that new money flows create new dependencies, the Mexican district of Zacatecas started the programme called “*tres por uno*” (three for one) in 1986. This means that for every dollar sent from the hometown associations to the country of origin, the state, federal governments and municipalities also contribute a dollar each. This money is *inter alia* used for employment-oriented projects and the advancement of infrastructure. In 2001 the 3x1 Programme became a federal level programme under the *Secretaría de Desarrollo Social*.

One of the positive aspects is that local governments and hometown associations work closely together. The effects on the labour market are not quite clear. But in 2006, empirical studies showed that every dollar of remittances sent to Mexico allowed the Mexican economy to grow between USD 2.69 and USD 3.17. Smaller firms in urban Mexican areas take about 20% of their invested money from remittances.

In conclusion, projects based on networks and organised diaspora communities, like the hometown associations, seem to be more successful in having a positive impact on the economy and the labour market than projects that focus on individual transfers.

***Regarding diaspora networks***

100. There are three key characteristics of diaspora networks that are interesting to development policy-makers: *i)* they can be information intermediaries; *ii)* they have access to “inside information” about their members; and *iii)* they have recourse to contract enforcement mechanisms not available to outsiders.

101. Diaspora networks can increase the contribution of migration to labour market efficiency. Their role as information intermediaries certainly works as they communicate labour market information about the most remunerative job opportunities to would-be migrants. If migrants’ associations are active in labour market integration, they also help in social integration.

102. Diaspora networks can reduce the costs of brain drain to developing countries. If diaspora networks can be encouraged to facilitate “virtual return”, they can reduce the cost of the loss of skilled workers for sending countries. Circular migration regimes that facilitate temporary movement of such workers, including the acquisition of new skills and practice, will complement the activities of networks and allow people in sending and receiving countries to participate in transnational networks. Proposals to pool remittances for investment in educational and community development are a concrete example of diaspora contribution to local development.

103. National migration policies should include diaspora policy, such as encouraging and mobilising migrants’ organisations and diaspora networks as partners in co-development initiatives. Furthermore, international donors can facilitate networking and communication of diaspora communities.

***Regarding return migration***

104. It is well known that restrictions on temporary migration to northern countries often lead to migrants overstaying their visas once they have crossed the border to the north. Yet temporary or return migration could potentially be conducive to the development of the migrants’ regions of origin, and an increase in such migration could thus be positive for development.

105. However in terms of control of migratory flows, it is very difficult to distinguish between genuine temporary migration and entry for permanent settlement. Migrants would have a greater incentive

to return when their contract period ends because of the likelihood of repeat migration and because governments have detailed information about them (which is a fundamental difference to irregular migrants). Cooperation on screening would be more difficult at the regional level and most likely unfeasible at the multilateral level.

106. Successful temporary programmes avoid the shortcomings of the well-known guest-worker schemes through flexible working arrangements, close supervision of recruitment procedures, clear admission criteria and protection of fundamental rights. Multiple-entry visas raise the likelihood that migrants will return to their home countries and they encourage circularity by reducing the uncertainty surrounding re-entry into a particular OECD country. Mechanisms to transfer pension or social security contributions to an account in the home country to be collected by the migrant only upon return will likewise encourage circular movement.

107. Another element of effective management of temporary migration is active recruitment. Repeat contracting with agents, with a good record of transparency, reliability and treatment of workers, could provide incentives for agents to maintain core standards.

108. For example, the African Human Resource Programme (AHRP) touted by the GCIM seeks to create a database of African teachers in universities and high schools in Europe, the United States, Canada and elsewhere. It will be available to African states and other stakeholders active in education and teaching in Africa. Given the success of similar university programmes this idea could be productive.

## Annex 1

### *Further Implementation Experiences*

#### *Emigration, wages and economic adjustment*

1. **Bilateral agreements between sending and receiving countries:** For instance, Mali and France have established the **Mali-France Consultation on Migration**, an annual bilateral discussion at the ministerial level dealing with three issues: a) the integration of Malians who want to remain in France; b) co-management of migration flows; and c) cooperative development in emigration areas of Mali. Another example: the **Portugal-Cape Verde** joint commission on migration.
2. **Agence Nationale pour la Promotion de l'Emploi et des Compétences (ANAPEC):** This government agency facilitates seasonal employment of Moroccan workers in Europe (especially for agricultural work in Spain) and in Arab countries.
3. **Mainstreaming migration into Poverty Reduction Papers (PRSPs) and National Development Strategies:** Migration and its potential positive impacts are integrated into policies for growth and poverty reduction in countries, where emigration is high and remittances play an important role as a family resource and as an investment base. The Philippines arguably has pursued this. Discussions are underway in other countries, including Ghana and Kenya.
4. **Seasonal Agriculture Workers Scheme (UK):** Full-time students (aged 18-25) not living in countries of the European Economic Area are allowed to work in agriculture and horticulture in the UK. This gives them the opportunity to learn new methodologies and technologies and apply them upon returning home.

#### *Effects of remittances on the labour market*

1. **Diaspora bonds** are managed as a debt instrument issued by a country (or potentially, a sub-sovereign entity or a private corporation) to raise financing from its overseas diaspora. This finances development in the form of public sector projects (housing, communication or infrastructure). Israel and India for instance, have raised USD35-40 billion using these bonds.

#### *Diaspora networks and the labour market*

1. **The Silicon Valley Indian Professionals Association (SIPA):** A platform that focuses on creating value of information for its members and knowledge that engenders in the meeting of corporate leaders, workforce, consultants, and service providers. A further aim is to develop cooperation and exchange between high-skilled Indian expatriates, and between India and the U.S. in areas of high technology. URL: [www.sipa.org](http://www.sipa.org)
2. **The Indus Entrepreneurs (TiE):** The Indus Entrepreneur group has more than 12,000 members in 11 countries. Entrepreneurs and professionals with roots in the Indus region founded the group in the Silicon Valley in 1992. URL: [www.tie.org](http://www.tie.org)
3. **Brain Gain Network (BGN):** An online networking and productivity tool started in 1992, which connects professionals and students interested in helping to increase the global competitiveness of the Philippine high-technology economy. URL: [www.bgn.org/bgn](http://www.bgn.org/bgn)

## Annex 2

### *Examples of transnational cooperation between trade unions*

#### **Cooperation agreement between trade union organizations in Costa Rica (CTRN)<sup>105</sup> and Nicaragua (CST)<sup>106</sup> to establish a trade union support centre for migrants**

There is a high level of migration between Costa Rica and Nicaragua. However the trade union movement has had difficulties in tackling the issue of migration in an effective manner. There can be no progress in defending migrant workers' rights unless bilateral relations and international solidarity are strengthened. The "Confederation of Workers Rerum Novarum" of Costa Rica (CTRN) and the "Central Sandinista de Trabajadores" of Nicaragua (CST) have therefore signed a cooperation agreement to defend the rights of migrant workers in the region. Both organizations agree that the situation facing migrant workers needs to be addressed from the perspective of broad trade union solidarity and gender equality since migrant women workers suffer the worst marginalisation due to their unequal position in society. They have also agreed to develop good practices on trade union cooperation to support migrant workers. The project will run for two years focusing on the establishment of a trade union support centre for migrants to be based in Costa Rica. In addition, both organisations intend to develop efforts to raise awareness on combating racism and xenophobia by providing trade unions and the general public with information on the positive contribution that migrant workers can make to the economy of the host country. They have also included in their general programmes, the organisation of seminars and conferences on specific issues linked to migration. They will also actively promote the ratification and effective application of the relevant ILO conventions, *i.e.* numbers 97 (on migrant workers) and 143 (on migrants in abusive conditions and the promotion of equal opportunity and treatment of migrant workers) and the adoption of the ILO's multilateral framework on labour migration.

#### **Partnership agreement between trade union organisations in Senegal (CNTS)<sup>107</sup> and Mauritania (CGTM)<sup>108</sup>**

Mauritania and Senegal are both transit countries for migrant workers. The "Confédération Nationale des Travailleurs du Sénégal" (CNTS) and the "Confédération Générale des Travailleurs de Mauritanie" (CGTM) have developed a partnership agreement enabling them to play a role in the management of migratory flows and the clandestine immigration of workers between the two countries or across their borders. The objective is to help trade union organisations in their work related to migrant workers in both the source and destination countries, to promote, protect and defend the rights of migrant workers, and secure equal rights for women and migrant workers focusing on the specific problems they face. Both organisations will exchange information regularly on the labour market situation in the two countries, help promote social partnership at all levels, establish better cooperation with employers' organisations, harmonise working conditions to combat the exploitation of migrant workers, initiate national level tripartite consultations in the countries and actively promote the ratification and effective application of the relevant ILO conventions, *i.e.* numbers 97 (on migrant workers) and 143 (on migrants in abusive conditions and the promotion of equality of opportunity and treatment of migrant workers), and the adoption of the ILO's multilateral framework on labour migration. Furthermore, they will organise visits to each other's countries and they will equally promote the establishment of information centres on immigration in the two countries.

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<sup>102</sup> Fact Sheet: H-2A Temporary Agricultural Worker Program, 2008, Office of the Press Secretary, Department of Homeland Security, United States of America; accessible at [http://www.dhs.gov/xnews/releases/pr\\_1202308216365.shtm](http://www.dhs.gov/xnews/releases/pr_1202308216365.shtm)

<sup>103</sup> The Malaysian Trade Union Congress is the biggest national trade union centre in Malaysia and has approximately 405000 members.

<sup>104</sup> The Indonesian Trade Union Congress is the biggest national trade union centre in Indonesia and has approximately 507000 members.

<sup>105</sup> The CTRN is the second biggest national trade union centre in Costa Rica and has approximately 30000 members.

<sup>106</sup> The CST is the second biggest national trade union centre in Nicaragua and has approximately 40000 members.

<sup>107</sup> The CNTS is the biggest national trade union centre in Senegal and has approximately 60000 members.

<sup>108</sup> The CGTM is the third biggest national trade union centre in Mauritania and has approximately 25000 members.

## EMPLOYMENT AND LABOUR MARKETS IN FRAGILE STATES POLICY AND PRACTICE

Monique Calon, Ministry of Foreign Affairs, The Netherlands

In fragile states and situations, the challenges to be confronted to restore the confidence people have in government, to rebuild sustainable livelihoods and repair the damage done as a result of conflict, neglect and abuse of power are daunting. Donors are becoming increasingly aware of the need to invest in fragile states to avoid conflict, promote human rights and stimulate economic growth. Pro-poor economic growth is increasingly seen as a major force in combating fragility and redressing inequalities. Employment and labour market policies are an essential part of prevention and recovery efforts. In this context donors should:

- help governments in fragile states design and implement employment strategies emphasizing equal opportunities and increasing the access of the poor to remunerative employment
- support partnerships between government, the private sector and civil society groups to design and implement programmes to create employment opportunities
- ensure that there is a smooth transition from humanitarian assistance to structural economic development by creating short term employment conducive to economic recovery. At the same time, steps need to be taken to create an enabling environment for structural economic growth and equity in access to productive resources and employment

### 1. Introduction

1. The OECD/DAC endorsed the DAC Principles for Good International Engagement in Fragile States and Situations with a view towards improving development effectiveness in fragile states. The Whole of Government approach has been adopted by the OECD as a guiding principle. The long term vision for international engagement in fragile states is to help national reformers build effective, legitimate, and resilient state institutions, capable of engaging productively with their people to promote sustained social and economic development.

2. POVNET has taken on the challenge of developing donor guidance for employment and labour market issues in fragile states as a means to translate these basic principles into practical guidelines for donors. Donors are becoming increasingly aware of the need to invest in fragile states and situations to avoid conflict, protect and promote human rights and generate equitable growth. This policy note aims at identifying policies and practices to contribute towards these goals through employment creation and labour market policies.

3. The main questions which this paper seeks to address are:

- how employment promotion and improved labour markets in fragile states as a part of economic reform and recovery efforts can contribute towards good governance and security as well as pro-poor economic growth
- how the donor community can contribute towards promoting employment and effective labour market policies in fragile states

## 2. Why is employment promotion important in fragile states?

4. Fragile states, *i.e.* countries or regions with weak governance and prone to conflict, are usually not able or willing to ensure that the basic needs of the population are met. One third of the world's poor amounting to one billion people, including about 340 million of the world's extremely poor, are estimated to live in fragile states. Fragile states have poverty rates averaging 54 per cent, compared to 22 per cent in other low income countries<sup>109</sup>. For these people productive employment is an important pathway out of poverty. In fragile states and situations creating an enabling environment for equal access to employment is a means to reduce social and political tensions which lead to conflict. In post conflict countries and situations, employment creation is part and parcel of reconstruction efforts whereas a longer term effort is needed to engage in reforms to ensure equal access to employment and productive resources.

*Equal access to employment is a means to prevent fragility*

5. In fragile states and situations, access to scarce productive resources and employment is mediated through ethnicity, religion, regions and other characteristics which distinguish between groups in the population. Where inequalities become institutionalized and lead to income disparities they exacerbate tension and conflict. Employment opportunities and access to productive resources are often used by the political elite to consolidate its position and dispense favors. Fragile states are characterized by increasing group inequalities, in particular in terms of economic opportunities.

6. Unemployment, especially if confined to specific groups in the population, is a major threat to stability and economic growth. Unemployed youth, for example, are often recruited into armed militias or criminal activity. Regions where groups in the population feel marginalized in terms of access to productive resources, employment and services are vulnerable to conflict.

7. Employment and labour market policies, programmes and institutions can either promote divisions in society or, alternatively, be used to promote social and economic inclusion<sup>110</sup>. At the 11<sup>th</sup> ILO African Regional Meeting (2007), the African heads of state expressed '...grave concern that widespread poverty and social exclusion (...) are sowing the seeds for potential future conflicts'. They further stated that 'social institutions, especially strong and representative employers' and workers' organizations, contribute to increased inclusion, more and better jobs and the processes of dialogue that are vital to conflict prevention.

8. Last but not least, it is the people themselves who need to be able to foresee in their basic needs. Labour is the most important asset of the poor. Labour markets should create opportunities for poor and marginalized groups in society to put this asset to work and contribute to economic growth. Governments in fragile states are unable or unwilling to provide an enabling environment for equal access to productive employment thereby curtailing economic growth for the benefit of the whole community and creating instability.

9. In fragile states engagement of the international community in developing policies and programmes to create employment could effectively contribute towards preventing economic decline and conflict. The types of policies and programmes to be developed depend on local conditions and the

presence of sectors which lend themselves to the creation of employment, particularly for the poor, as well as political ambitions to promote equal opportunities.

10. In many of the poorest countries, some of which are considered to be fragile states or in danger of becoming fragile due to low and skewed economic growth, agriculture is the mainstay of the poor. Creating employment in agriculture involves a different set of parameters than in the formal urban setting. In other countries, due to factors such as shortages of arable land, there may be needed to encourage more off-farm employment. Employment policies therefore need to be constructed on soled opportunities as well as political ambitions. They need to reflect the concern of government for all of its citizens as well as promoting economic growth. If not, there is a risk that groups excluded from the labour market will rebel. A lack of employment opportunities may also lead to increased illegal economic activities such as poaching and smuggling which may be the only way to earn a living.

11. Governments in fragile states could be assisted in developing legal and regulatory frameworks for the labour market which emphasis equality, equity and ‘rule of law’ to prevent discrimination and exclusion.

12. Donors are also becoming increasingly aware of the need for prevention, not only for humanitarian reasons or internal security in the affected areas or countries, but in their own interest – to protect investments and trade relations and to protect against the effects of extremism and terrorism. Moreover, there is a strong human rights argument to contribute towards creating equal opportunities for employment and combating discrimination.

13. Investing in peace, as opposed to dealing with the aftermath of and social, political and economic damage caused by violent conflict and serious economic decline, also makes economic sense. We should be able to ‘read the writing on the wall’ by now and take appropriate action to engage with governments and civil society groups in fragile states to address issues of governance, including access to employment, productive resources and equity. The World Bank has estimated for every ... spent on peacekeeping, is saved on dealing with the damage caused by violent conflict. Even in countries such as Kenya where the conflict was contained through political dialogue repairing the damage to the economy and therefore also to employment will take years.

14. In conclusion, there is sufficient evidence to support investing in employment strategies in fragile states as a means to avoid conflict, address inequalities and avoid further economic decline. Employment strategies focusing on reducing inequalities and increasing access to (public and private) productive resources and services act as a barrier to conflict and enhance the legitimacy of government. Donors should engage in dialogue with government to promote equal access to employment, productive resources, services and skills as well as engaging with the private sector. Internationally agreed norms with regard to workers’ rights, child labour, exploitation of natural resources and CSR are important tools to inform the political dialogue. Support should also be provided to build institutions representing employers, workers and the business community. Where necessary, donors could support specific programmes to promote employment, including skills training, micro and meso finance, private sector development and economic infrastructure. These types of programmes aimed at increasing employability and employment opportunities are already common in low income countries. However, in fragile states and situations there may be need to discriminate positively in favor of certain groups which have been marginalised in the past.

*The role of employment in dealing with the aftermath of armed conflict*

15. Armed conflict invariably poses additional challenges which need to be addressed. In a country or region where armed conflict has destroyed much of the social and economic infrastructure, employment is often limited to the informal sector for survival and illegal activities in the context of a war economy.

Rebuilding the state required both short and long term investments. Creating employment is an crucial element in post conflict situations.

16. In a recent study by the Conflict Research Unit at the Clingendael Institute in The Netherlands, respondents in both Bosnia-Herzegovina and southern Sudan, two completely different worlds, emphasized the need to create jobs as an essential part of post conflict recovery efforts. They said that peace can only be achieved and sustained if people have 'money in their pockets'.

17. In the transition from post conflict humanitarian assistance towards structural development, employment creation plays a key role, initially as a means to rebuild the country and provide basis services and sustenance and later as a crucial element in maintaining pro-poor growth and avoiding future conflicts. A number of studies also deplore the missed opportunities to use humanitarian assistance and recovery funds to create employment rather than merely dispensing goods and services.

18. Rebuilding the state after armed conflict is a complex and very expensive task. Economic infrastructure has been destroyed or neglected, services have failed to deliver and the economy needs to be redesigned to redress past inequalities and create a basis for sustained economic growth.

19. Priorities on the short term include, for example, rebuilding transport and communication infrastructure, providing basic services to communities and returnees, redistributing productive assets, including land for cultivation, suppressing illegal trade in arms and natural resources and ensuring a minimum level of security. Many of these tasks require significant human investment. Employment is therefore a central part of post conflict recovery efforts. Governments, donors, private sector operators and civil society organizations need to engage in labour intensive recovery and reconstruction efforts. Initiatives which have proven successful in many post conflict countries and regions are, for example, labour intensive public works programmes and microfinance. Public-private partnerships have been successful in assisting governments to provide basic infrastructure and services (**SEE BOX: AFD WATER SECTOR INITIATIVE IN CHAD: to be inserted**). In some cases reviving agriculture through free or subsidized distribution of seeds, tools and fertilizer has been a major part of post-conflict and recovery programmes. A longer term effort is also needed to fully restore food security.

20. Creating employment opportunities for returnees, (ex) combatants and IDPs is a major challenge in post conflict countries and situations which has to be dealt with urgently. Opportunities are very location specific and require close collaboration between government institutions, private sector operators and civil society. In Afghanistan, for example, a group of institutions including international agricultural research institutions such as ICARDA and development agencies are actively involved in rebuilding the agricultural sector. This initiative also involves drawing farmers away from poppy production for opium by promoting new crops such as saffron, almonds and vegetables which are more profitable than poppies for opium. (**SEE BOX: SAFFRON PRODUCTION IN AFGHANISTAN; to be inserted**)

21. Absorbing the labour force in both urban and rural areas and reintegrating people into war-torn communities is a major part of post conflict programmes. In addition to training and credit schemes, there are also good examples of labour intensive public works programmes, as food or cash for work, which not only create employment but also contribute towards (re)building economic infrastructure and reconciliation/peace building within communities. These programmes also offer opportunities not only to build infrastructure but also create small scale enterprises and revive agriculture. Rural communities are often the most affected by conflict. In Rwanda, for example, the government has initiated a massive program focusing on rehabilitation of rural roads, terracing hillsides, restocking lakes and marshland development. This has led to the emergence of small construction companies, associations specialized in constructing terraces and farmer groups which build and maintain irrigation and drainage infrastructure. A similar program based on agricultural commodity chain development and natural resource management has

been launched by IFDC in the Great Lakes region in central Africa (covering the East Congo, Rwanda, Burundi and southern Uganda)

(BOX to be inserted)

22. However, these programmes are not sufficient to rebuild the state and ensure future security and pro-poor economic growth. Until recently, the complex issue of reviving the private sector and creating an enabling environment for economic growth received very little attention from policymakers involved in post conflict recovery efforts. This is changing as donors and governments in post conflict countries are becoming more aware of the role of the private sector in creating employment. In post conflict countries, revival of the private sector in the broadest sense of the word, is increasingly seen as a pre-condition for stability as well as for economic recovery. IFC has recently launched an initiative to support governments in post-conflict countries to develop legal and regulatory frameworks to promote private sector development and contribute towards capacity building (*SEE BOX: IFC CASA: to be inserted*)

23. The ILO has published '10 Guidelines for employment friendly recovery' in post crisis situations. These guidelines (Annex 1) are an excellent starting point for donor and government policy and strategy development.

### **Main messages and policy recommendations**

24. Employment and equal access to employment contribute towards stability and economic growth. Governments can use employment and access to employment as a means to generate or diffuse tensions and the risks of conflict. Institutionalized group discrimination is often the cause of conflict.

25. It makes sense to invest in policies and programmes to promote equal access to employment in fragile states to avoid increasing instability, conflict and economic decline. The costs of prevention are much lower than the costs of dealing with the aftermath of violent conflict.

26. While government is responsible for creating a favorable environment for employment creation and the organization of labour markets, there is also need for strong institutions representing the interests of different groups involved in economic activity – employers, workers, self employed agricultural producers etc.

27. Special attention is needed for marginalized groups whose access to employment is often a result of political bias towards certain groups in the population. The international community has a responsibility to engage in a dialogue with government to ensure equal access and opportunities.

28. There has been too little attention given to the transition from humanitarian assistance after a crisis (conflict, severe economic decline, natural disasters) to structural economic development. The high level of aid during emergencies creates dependency and tends to be reduced before sufficient safeguards are put in place to ensure sustained peace and stability.

29. During the transition phase governments, donors and other stakeholders should take appropriate measures to start a process leading towards structural development. This involves improving infrastructure, providing essential services, developing appropriate legal and regulatory frameworks and capacity building.

30. One of the main challenges is redesigning the social and economic fabric to redress imbalances of the past which have led to instability. Often capacities are limited within the country due to the brain drain and the conflict or crisis itself. Donors could play an important role in rebuilding capacities by offering scholarships or assisting government in reviving educational institutions. Specialized technical

assistance (for example as provided by IFC) is also needed especially where old institutions need to be replaced by new institutions which reflect the new situation.

31. In the immediate post crisis situation priority should be basic food security and generating income to meet basic needs. Dependency on aid should be curtailed as quickly as possible and where possible the local private sector and local communities involved in producing and procuring goods and services thereby also creating employment.

32. Also in post conflict situations, although immediate and urgent needs should be addressed, the process of rebuilding institutions for structural development should feature on the agenda from the beginning. This should include labour market institutions such as trade unions, employers' and farmers' organizations.

33. More attention is needed for involvement and development of the local private sector, including agriculture, which in most countries is the main source of employment. In the initial phases labour intensive public works programmes, public private partnerships and targeted support to local entrepreneurs and producers are good options.

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<sup>109</sup> Speech by World Bank Group President Robert B. Zoellick, September 12<sup>th</sup> 2008

<sup>110</sup> Poverty and Conflict, The inequality link, Coping with Crisis Working Paper Series, International Peace Academy, June 2007

**SOCIAL CASH TRANSFERS AND EMPLOYMENT  
A NOTE ON EMPIRICAL LINKAGES IN DEVELOPING COUNTRIES**

Michael Samson, Economic Policy Research Institute (EPRI), South Africa

**KEY MESSAGES**

- ✓ Empirical evidence from South Africa indicates that social cash transfers
  - provide critical resources funding job search, particularly for rural women who migrate to look for work
  - enable the poorest households to better manage social risk and increase their labour market participation
  - increase the resilience of agricultural smallholders in maintaining production
  - promote human capital development, reinforcing long-run employment impacts.
- ✓ While the measured direct effects on employment are modest, they are positive and statistically significant, refuting the notion that social cash transfers create disincentives for employment and economic growth.
- ✓ Further research into linkages between social cash transfers and employment will more effectively support policy development.

**Introduction**

1. Social cash transfers and employment interlink in many important ways. For many households decent employment is the best path out of poverty and the most effective instrument of social protection. Social cash transfers can also promote employment — certainly in the long run by nurturing the human capital accumulation of poor households. A more contentious issue is the shorter run question of how social cash transfers interact with households' labour market behaviour.

2. The employment impact of social cash transfers can be tested in terms of both labour supply and labour demand effects. Labour supply impacts can be negative—in terms of income and incentive effects—or positive—in terms of enabling poor workers to more effectively participate in the labour market. Demand effects potentially exert an impact on labour productivity, which would raise employers' demand for these workers. In addition, social transfers may stimulate local economies and produce employment—or directly create jobs through their core operations.

3. Certain types of social transfer programmes—particularly public works schemes—explicitly aim to promote labour market participation and employment. Numerous studies document the direct impact of public works in terms of providing short term jobs and reducing immediate unemployment—in India, Bangladesh, Malawi, South Africa and many other countries (Chirwa *et al.* 2004; Devereux *et al.*, 2006; McCord 2004 and 2005). A more contentious question is the long term impact—whether or not public

works programmes enable workers to exit public works and engage in sustainable livelihoods and employment. Argentina's *Jefes y Jefas de Hogar* public works programme, for example, increased the propensity of workers to participate in the labour force and to find a job in the formal sector (Ronconi 2005), particularly for women (Devereux *et al.* 2006).

4. Other programmes, however, yield different results. Slater (2006) warns that households participating in Ethiopia's *Productive Safety Net Programme* may find the work requirement reduces their ability to pursue successful alternative livelihood activities. McCord (2009) provides a critical review of the potentially counter-protective impacts of public works programmes, and a thorough analysis of the relationship between labour markets and social protection for public works programmes.

5. Another set of issues arises with social transfer programmes not directly linked to employment—such as social pensions, child support grants, disability benefits and other types of transfers. Schüring *et al.* (2006) find that participants in Zambia's cash pilot scheme use a significant proportion of the benefits to hire labour, for example in order to cultivate the land around their homes and consequently multiply the value of the social transfers while creating employment for local youth. Barrientos and Sabates-Wheeler (2006) find that Mexico's *Progresa* (now *Oportunidades*) social transfer programme is associated with local economy impacts that improve consumption, asset accumulation and employment broadly within communities—for both programme participants and non-participants. Gertler *et al.* (2005) find that participants in *Progresa* invest a portion of their social transfers in productive assets and are more likely to engage in entrepreneurial activities, improving their potential for sustainable self-sufficiency. Harnett and Cromwell (2000) found that participants in one of Malawi's social transfer programmes were empowered by the resources to invest in their own farms during the planting season rather than rely on dead-end casual employment for their immediate survival. In South Africa, a wide-ranging debate has explored many dimensions of the impact of social grants on employment and household labour market behaviour.

### **Evidence from South Africa**

6. The first wave of debates over the linkages between social cash transfers and employment in South Africa focused narrowly on income and incentive effects associated with the system of social grants. Bertrand, Miller, and Mullainathan's (2000) study of workers in three-generation households (which include children, older people and other adults) documented a drop in the labour force participation rates of the other adult men when an older person reached the age that qualifies for the social pension. They interpreted this partly as resulting from the negative income effect, based on the theoretical rationale that as household income rises, the additional benefit to the household from working for further income falls, and so work incentives are dampened. Case and Deaton (1998) document how social pensions are pooled with other household income, and thus potentially affect the labour market decisions of all workers within the household. Bertrand *et al.* also conclude the effect results from labour income's impact on intra-household allocation of grant resources, but point out that women's labour force participation was unaffected.

7. Dinkelman (2004) found similar results with better panel data, but documents how an older women's receipt of a social pension has a strong positive impact on other women's labour force participation. Samson *et al.* (2000, 2001, 2002 and 2004) disputed Bertrand *et al.*'s results using more recent Labour Force Survey data (Statistics South Africa 2000 and 2001) and a methodology that differed from Bertrand *et al.*'s work in that it explicitly tested the labour market responses of the poorest households. For the workers in the lowest income households, social grants had a positive and significant impact on labour market participation and the probability of finding employment. All these econometric studies focused on income and incentive effects, and relied heavily on cross-sectional econometric analysis that suffered from potentially significant econometric biases, particularly those resulting from unobserved heterogeneity.

8. The second wave of debates explored the deeper realms of sociological behaviour, examining household formation dynamics and the poor's response to risk and vulnerability. Klasen and Woolard (2005) argue that "the unemployed get stuck in rural households in order to get support from pensions and remittances and thereby reduce their search and unemployment prospects." Keller (2004) finds similar results, but argues that the effect is primarily due to young workers delaying leaving grant-receiving households. Posel, Fairburn, and Lund (2006) explicitly addressed Bertrand *et al.*'s earlier analysis of the 1993 household living standards data, but employ a more rigorous methodology that incorporates migrant workers, an important factor in South Africa's labour markets. They refute Bertrand *et al.*'s results, finding no work disincentives from social pensions but rather positive and significant impacts for female labour migrants. They conclude that social grants help finance women's migration for job search and assist older people in caring for the workers' children. These results corroborate earlier studies that interpreted positive labour market impacts as suggestive that social grants provide critical resources funding job search. (Samson *et al.* 2004 and Kingdon and Knight 2000). These results are consistent with Shoër and Leibbrandt's (2006) findings that domestic duties constrain those wish to work from more active job search.

9. One of the most important ways in which social grants may affect employment decisions is through the improved management of social risk. Social grants reduce the downside risk and also relax liquidity constraints. (Ravallion 2003, Devereux and Sabates-Wheeler 2004, and Samson *et al.* 2002, 2004). Social grants enable workers to invest in more productive job search, providing the critical support to look for decent work and not attach themselves to the worst forms of labour out of desperation (Wittenberg 2002). Social cash transfers may reduce the impact of shocks on livelihoods and employment at a macro-economic level by stimulating overall economic activity, and they protect households by reducing the impact of shocks on productive assets. For example, economic shocks are less likely to force poor households to sell their livestock – often their only productive asset – if social cash transfers help them cope with the loss of income.

10. At the household-level transfers reduce risk by providing the security of a guaranteed minimum level of income. This better enables poor households to send children to school because they can afford for them not to be working, as well as afford fees, uniforms and other school expenses. The unemployed and lowest paid workers can take a chance on riskier ventures that are likely to result in a higher income, or acquire human capital such as education in order to find higher wage employment. The time and travel costs of job search – with its unpredictable outcomes – can lock vulnerable workers into poverty traps. Social cash transfers provide a coping mechanism for the least fortunate, supporting a minimal level of subsistence and allowing them to invest time and money to improve their chances of getting better employment. Adamchak (1999) finds similar results in Namibia with the social pension.

11. Keswell (2004) uses panel data from one of South Africa's poorest provinces to evaluate the risk management properties of social pensions, finding that it enables the poorest households to avoid less efficient insurance mechanisms and improves employment prospects by reducing the risk and cost of job search. Social transfers may also support other forms of livelihoods besides employment. Lund (2002), Ardington and Lund (1995) and Cross and Luckin (1993) document the role of social pensions in backing credit, renting capital equipment and buying the necessary inputs for agricultural activities. Social grants also directly support nutrition, access to transportation services, and other short run productivity-enhancing expenditures. Over the longer term, social grants have documented positive impacts on nutrition, health, education and training. Shoër and Leibbrandt's study of labour markets in South Africa finds hunger negatively affected a quarter of job-seekers, while health problems had negative impacts on 13% of them.

12. The third wave of debates is currently in progress, relying on improving data sets and natural policy experiments to more explicitly test the direct impact of social transfers on worker's labour force participation decisions and outcomes in terms of success in finding employment. Samson *et al.* (2004)

linked Labour Force Surveys together to construct panel data to better explore the short run labour market impacts of social grants, finding generally positive impacts. More recent studies take advantage of the natural policy experiment resulting from South Africa's rapid increase in the scope and take-up of the Child Support Grant from 2002 to 2005. These studies find a significant and positive impact of the Child Support Grant on labour force participation in grant-receiving households. (Samson *et al.* 2004 and 2007, Williams 2007, Samson and Williams 2007).

13. More recent data confirms the result that working age adults in poor households that receive a social pension are more likely to look for work and more likely to find employment than comparable adults in households that do not receive the social pension. Matching the September 2004 Labour Force Survey to the March 2005 survey and correcting for mis-matched individuals provides a dynamic picture of how labour force participation changes for households receiving and not receiving the social pension.<sup>111</sup>

14. The table below compares the change in labour market participation for out-of-the-labour-force working age adults (those older than 16 years) in households with no employed individuals in September 2004 but including at least one older person (defined in terms of age eligibility for South Africa's older person's pension). The first row of data shows the proportion of these adults who were employed in March 2005, broken down by status in terms of household receipt of the social pension. The second row shows the proportion of adults who were actively looking for work but not employed. (None of the adults in this sample were employed in September 2004 or looking for work.). The third row shows the proportion of adults with an unchanged status—those who were not participating in the labour force (out-of-the-labour-force).<sup>112</sup>

15. This methodology follows a standard approach employed to identify the probability that an individual will “transition” from one labour market state to another—for example, to make the transition from unemployment to employment, or from non-participation in the labour market to active participation.<sup>113</sup> The “probabilities” refer to the proportion of individuals in each category during September 2000 that made the transition to each respective category in February 2001.<sup>114</sup> For example, of those out-of-the-labour force adults in households receiving a social pension in September 2004, 9% had found employment by March 2005. This 9% figure is interpreted as the simple probability that an out-of-the-labour-force adult in September 2004 living in a household that receives a social pension would find a job and be employed in March 2005. The other entries in the table can be similarly interpreted. For example, of those out-of-the-labour force adults in households that did not receive a social pension in September 2004, only 7% had found employment by March 2005. This 7% probability is lower than that associated with a similar individual in a household receiving a social pension. In this sense, the probability that an out-of-the-labour-force adult finds employment over the time period is greater if the person lives in a household receiving a social pension. Likewise, the probability of beginning to actively look for work is greater if the person lives in a household receiving a social pension.

**Table 1: Impact of the social pension on labour force participation**

corrected data	Household receives social pension in 2004	Household does not receive social pension in 2004	Improvement associated with social pension
<b>Probability that a poor working age adult will:</b>			
Find employment in 2005	9%	7%	2%
Be actively looking for work in 2005	15%	13%	2%
Not participate in the labour force in 2005	76%	80%	4%
NOTE: Sample includes working age adults (older than 16) in households in the lowest income quintile with older people but with no working individuals in September 2004.			

*Source:* Statistics South Africa Labour Force Surveys and EPRIS calculations

16. In households that received the social pension, 9% of adults were employed in March 2005 and another 15% were actively looking for work. In households that did not receive the pension, only 7% were employed and another 13% were actively looking for work. Receipt of the social pension was associated with a 2% higher probability of finding employment and a 2% higher probability of actively looking for work. Alternatively, receipt of the social pension was associated with a 4% lower probability of not participating in the labour force.

17. The child support grant demonstrates a similar effect. Working age adults that were not participating in the labour force—particularly women—in poor households that receive a child support grant are more likely to look for work and more likely to find employment than comparable adults in households that do not receive the child support grant. The matched Labour Force Survey similarly provides a dynamic picture of how labour force participation changes for households receiving and not receiving the child support grant.

18. The tables below compare the changes in labour market participation for working age adults and working age women in households with no employed individuals in September 2004. The rows follow the format of the table above, with the first row showing the proportion of adults who were employed in March 2005, broken down by status in terms of household receipt of the child support grant. The second row shows the proportion of adults who were actively looking for work but not employed, while the third row shows the proportion of adults who were not participating in the labour force.

**Table 2: Impact of the child support grant on labour force participation**

corrected data	Household receives child support grant	Household does not receive child support grant	Improvement associated with child support grant
<b>Probability that a poor working age adult will:</b>			
Find employment in 2005	15%	13%	2%
Be actively looking for work in 2005	20%	17%	3%
Not participate in the labour force in 2005	65%	70%	5%
NOTE: Sample includes working age adults (older than 16) in households in the lowest income quintile but with no working individuals in September 2004.			

*Source:* Statistics South Africa Labour Force Surveys and EPRI calculations

19. In households that received the child support grant, 15% of adults were employed in March 2005 and another 20% were actively looking for work. In households that did not receive the child support grant, only 13% were employed and another 17% were actively looking for work. Receipt of the social pension was associated with a 2% higher probability of finding employment and a 3% higher probability of actively looking for work. Alternatively, receipt of the child support grant was associated with a 5% lower probability of not participating in the labour force.

20. The effects are even stronger for women, as documented in the table below. In households that received the child support grant, 15% of adults were employed in March 2005 and another 20% were actively looking for work—the same proportions as for all adults. In households that did not receive the child support grant, only 12% were employed and another 14% were actively looking for work. Receipt of the social pension was associated with a 3% higher probability of finding employment and a 6% higher probability of actively looking for work. Alternatively, receipt of the child support grant was associated with a 9% lower probability of not participating in the labour force.

**Table 3: Impact of the child support grant on female labour force participation**

corrected data	Household receives child support grant	Household does not receive child support grant	Improvement associated with child support grant
<b>Probability that a poor working age woman will:</b>			
Find employment in 2005	15%	12%	3%
Be actively looking for work in 2005	20%	14%	6%
Not participate in the labour force in 2005	65%	74%	9%
NOTE: Sample includes working age women (older than 16) in households in the lowest income quintile but with no working individuals in September 2004.			

*Source:* Statistics South Africa Labour Force Surveys and EPRI calculations

21. While the magnitudes of these effects are relatively small, it is important to emphasise that social transfers are not intended as employment generating schemes. Their major impact is social protection—with support of labour market participation an ancillary outcome. Nevertheless, this evidence contradicts the misplaced notion that social grants create dependency. On the contrary, social grants support households to participate more actively and successfully in the labour market, assisting workers to break the poverty trap. A more detailed policy discussion and rigorous treatment of the methodology is provided in Samson *et al.* (2007), Samson and Williams (2007) and Williams (2007), including the econometric

models that demonstrate the positive and significant impact of social grant receipt on labour force participation used pooled cross-sectional analysis.

### **Social Cash Transfers and Agricultural Resilience in South Africa**

22. South Africa's Child Support Grant (CSG) likewise is associated with improved resilience for agricultural smallholders. A non-experimental panel study evaluation of the CSG impact assessed the linkages between grant receipt and household agricultural activities. The study employed a propensity score matching approach which tested several alternative methodologies. Using a panel of data from 2002 to 2004 constructed from Statistics South Africa's General Household Survey, the study found that grants improve household resilience in terms of maintaining agricultural cultivation.

23. From 2002 to 2004, the number of poor households in South Africa cultivating land fell. Yet, the proportion of households with children receiving the CSG that stopped farming activities was statistically significantly lower than the proportion of those not receiving the CSG, and this result was consistent across the matching techniques. In other words, households receiving the CSG are significantly more likely to continue farming activities. This evidence suggests that the Child Support Grant may have improved household resilience in maintaining agricultural production in the face of an overall downward trend.

24. This result is consistent with the risk management results found for cash transfers in the Social Cash Transfers Good Practice Note (EPRI 2009). Agricultural shocks are increasing the overall riskiness of agriculture in South Africa, perhaps in part due to climate change. In the absence of social cash transfers, poor households may find it optimal to shift out of agriculture in the face of the increased risk—and into potentially lower return but less risky activities. Social cash transfers help to address the increased risk agricultural households face—and improve their resilience in maintaining production.

### **Employment and Social Cash Transfers: A Potential Virtuous Circle**

25. The emerging evidence base on the linkages between employment and social cash transfers suggests the potential of a virtuous circle. Decent work provides one of the best paths out of poverty for many of the poorest and most vulnerable. Better employment options reduce poverty for those able to work while fostering economic growth, expanding the resource base for social policy. In turn, social cash transfers help the poor and vulnerable to manage risk, enabling them to better invest in high-risk high-return job search. In addition, the transfers can directly support engagement in labour markets—in the short term by funding nutrition and transportation, and in the longer term by promoting investment in human capital.

### **Policy Implications**

26. Research into linkages between employment and social cash transfers does not suggest a competition across policy options but rather important complementarities. Decent work is a critical ingredient for pro-poor growth. Social cash transfers do not necessarily create work disincentives—but in some cases may actually promote engagement in labour markets. While the emerging evidence base suggests the short term effects may be relatively small—and certainly not a substitute for more pro-active employment policies—the longer term human capital impacts may prove a substantial complement.

### **Suggestions for further research**

27. Most of the direct rigorous evidence on linkages between employment and social cash transfers is limited a few middle-income countries, particularly South Africa. While anecdotal and indirect evidence exists for several other countries, additional credible evidence will more effectively support policy development. Three areas may prove fruitful:

- An extension of existing employment research approaches for South Africa to other countries, particularly Brazil and Mexico (where social transfers are likely to be large enough and implemented over a sufficiently extended time frame to have observed impacts measured in Labour Force Surveys) as well as further research for South Africa.
- More refined research that focuses on other aspects of livelihoods, other than formal employment. These would be particularly important in low-income countries where targeting mechanisms reach the very poorest—for whom a broader range of livelihoods strategies may be more important.
- Research into the linkages between social cash transfers and smallholder agriculture activity, particularly in the context of adaptation to climate change. In many developing countries, climate change is increasing the overall risk associated with smallholder production.

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111 The results from the uncorrected data are not materially different. After September 2004 Statistics South Africa ceased to track social grant status in its Labour Force Survey.

112 The matching methodology utilised for the analysis in this paper corrects a commonly cited problem with South Africa's Labour Force Survey, in which individual households are not properly linkable with the identifiers reported by Statistics South Africa. The results reported, however, are not sensitive to the specific approach taken to match the records. While there are small differences between these figures and those resulting from the uncorrected data, the magnitudes of the associated improvements are virtually the same with either approach.

113 For example, see Agüero, Carter and May (2006).

114 Baulch and McCulloch (1998) provide a clear explanation of the relationship between transition matrices and probabilities (in the context of poverty): "A poverty transition matrix shows the number of households in and out of poverty in a particular period, broken down by their poverty status in a previous period. Thus it is easy to see the number of households who have been poor or non-poor in both periods along with the number who have escaped poverty and those who have entered poverty. This approach has been used in a number of studies in both industrialised and developing countries. From any poverty transition matrix it is straightforward to calculate simple probabilities of entering and exiting poverty between the two periods. For example the simple probability of exiting poverty is simply the number of households exiting poverty divided by the number of households who were poor in the previous period." Labour market transition matrices work exactly the same way—except that the states are non-participation in the labour market, unemployment and employment rather than "poor" and "non-poor".