Economic Commission for Africa

Economic Report on Africa 2005

Meeting the Challenges of Unemployment and Poverty in Africa

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Foreword

With the highest incidence of poverty in the world, Africa urgently needs to create more employment and thus tackle the scourge of hunger, malnutrition and the overall low living standards the continent continues to witness.

Indeed, unemployment is one of the greatest challenges to Africa?s development, with an estimated 10.9 per cent and 10.4 per cent of job seekers unemployed in 2003 in Sub-Saharan and North Africa, respectively. These are respectively the second and third highest unemployment rates in the world, with the Middle East region experiencing the highest rate.

But the picture is even bleaker than these averages suggest, for they do not include the large numbers of working poor and those who have given up trying to find decent employment and are therefore not counted. Furthermore, these rates do not reveal the uneven distribution of unemployment across countries and regions, and within countries, age and gender groups. Based on the current demographic trends, it is estimated that Africa would need to create about 8 million new jobs every year in order to absorb the rising numbers of job seekers.

In addition to its traditional role of reviewing Africa?s economic performance over the preceding year, and projecting medium-term prospects for the continent, this year?s *Economic Report on Africa* (ERA 2005), the sixth in an annual series, provides a detailed analysis of the challenges of unemployment and poverty reduction, key issues at the heart of the debate on Africa?s development.

The poverty rate has remained practically stable on the continent for the past two decades, even as it declined in other developing regions. In real numbers, at least 61 million more Africans go hungry today than they did in 1990.

The creation of more decent jobs, accessible to the poor, constitutes the most effective channel through which poverty can be addressed in Africa. This link has been acknowledged at the highest political level over the last three decades. Most recently in 2004, Africa?s heads of state and governments adopted the Ouagadougou Declaration on ?Employment and Poverty Alleviation in Africa,? renewing their pledge to fight poverty through employment.

ERA 2005 provides an in-depth analysis of the obstacles to employment creation and proposes measures necessary to translate Africa?s political words into action.

Targeted to African and non-African policymakers and scholars to inform and stimulate discussions on the theme of employment and poverty reduction, ERA 2005 conducts a detailed analysis of the challenges of unemployment and poverty reduction in Africa.

The report notes that only about a quarter of Africa?s countries can show growth rates of at least 5 percent over the last decade. In addition to sustained growth, a more equitable distribution of the fruits of growth is crucial for effective poverty reduction. Sustained and equitable growth requires that African countries strengthen their economic and political governance.

Several initiatives on the continent show governments? commitment to improving conditions for people, giving me cause for optimism. In some countries, for example, information technology is being used to drive the labour-intensive and well-paid call-centre industry, the kind of strategy that could help reduce the continent?s over-dependence on agriculture.

Economic transformation that transfers a substantial part of the labour force from agriculture to other relatively productive sectors is imperative. For this to occur, governments must undertake reforms that provide an environment conducive to private enterprise operation.

I am confident that the analysis and recommendations in this 2005 edition of the *Economic Report on Africa* will be of benefit to African policymakers and their development partners in their collective fight against poverty in Africa.

K. Y. Amoako
Executive Secretary
September 2005
Addis Ababa

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Meeting the challenges of unemployment and poverty in Africa

Poverty in Africa is substantially higher than in other developing regions. More enigmatic is that poverty in Africa is chronic and rising. The share of the total population living below the $1 a day threshold of 46 per cent is higher today than in the 1980s and 1990s—this despite significant improvements in the growth of African GDP in recent years. The implication: poverty has been unresponsive to economic growth. Underlying this trend is the fact that the majority of people have no jobs or secure sources of income.

Various reasons have been given for Africa's lack of response of poverty to economic growth. First is the inadequacy of the growth rate. African countries need to grow by an estimated 7 per cent a year to reduce poverty enough to achieve Millennium Development Goal 1, of halving the number of poor people by 2015. This growth is far higher than the average of nearly 4 per cent in the last decade.

Second is the low labour absorption in the growth sectors. Growth has been concentrated in the traditionally capital-intensive extractive sector. Agriculture, which employs most people in most African countries, is characterized by low productivity growth, and thus has not provided enough real employment and income security to the population, particularly in rural areas.

Third is inequality in the distribution of opportunities created by economic growth.[1] Poor people lack the capacity to meaningfully participate in the economy, either as producers of goods and services or as suppliers of labour. There is a close association between employment performance and poverty prevalence: poverty rates have remained roughly constant in the same manner as the recorded unemployment rate since the 1980s (Tarantino 2003; ILO 2004c). And the volatility of growth has added to the vulnerability of poor people. Only a few countries in Africa have sustained growth over the years. Yet that is precisely what is required to increase employment and reduce poverty.

- Decent employment is the main escape route. A major route out of poverty in Africa is decent employment, a concept that encompasses the quality of employment—rooted in productive and secure jobs that provide adequate income and reasonable work conditions—and the quantity of employment.[2] Decent employment strengthens the link between economic growth and aggregate poverty reduction.

Prerequisites for creating decent employment include the transformation of African economies from low productivity traditional agriculture to labour-intensive high value agriculture

and agroprocessing—and to the growing industrial and services sectors, taking advantage of globalization's opportunities. Political leadership is thus required in managing African economies to give priority to broad-based employment creation in national development programmes, including poverty reduction strategies.

- Political awareness is emerging among leaders. Interest in dealing with Africa's employment challenge is emerging. African governments have, in recent years, asked about the connection between employment and poverty reduction and macroeconomic management and development frameworks.

The Declaration on Employment and Poverty Alleviation in Africa by the Heads of State and Government of the African Union in 2004 acknowledged that widespread poverty, unemployment and underemployment compromise basic human rights and the dignity of individuals and communities—and constitute a threat to social, economic and political stability. The declaration emphasized the urgency of employment creation as an "explicit and central objective of our economic and social policies".[3]

- Empirical analyses to guide policy are lacking. African development policies and poverty reduction strategies are often silent with regard to employment. Data on the labour market are often not available, undermining the capacity to translate a political agreement on the centrality of employment creation into concrete development strategies. The lack of detailed analyses of employment in national development programmes may be attributed to the assumption that growth would automatically translate into more jobs, and to the lack of understanding of how the labour market works in Africa (ILO and UNECA 2004). There is a need for thorough analysis of employment issues to inform the poverty reduction and development policies of African countries.

- ***Reducing poverty by generating employment.*** This report focuses on four key challenges for Africa in the fight against unemployment and poverty: achieving structural transformation to break away from the underutilizationse of rural labour, addressing widespread youth unemployment, harnessing globalization to create decent jobs and creating an enabling environment for accelerated expansion of private sector job-creation through increased investments.

The report puts forward concrete approaches for decent employment-based poverty reduction programmes in Africa:

- Structurally transforming the economies of African countries through labour-intensive technologies, underpinned by productivity enhancements in agriculture and the informal sector.

- Improving poor people's access to productive resources and requisite human capital to enable them to share in the benefits of growth.

- Minimizing regulatory obstacles to private investment, domestic and foreign and providing productive infrastructure to make domestic firms competitive in a globalizing environment.

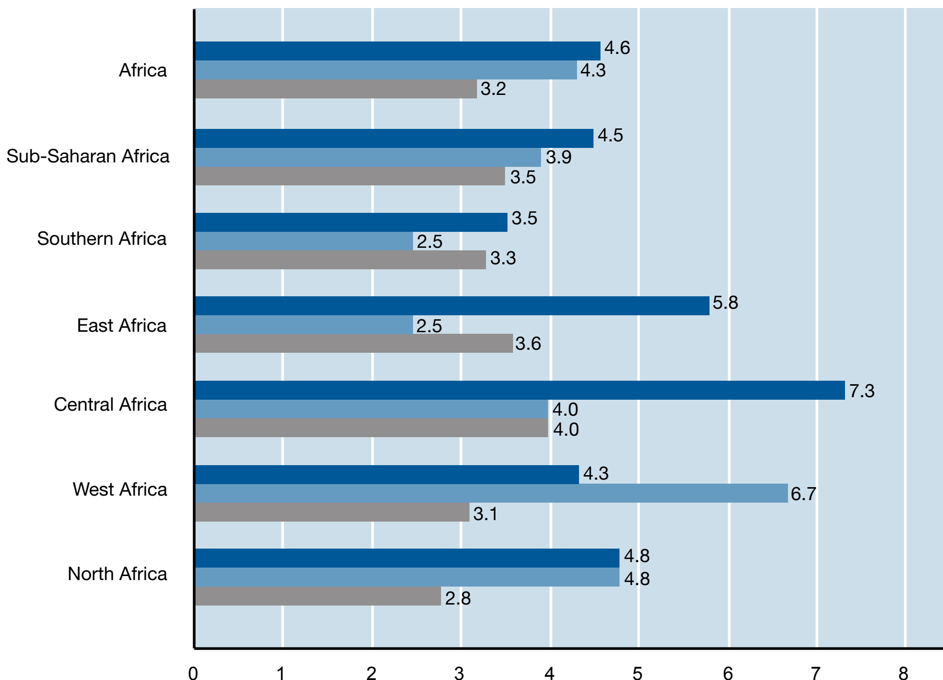
- Improving political governance to sustain growth, and to facilitate the equitable distribution of income and other economic opportunities, backed by the political will to secure change from traditional attitudes where desirable.

Macroeconomic performance

Higher GDP growth in 2004—but not enough to arrest poverty and unemployment

Africa recorded 4.6 per cent growth in 2004—the highest in almost a decade, and a continuing improvement over both 2002 and 2003 (figure 1). This improvement over 4.3 per cent in 2003 was underpinned by the strong global recovery and the resultant higher commodity prices, including higher oil production. Also contributing were good macroeconomic management, better agricultural performance across the continent, improved political situations in many countries and continued donor support in the form of aid and debt relief.

Figure 1
GDP growth, by African region, 2002–04 (%)



Source: *ECA, from official sources.*

Prospects for growth in 2005 are high for oil-producing countries but shaky for oil-importing countries. The weather is expected to continue to be favourable, in support of agricultural sector growth and overall economic growth in a low-inflation environment. But continuing appreciation of domestic currencies, especially in the euro-pegged economies, is likely to hurt growth.

Marked regional and country differences in growth performance

The regional differences in growth are marked (see figure 1). Except West Africa, regional growth was generally higher in 2004 than in 2002 and 2003. Central Africa was the fastest growing in 2002 and 2004. In 2004 it led the subregions with 7.3 per cent, followed by East Africa (5.8 per cent), North Africa (4.8 per cent) and West Africa (4.3 per cent).

Most countries failed, however, to meet the 7 per cent or more required to achieve Millennium Development Goal 1 to halve poverty by 2015. Only six countries achieved 7 per cent GDP growth in 2004: Chad (39 per cent), Equatorial Guinea (18.3 per cent), Liberia (15 per cent), Ethiopia (11.6 per cent), Angola (11.5 per cent) and Mozambique (8.3 per cent). Seventeen African countries registered positive but less than 4 per cent growth in 2004, while two contracted. Over 2000–04, only five countries achieved 7 per cent growth (Equatorial Guinea, Chad, Mozambique, Angola and Sudan), another nine grew at 5–7 per cent (Ethiopia, Rwanda, Liberia, Uganda, Burkina Faso, Mauritius, Senegal, Tanzania and Botswana), and two contracted (Seychelles and Zimbabwe).

Macroeconomic conditions—low inflation and improvements in fiscal health and the current account

Macroeconomic conditions in the region continued to improve in 2004, thanks to prudent monetary and fiscal policies, better food supplies, increased official development assistance (ODA) inflows and debt relief as well as higher commodity prices. The restoration of peace and the stable political situation in several countries also contributed to the favourable macro-economic climate.

Inflation—measured by the consumer price index—eased to single digits at 8.4 per cent, down from 10.6 per cent recorded in 2003, as the pressure from high oil prices was relieved by good harvests and tight monetary and fiscal policies in many parts of the continent. On average, the fiscal deficit of the central government declined to an estimated 0.8 per cent of GDP in 2004, from 1.5 per cent in 2003. This is a remarkable achievement given the pressure on many countries to increase spending on poverty reduction.

The current account registered a surplus of $2.8 billion in 2004, after three years of deficits. It improved from a deficit of 0.2 per cent of exports of goods and services in 2003 to a surplus of 1.2 per cent in 2004, thanks to rising oil and commodity prices. The number

of countries registering current account surpluses rose from 11 in 2003 to 14 in 2004, eight of them oil producers.

The Heavily Indebted Poor Countries Initiative provided fiscal support—but not enough to ensure sustainable debt

Major contributors to Africa's improved macroeconomic situation were the debt relief through the Highly Indebted Poor Countries (HIPC) Initiative and increased inflows of ODA. The HIPC Initiative aims to reduce the external debts of heavily indebted poor countries by providing debt relief, and thereby redirecting resources to investments in social development that would otherwise have been used for debt-servicing. Because the initiative is still unfolding, strong views on its long-term effects may be premature. But some key constraints have been identified: the slow pace of delivery, the probability of achieving long-term debt sustainability, methodological weaknesses in estimating sustainable debt, the difficulty for countries to remain on a policy reform track after the decision point and the insufficiency of debt relief.

Despite these constraints, 12 African countries had reached their HIPC completion point by the end of 2004 and qualified for debt relief. In 2004 alone five African countries reached their completion point in the enhanced HIPC Initiative: Ethiopia, Ghana, Madagascar, Niger and Senegal. While no country reached the HIPC decision point in 2004, 11 countries had reached it before that year, qualifying for interim debt relief. Burundi and the Republic of Congo are expected to reach their decision points in 2005.

Official development assistance is increasing

Net ODA flows to Africa, key for boosting growth in African countries, increased to a record high of $26.3 billion in 2003, from $21 billion in 2002. This reversed the downward trend since the 1990s. Development Assistance Committee (DAC) donors as a group donate far below the promised 0.7 per cent of gross national income (GNI) to ODA, but four countries exceeded this benchmark in 2003: Denmark (0.84 per cent), Luxembourg (0.81 per cent), the Netherlands (0.80 per cent) and Sweden (0.79 per cent). Expected ODA from DAC countries is projected to rise from the current 0.25 per cent of GNI to about 0.30 per cent by 2006, consistent with the Monterrey Declaration of 2002.

The unemployment challenge

While macroeconomic performance has markedly improved in Africa since the mid-1990s, there seems to be little impact on unemployment. Average annual GDP growth increased steadily from less than 3 per cent in 1998 to 4.6 per cent in 2004. Yet unemployment has hovered around 10 per cent since 1995 (figure 2).

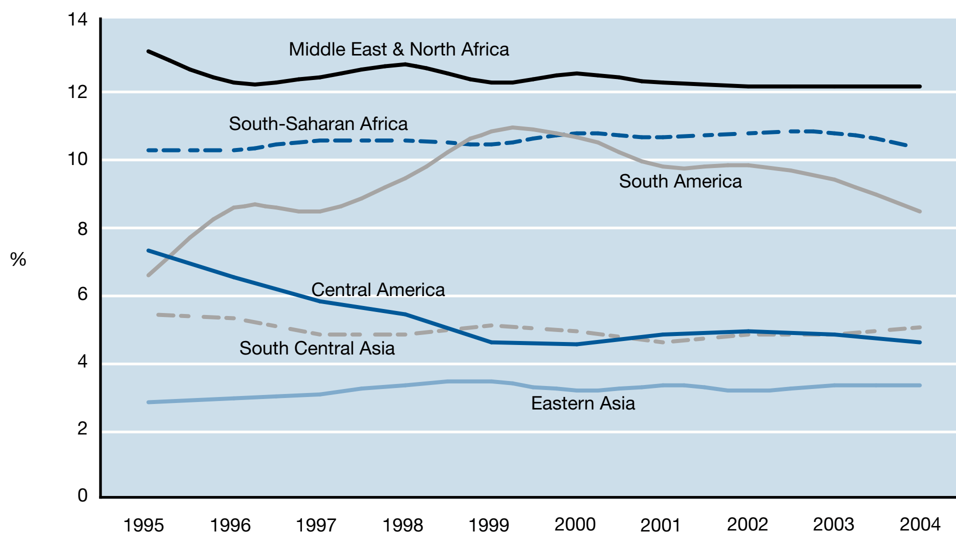
The employment picture is bleak

The average rate of unemployment for 2003 is estimated at 10.9 per cent for Sub-Saharan Africa and 10.4 per cent for North Africa, higher than most other developing regions (ILO 2004a) (see figure 2).

Measured unemployment in Sub-Saharan Africa was estimated at 29.4 million, with marked differences by subregion, country, gender and age group. West Africa had the lowest unemployment rate in 2003, at 6.7 per cent, explained mainly by low participation in paid employment and the formal sector. Southern Africa had the highest rate, at 31.6 per cent. Among countries, the unemployment rate is low in Uganda, at 7 per cent, but high in Lesotho, at 39 per cent, in 1997.[4] Young females in Sub-Saharan Africa have a lower unemployment rate (18.4 per cent) than males (23.1 per cent), but their labour force participation is lower.

Figure 2

Unemployment rates, by region, 1995–2004 (%)



Source: *Tarantino 2003.*

This "measured" unemployment for Africa, though higher than in other regions, seems unreliable and unrealistically low. Why? Many countries do not collect or report information. Reporting countries provide incomplete data, and not all the reported information is comparable across countries (box 1). Moreover, the computation of unemployment rates assumes that participants in the informal sector are employed, despite the fact that the vast majority of them work and earn very little.

Box 1

Comparability a problem? Yes

Labour market indicators may not be comparable across economies for several reasons.

- *Conceptual variation.* National statistical offices, even when using International Labour Organization conceptual guidelines, do not follow the same measurement of employment and unemployment. For example, countries adopt different age limits in their definition of the labour force. Lower age limits in available data vary from age seven in Uganda to age 18 in Tunisia. And some countries use different upper age limits in estimating unemployment rates: age 64 in Egypt and age 69 in Namibia. Moreover, countries such as Lesotho, Zambia and Zimbabwe estimate unemployment rates from the civilian labour force rather than the total.

- *Different sources.* National labour market estimates are based on information from different sources. These differences generate substantial discrepancies in unemployment rates. In South Africa the unemployment rate derived from employment office records was 5.4 per cent in 1997, while the rate from the 1999 household survey was as high as 25.3 per cent. Unemployment rates in Algeria, Burundi, Mauritius and Nigeria are obtained from official estimates, rendering them not comparable with unemployment rates from household surveys in Egypt, Kenya, Uganda and Zimbabwe

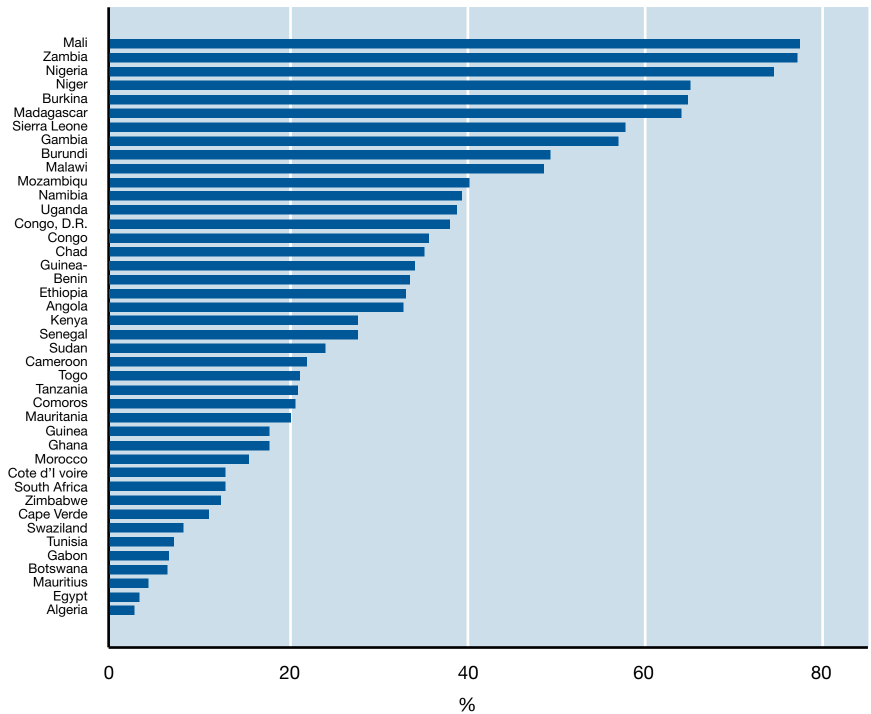
- *Changing number of observations per year.* Due to seasonality, statistics for a given year may differ depending on the frequency: monthly, quarterly, semiannually or annually. In some countries estimates are based on two observation periods a year: March and September for Mauritius, and May and November for Egypt.

Source: *ILO 2005a, 2005b.*

Unemployment is disguised by the high proportion of working poor and discouraged workers

The working poor account for almost 45 per cent of the total number of the employed in Sub-Saharan Africa (ILO 2004a). An estimated 110 million people considered employed earn below the poverty wage and are unable to provide their families with decent living conditions. In 1997 the working poverty rate was about 75 per cent in Mali, while only 3 per cent of the employed were living below the poverty line of $1 a day in Algeria (Majid 2001) (figure 3). The working poor are mostly engaged in the informal sector and in agriculture, where underemployment is the norm.

Figure 3
Working poverty rates, by country, in 1997 (%)



Source: *Majid 2001.*

Nonagricultural workers, especially women, are concentrated in the low-paying informal sector

Over 1994–2000 informal employment accounted for 72 per cent of nonagricultural employment in Sub-Saharan Africa (ILO 2002). If South Africa is excluded, this share rises to 78 per cent. In North Africa 48 per cent of nonagricultural employment is informal.

Informal employment is generally a larger source of employment for women. In Sub-Saharan Africa 84 per cent of female nonagricultural workers are informally employed, compared with 63 per cent for their male counterparts. In North Africa, however, only 43 per cent of female nonagricultural workers are informally employed, compared with 49 per cent for men.

Workers in the informal economy tend to earn less than their counterparts in the formal sector. For example, whereas workers in the formal sector are usually paid more than the minimum wage—thanks to government wage policy and union activity—survey evidence from five African cities shows historically high proportions of informal sector workers earning less than the minimum wage (Charmes 1990): 67 per cent in Yaounde, 43 per cent in Bamako, 33 per cent in Lomé and 23 per cent in Kigali.

Workers in the informal economy thus face a substantially higher prevalence of poverty—and a high exposure to risk, given the conditions they live and work in (Chen 2000). Informal workers also tend to have little or no access to formal risk-coping mechanisms, such as insurance and pensions, or to services for production. They also lack the resources to pay for housing, healthcare, education and training.

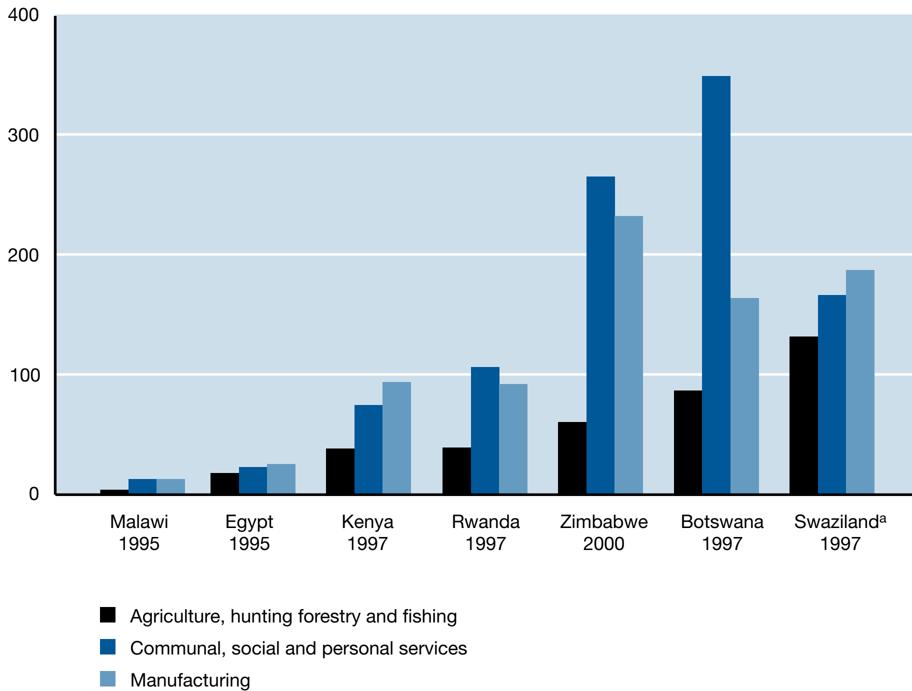
Several factors account for the exclusion of the bulk of the population from formal employment: slow growth of the formal sector, limited labour market endowments and institutional barriers such as unions.

High underemployment in the rural economy

Most workers in Africa are in the agricultural sector, characterised by seasonal underemployment. Many in rural areas work fewer hours than they would like, earn less than their counterparts in manufacturing and services (figure 4), use their skills less and are generally less productive.

Figure 4

Monthly wages by sector for seven African countries, various years ($)



***a.** Data are for unskilled workers only.*

***Source:** ILO 2005b*

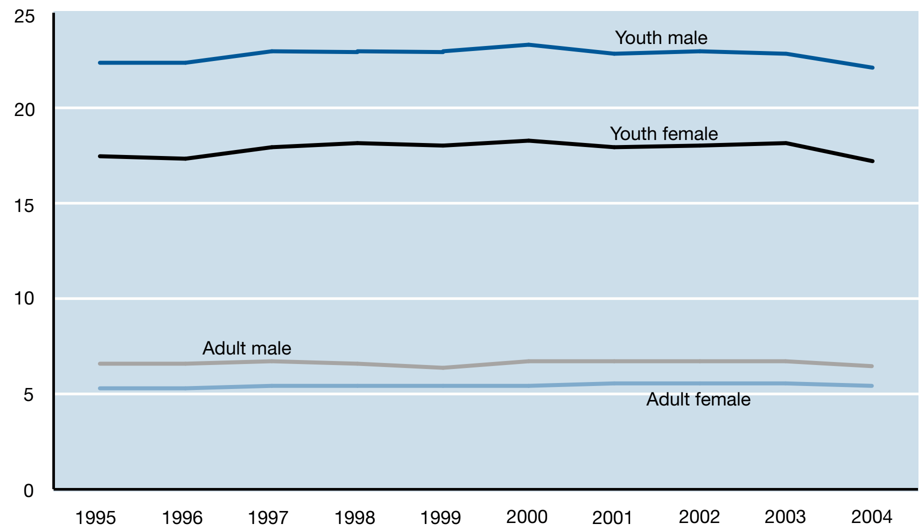
In addition, traditional work arrangements—where the available tasks are through voluntary labour exchanges and community labour, common in many rural communities—distort labour allocations and lower the hours worked and incomes of individual community members. This under utilisation of the labour force's productive capacity is a major source of working poverty.

Youth unemployment is twice the average

Unemployment among youth is a particular problem in Africa (figure 5). At 21 per cent in Sub-Saharan Africa and 22.8 per cent in North Africa, the unemployment rate for youth ages 15–24 was twice that of the overall labour force in 2003 (ILO 2004b). In Sub-Saharan Africa unemployed youth as a share of the total unemployed was 63 per cent, even though youth made up only 33 per cent of the labour force. These much higher unemployment rates for youth hold for both males and females (see figure 5).

Figure 5

Unemployment rates in Sub-Saharan Africa, by gender and age group, 1995–2004 (%)



__Note: Youth__ refers to people ages 15–24 (or the closest available ages); __adult__ refers to people ages 25–64.

__Source:__ Tarantino 2003.

Female unemployment is disguised disproportionately

The official unemployment rate is lower for women than for men among both adults and youth, though more so for youth (see figure 5). This gap is observed only in Sub-Saharan Africa and East Asia. And the reality of the African labour environment is that

a disproportionately large share of female unemployment is disguised (box 2). So the effective unemployment rate for women is likely to be higher than what official statistics indicate.

Box 2

Female unemployment in Africa is underestimated

Female unemployment in Africa may be underestimated for several reasons:

Given social norms, women are disproportionately involved in unpaid work at home and are not counted as unemployed.

More women than men can also be classified as "discouraged workers." Women are less likely to find jobs in an environment of high unemployment so they drop out of the formal labour market and perhaps resort to the informal sector. In either case, they would not be counted as unemployed in the official statistics, and their unemployment would be "disguised".

The official unemployment rates mask the fact that female workers are mostly in informal employment in Africa. In Sub-Saharan Africa 84 per cent of female nonagricultural workers are in the informal sector, compared with 63 per cent of males. In addition, most female informal sector workers are in self-employment rather than wage employment. In North Africa 72 per cent of female informal sector workers were self-employed in 1994–2000.

Source: *ILO 2002.*

The poverty-unemployment relationship

Poor people have severely limited access to, and control over, key assets, including land and physical and human capital. Lacking production and labour market endowments, the poor have low income and low consumption. Most poor people are also inadequately educated and may be less healthy than the rest of the population. Many depend for their livelihoods on (low productivity) subsistence agriculture or on the informal sector, where returns to labour and capital are generally low. Workers in the informal sector have low salaries, limited protection and frequent spells of unemployment. These factors, coupled with lack of access to the institutions that shape policies, prevent poor people from acquiring the capabilities for decent living.

The number of people living below the poverty line only tells half the story. In Africa, not only do many people live below the poverty line but they also stay poor for long and sustained periods. Many of these chronically poor people only emerge briefly from poverty because of seasonal employment, but lack the impetus to contribute to technological change and economic growth. Unable to directly participate in the growth process, for this group, albeit insufficient, overall economic growth is necessary to boost their incomes.

In sum, the absence of a clear link between economic growth and poverty reduction has been shaped by two factors: first, the low employment intensity of the growth process, and second, poor people's inability to integrate into the growth process and reap the gains from employment opportunities.

Employment content of poverty reduction programmes needs to be addressed

A major framework for poverty reduction in Africa is the Poverty Reduction Strategy Paper (PRSP), an initiative of the World Bank and the International Monetary Fund, embraced by many African countries. This instrument has enabled countries to increase investment in social services and achieve good results from fiscal operations. However, there is a need to re-think how employment can be mainstreamed into PRSPs. An evaluation of the 21 full PRSPs in Africa reveals considerable scope for incorporating neglected aspects of employment. Policy measures should be more sensitive to addressing African national employment concerns more systematically.

Most PRSPs do address employment generation through policies in agriculture and rural development, credits and loans, education and training, infrastructure investment, institutional capacity building and private sector development. But important employment effects of other policies—such as liberalization and privatization, global and regional integration and the effects of globalization—are ignored.

Broad-based employment growth is required to reduce poverty

Curbing poverty through employment generation demands deliberate action. It requires coordinating the supply and demand for labour, because employment-intensive growth is necessary but not sufficient. That is, even if jobs are create, it is unlikely that the poor possess sufficient skills to take advantage of the new employment opportunities. That is why poor people must have access to human capital (education, skills and training, health), to assets such as land, and to markets. Special measures are required to overcome gender discrimination and restrictive labour regulations.

Meeting the challenges of employment for poverty reduction

The fundamental issue in Africa's labour markets is the failure to create more and better paid jobs to meet the needs of the labour force and reduce poverty. The four key challenges:

- Achieving structural transformation to break away from rural underemployment and poverty.
- Addressing youth unemployment.

- Harnessing globalization to create decent jobs.
- Facilitating private sector investment to create more employment.

Structural transformation is required to break away from rural underemployment and poverty

Stronger linkages among sectors, especially between the rural agricultural economy and the modern industrial and service sectors, are needed to enhance the employment and poverty-reduction effects of growth. They require structural transformation of African economies to generate employment growth that at least match the growth of the labour force.

The problem of low employment is rooted in the lack of structural economic transformation to diversify away from an agricultural sector characterized by low and falling productivity (Khan 1997). Agricultural productivity growth and increased farm incomes are prerequisites for structural transformation. Feedback from productivity gains in agriculture has been shown to spur growth of the manufacturing sector, for example. Empirical evidence shows that poverty reduction is strongest when agricultural growth is sustained at above 2 per cent a year (Islam 20045 [2004 in references]).

The continued annual decline in agricultural labour productivity in Africa therefore constitutes an impediment to structural transformation (FAO 2005).

The African labour force has been locked in this sector using traditional methods of production without expanding manufacturing and services to absorb excess labour from agriculture. Meanwhile, rapid urbanization has created an urban labour surplus. Raising productivity across the economy requires increased financial and human capital development, which requires demographic transition—namely, low mortality and fertility rates.

To transform the agricultural and the rural sectors would require agroindustrial, agribusiness and service sector development to be accompanied by increased agricultural productivity through initiatives that promote human capital development and spur a green revolution. This would have positive effects on urban labour markets by reducing food prices and hence the nominal wage growth necessary to absorb labour in the urban industrial sector.

Stimulating structural transformation in Africa to accelerate growth, create employment, and reduce poverty hinges on completing Africa's demographic transition, smoothing population migration from rural to urban areas and reducing population and urbanisation growth rates; increasing agricultural productivity, and enhancing agricultural links to the industrial and service sectors; and facilitating the growth of job-creating small and medium-size enterprises through rigorous public-private partnerships to improve the provision of infrastructure, credit, inputs, markets, training and other services.

Youth unemployment needs to be tackled head-on

Youth in Sub-Saharan Africa are 3.5 times more likely to be unemployed than adults are (ILO 2004b). A survey in South Africa found that 39 per cent of unemployed youth had almost stopped actively searching for a job (Kanyenze, Mhone and Sparreboom 2000). Less experience and inadequate education put youth at a disadvantage even when higher economic growth translates into overall increased employment opportunities. During periods of economic upturn youth are the last to be hired, and in economic downturn they are first to be fired.

Severe economic and social costs are associated with youth unemployment. With limited options unemployed youth are more likely to engage in criminal behaviour, particularly armed robbery, as evidenced by events in Nigeria and South Africa, as well as other high risk and self-destructive behaviour, such as sex work and illicit drug use. A particularly troublesome adverse consequence of youth unemployment is the recruitment of child combatants for armed conflict, which has harmed African economies (Fosu 2005a). Key tasks to address the special difficulties of youth in labour markets are: mainstreaming youth employment programmes and policies; reforming education; engaging in public-private sector partnerships in order to secure resources; and providing for the health of youth, especially young women.

Mainstreaming youth in key development programmes such as poverty reduction strategies is imperative for addressing the youth employment problem. However, the employment content of PRSPs in Africa remains weak. This shortcoming must be addressed in the next generation of poverty reduction strategies. Furthermore, the development of national employment strategies targeting youth employment should be accelerated by adoption of the UN Secretary-General's Youth Employment Network initiative, coupled with the establishment of job centres with specific youth departments.

Youth unemployment is partly the consequence of a mismatch between inadequate educational outcomes and skills demanded (Boateng 2002). The educational system must provide the skill profiles required by the labour market if employability of young people is to be enhanced. At the formal school level this requires achieving full enrolment in primary schools and reducing dropout rates. Also required are complementary policy interventions to enhance quality, gender parity, curriculum development and technical and vocational education.

Partnerships are essential for overcoming financial and resource constraints in education. They also help provide feedback from the private sector to the educational system on labour market needs, thus mitigating the skills mismatch in education systems in much of Africa.

Health policies that address youth in general, and young women and HIV/AIDS in particular, are crucial. Good health is the basis for performing well in education, training and on the job. The causality between youth health and unemployment runs both ways. On one hand, unemployed youth are vulnerable to the health risks associated with poverty, marginalisation and risky behaviour. On the other hand, poor health status constrains

young people from actively participating in the labour market due to absenteeism, which compromises their trainability and undermines productivity.

Harnessing globalization to create decent jobs and reduce poverty

Although Africa's share in worldwide flows of trade, investment and remittances is low, globalisation affects its economies substantially.[5] On the basis of foreign trade as a share of GDP, Africa is one of the most open regions in the world, behind only East Asia. However, the share of foreign direct investment in GDP remains at around 2 per cent, and worldwide, foreign direct investment has fallen, while Africa's share of world exports has declined from about 6 per cent in 1980 to approximately 2 per cent in 2003 (UNCTAD 2004). Africa has apparently failed to harness the forces of globalization.

Globalization plays an important role in creating decent jobs in the domestic labour market through increased investments, diffusion of technology and improved labour standards. However, there are downsides. Domestic economic decisions are heavily influenced by global conditions, and production processes are spread over several continents, meaning employment could be less stable and requiring measures to address these downside risks.

The magnitude of benefits from globalization is positively linked to productivity growth. Trade and foreign direct investment will increase only if a country is competitive in the international market. Competitiveness in turn depends crucially on wage-adjusted productivity. Likewise, there is a strong link between productivity growth and poverty reduction, as increases in productivity will allow wages to rise. Though a higher share of exports is generally associated with less poverty, this effect is stronger for countries with high literacy rates and a low share of raw material exports.

To create competitive conditions for enhancing the positive impacts of globalization for poor people, the following measures are recommended:

- ***Upgrading skill levels.*** Globalization will increase employment and reduce poverty in Africa only if skill levels are improved and economic structures are transformed. The East Asia success story of the 1970s and 1980s is not likely to be repeated in Africa if skill supply is inadequate. Unit labour costs in Africa are higher than in East Asia. To be competitive African countries need to increase and retain investment in human capital and address institutional factors fuelling nominal wage growth.

- ***Developing key infrastructure.*** Infrastructure provides the main mechanism for transmitting global opportunities to local markets. Lessons from both Asian and African countries show that productivity and hence employment-creating investments can be raised if key infrastructure is installed. Information and communication technology infrastructure, for example, has to be updated. In an increasingly knowledge-intensive world support for knowledge-based development is necessary for effective participation in the world economy (Lall 2004).

- ***Well designed industrial policies.*** The "Asian miracle" was not driven by liberalization *per se* but by well-designed industrial policies, including directed credit, trade protection, export subsidization and tax intervention. The East Asia policy package worked because incentives were combined with discipline through government monitoring and the use of export performance as a productivity yardstick. In Africa export processing zones have been successful in Madagascar and Mauritius. By 2001 in Madagascar export processing zones firms had created more than 100,000 jobs (Glick and Roubaud 2004). Women accounted for 68 per cent of workers in the sector, though their share declined as the skills intensity of jobs increased. To be successful, export processing zones need strong government backing and effective public management to closely monitor enterprises. They should also be embedded in an outward-oriented strategy of development.

- ***Promoting sector and industry links.*** Labour-intensive sectors, as well as firms with strong links to other sectors of the economy, should be preferred in order to increase the domestic impact of technological upgrading. Link programmes should focus on the competitive needs of domestic enterprises through private and public support institutions. Indeed, complementarities with domestic firms should be the selective basis for attracting foreign direct investment (Fosu 2004).

- ***Taking a stake in global value chains.*** Tighter management of global value chains by multinational firms requires products of higher quality and more reliable supply. To increase the benefits from production of high value agricultural products, smallholders must be linked to international markets through those value chains. For example, to help small Kenyan farmers participate more in value chains of horticultural production, support for farmer groups, including joint irrigation schemes, is needed. Also needed are market information, extension services and standards. New institutional arrangements are needed to enforce contracts between farmers and exporters. These measures can reduce the risk for both farmers and exporters of high value products.

- ***Encouraging the African diaspora to invest.*** Migrants can contribute to employment creation through remittances. For example, migrants have financed most of a small Senegalese village's collective projects, such as the post office, drinking water systems, community clinics and school renovation. Likewise, returning migrants can use their experience and contacts to set up businesses. Migrant networks should be regarded as an asset and better exploited. Because contract enforcement across borders is especially difficult for small and medium-size enterprises, ethnic networks can play a crucial role in fostering cross-border trade and investment links. Furthermore, migrants can facilitate the flow of information and knowledge, thereby increasing productivity.

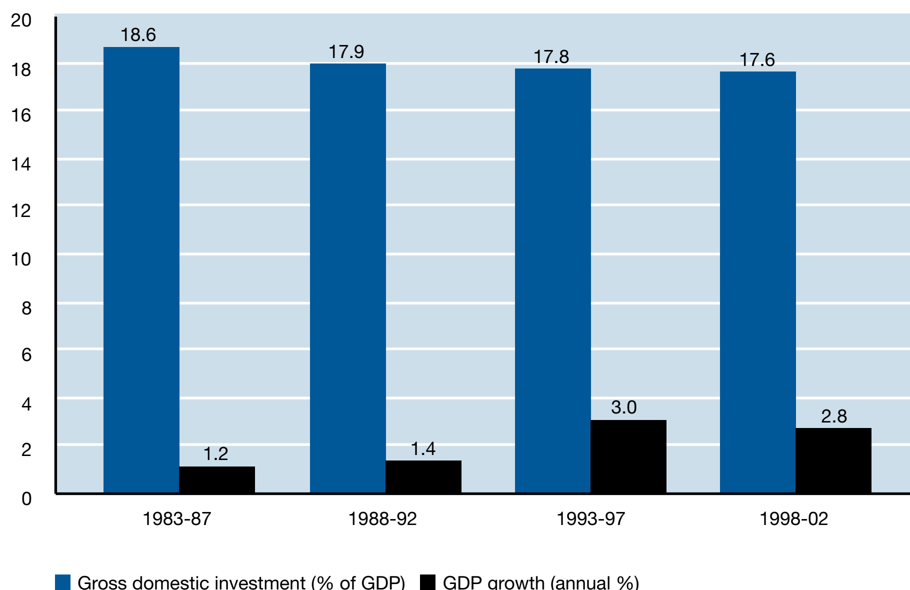
- ***Mitigating risks of globalization.*** Mitigating the adverse effects of globalization includes providing basic social security, retraining workers for growing sectors and improving access to education and credit. Providing safety nets will not only reduce adjustment costs but could also have positive dynamic effects. If poor farm households were protected against income losses, they could take on riskier but higher return activities, thus raising their average income.

Creating an enabling environment to generate decent private sector jobs

The public sector has traditionally been the largest employer in Africa. Facing fiscal constraints, however, African governments can no longer fulfil this task. So far, the formal private sector has not been able to take over the role as the major job supplier, with only around 10 per cent growth in employment (Adenikinju and Oyeranti 2003). Today, the role of government is to create an enabling environment for private sector development, the fruits of which include increased investments and employment for the population.

Macroeconomic stability is a key to an enabling investment environment. Macroeconomic stability in Africa was largely achieved in the mid-1990s: fiscal deficits have mostly been kept under control, exchange rate regimes have become more flexible, and inflation has been kept below double-digit levels in most countries. Meanwhile, economic growth has picked up. But it has not been associated with higher levels of investment. The average investment rate for Sub-Saharan Africa has largely stagnated over the last two decades (figure 6), suggesting that the improved growth performance is attributable to increased productivity of capital.

Figure 6
Gross domestic investment and real GDP growth in Sub-Saharan Africa, 1983–2002



Source: *World Bank 2004b.*

High transaction costs, resulting from an unfriendly business environment, are one of the main reasons why private investment is lagging. There is the need for African countries to address constraints in the business sector—poor infrastructure, the institutional setting responsible for the high cost of starting and operating a business and limited access to finance—in order to encourage private sector investment and create jobs. The cost of registering a business in Africa is the highest in the world, and is one of the main reasons why many small businesses decide to remain informal (World Bank 2004a). Firm surveys from various African countries reveal that bribes are a major cost to business, and the prevalence of corruption is linked to unpredictable and nontransparent interpretation of regulations (Collier 2000).

Poor infrastructure, in particular poor road networks, unreliable energy supply and insufficient telecommunication facilities create high transaction costs and are serious obstacles to operating a business. For example, in Uganda a survey of 243 firms found that firms often have to purchase their own generators because of unreliable energy supply (Reinikka and Svensson 1999). This cost represents 25 per cent of the firm's total investment in equipment and machinery. And many small firms cannot afford a generator. Given the constraint of public resources, infrastructure is a promising field for public-private partnerships.

Contract enforcement in Africa is extremely costly and lengthy. In four countries (Burkina Faso, Chad, Democratic Republic of Congo and Malawi) the cost is often higher than the claim itself (World Bank 2004a). So far, few African countries besides Tunisia, which has one of the fastest procedures for contract enforcements in the world, have successfully reformed.

Many informal sector enterprises in Africa fail to grow and succeed in the formal sector because the entrepreneur lacks bookkeeping and market analysis skills. Access to finance is also a major constraint for small enterprises in Africa. In most African countries banks are reluctant to lend to small and medium-size enterprises because small loans have high transactions costs and risks and low returns. Also supervisory and capital adequacy requirements often discourage serving small borrowers who lack collateral. Promoting microfinance institutions would increase the possibilities for the financial sector. For example, in Swaziland microfinance institutions provide 38 per cent of formal loans (Elhiraika 1999).

Labour markets in Africa suffer from several market failures. First, institutions such as public employment centres lack adequate resources to effectively coordinate labour demand and supply. Second, the state often intervenes in the labour market to protect workers. Although protecting labour is important, overprotecting labour can raise the implicit cost of labour, thereby discouraging employment in the private sector, as seen in several African countries.

Based on best practice examples across the continent and other developing countries, the following proposals should help address these constraints in Africa:

- ***Improving infrastructure.*** Private-public partnerships are key to mobilizing the resources required for improving infrastructure in Africa.

- ***Reducing transaction costs for formal sector businesses.*** A way to reduce business registration costs is to provide one-stop shops and minimize the number of required procedures. For example, by introducing one-stop shops, Morocco successfully reduced to five the number of registration procedures. Ethiopia also decreased the cost of registering a business by 80 per cent in 2003 simply by abolishing the requirement to publish notices in two newspapers.

- ***Addressing corruption.*** Addressing corruption starts from reforming bureaucracy, paying decent salaries, creating credible institutions to prosecute corrupt activities, and raising awareness of how corruption undermines the system.

- ***Ensuring contract enforcement.*** Having enforceable contracts is a key issue for a functioning private sector. Successful experiences worldwide show that successful reform must include bringing cases to court without lawyers, reducing written documents, improving information systems and judicial statistics, and introducing summary proceedings and random case management.

- ***Promoting entrepreneurial skills and harnessing networks.*** The positive returns from entrepreneurial training in Malawi and Zambia suggest that entrepreneurial training should be increased and entrepreneurial skills integrated into school and university curricula (Baerenz and Roesch 2003).

- ***Getting the financial sector ready for small-scale lending.*** Collateral requirements must be reformed to enhance small-scale lending. Introducing private and public credit registries with information on a client's track record would reduce the problem of asymmetric information, and could improve small and medium-size enterprises' access to credit, while reducing loan costs.

- ***Preparing the labour market to coordinate private sector employment.*** Job centres must be more than mere placement agencies. They need to assess training needs and offer adequate training in order to effectively coordinate demand and supply in labour markets.

- ***Improving overall governance.*** Improved public financial management, adherence to the rule of law and democratic principles, and macroeconomic stability are essential for generating sufficient investments to create employment and reduce poverty.

The way forward: a summary of policy recommendations

Decent employment should be at the heart of the poverty battle. Central to the poverty problem have been: the slow growth of jobs in the formal sector, the low earnings and low productivity in the informal sector, which employs most of the urban labour force, and stagnation in the agricultural sector, employing most of the rural population.

African employment and poverty reduction policymakers should therefore undertake measures aimed at:

- Improving agricultural productivity through modern farm techniques, small-scale irrigation and improved storage and packaging as well as strengthening agroprocessing and marketing infrastructure to link agriculture with other sectors of the economy.

- Promoting labour-intensive techniques, particularly in sectors that employ a disproportionate share of poor people.

- Diversifying exports to minimize adverse effects of terms of trade instability on households.

- Reducing taxes on producers to ensure that labour benefits from improved terms of trade.

- Bolstering intersectoral links to maximize spillover effects of growth through the design and promotion of integrated development projects.

- Maximizing private sector job creation by removing constraints to investments and growth and by minimizing bureaucratic constraints.

- Setting identifiable employment targets in a comprehensive development strategy to facilitate effective monitoring of progress in realizing employment goals.

- Ensuring that poverty reduction is incorporated into national budgets and is given priority funding from domestic and external sources.

- Implementing the policy recommendations of the Declaration on Employment and Poverty in Africa in the context of committed leadership, backed by sound analytical research.

Endnotes

1. For example, Ali and Thorbecke (2000) and Fosu (2005b) find that income inequality, resulting most likely from inequality in the distribution of opportunities, has a greater impact on poverty than growth.

2. "Decent work" sums up the aspirations of people in their working lives. It involves quality of opportunity for all women and men and opportunities for work that is productive and that delivers a fair income; security in the workplace; social protection for families; better prospects for personal development and social integration; and freedom for people to express their concerns, organize and participate in the decisions that affect their lives (see www.ilo.org/public/english/decent.htm).

3. See Commitment 5 of AU (2004).

4. See ILO (2004b).

5. For a survey on the importance of the global context for African economies, see Fosu (2001).

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Recent economic trends in Africa and prospects for 2005

Africa recorded 4.6 per cent growth in 2004, the highest in almost a decade. This improvement over 4.3 per cent in 2003 was underpinned by a strong global recovery, higher commodity prices and higher oil production and prices. Also contributing were good macroeconomic management, better agricultural performance across the continent, improved political situations in many countries and continued donor support through aid and debt relief.

> *Africa is far from the 7% growth needed to halve poverty by 2015*

Even so, Africa's overall economic growth fell short of the 7 per cent required to achieve Millennium Development Goal 1 to halve poverty by 2015. In 2004 only six countries realized growth rates of 7 per cent or higher: Chad (39.4 per cent), Equatorial Guinea (18.3 per cent), Liberia (15 per cent), Ethiopia (11.6 per cent), Angola (11.5 per cent) and Mozambique (8.3 per cent). Among them, only Chad, Equatorial Guinea and Mozambique have sustained growth of at least 7 per cent a year since 2001, and Angola since 2002. Except in Mozambique, oil fuelled this growth. Highly capital intensive, the oil sector's direct contribution to poverty reduction through employment generation is quite limited. And sustained growth alone may not translate into meaningful poverty reduction unless linked to broad-based employment creation.

Continuing improvements in macroeconomic conditions in 2004 contributed to African growth. On average, policymakers in the region pursued prudent monetary and fiscal policies. Inflation—measured by the consumer price index—eased to single digits at 8.4 per cent, down from 10.6 per cent in 2003, as the pressure from high oil prices was relieved by good harvests in many parts of the continent. Fiscal deficits of the central government fell to an estimated 0.8 per cent of GDP in 2004, from 1.5 per cent in 2003. This is a remarkable achievement, compared with fiscal performance in other regions of the world and given the pressure on many countries to increase spending for poverty reduction while maintaining low fiscal deficits.

By freeing up resources that would otherwise have been devoted to debt servicing, the Heavily Indebted Poor Country (HIPC) Initiative contributed to the improved fiscal position of eligible African countries and provided greater scope for higher social spending. In 2004 five African countries reached their completion point in the enhanced HIPC Initiative and received further debt relief: Ethiopia, Madagascar, Niger, Ghana and Senegal. While no country reached the HIPC decision point in 2004, Burundi and the Republic of Congo are expected to reach their decision points in 2005.

In several African countries higher commodity prices, including those for oil, improved the external balances. The estimated current account surplus of $2.8 billion in 2004 follows three

years of deficits. The regional current account balance has improved from a deficit of 0.2 per cent of exports of goods and services in 2003 to a surplus of 1.2 per cent in 2004. Some 14 countries registered current account surpluses, up from 11 in 2003, 8 of them oil producers.

"The continent faces several downside risks in 2005"

Notwithstanding the generally favourable economic trends in 2004, the continent faces several downside risks in 2005. The continued momentum in the global economy is marred by significant international imbalances, as evidenced by the large current account deficit in the United States and matching surpluses concentrated in a few EU member countries. A sharp depreciation of the U.S. dollar continues to be a possibility. It would lead to a decline in consumption, import demand and foreign investment in the United States, which could seriously impede the pace of global economic growth. Uncertainty about the direction of oil prices, already very high in nominal terms but lower than historical highs in real terms, poses another risk to the regional outlook. Finally, ongoing political instability in Sudan and Côte d'Ivoire may affect neighbouring countries.

The growing global economy

In 2004 the global economy posted 4 per cent growth, the strongest in two decades. Much of it was driven by the robust U.S. economy and the rapid growth in Asia, particularly China. Global economic growth in 2004 was not only strong, but also widespread. Except in South Asia and the Commonwealth of Independent States, growth picked up in all regional groupings in 2004 (UN 2005). The initial fear that the oil price rise would limit the global recovery did not materialize, because the effects were offset by strong global demand and rising non-oil commodity prices (box 1.1).

Figure 1.1

Annual real GDP growth of OECD, euro zone and G7 countries, 2002–04 (per cent change over the same quarter of the previous year)

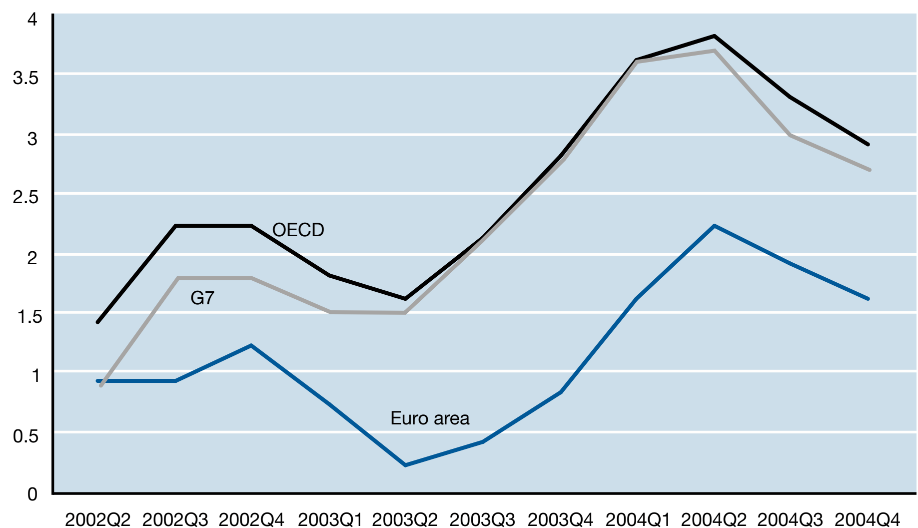
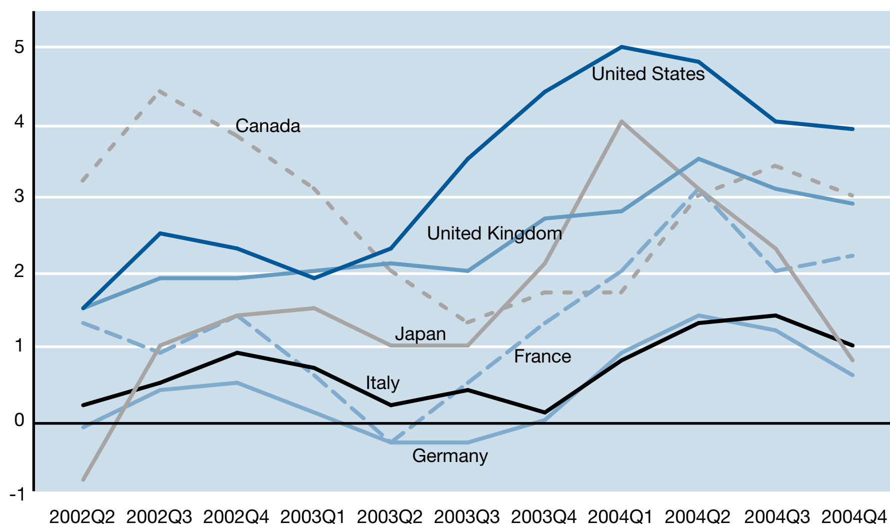


Figure 1.1 *(continued)*
Annual real GDP growth of OECD, euro zone and G7 countries, 2002–04 (per cent change over the same quarter of the previous year)



Source: *OECD 2005*

> *Improved, chances remain slim for recovery of private investment*

The U.S. economy registered 4.4 per cent real growth in 2004, up from 3 per cent in 2003, as a result of the significant rise in personal expenditures on durable goods, which was supported by a robust rate of expansion in non-residential fixed investment (figure 1.1). The twin deficits accelerated in the United States in 2004: the growing trade deficit led to another historical high current account deficit of 5.7 per cent of GDP, while the federal

Table 1.1
Quarterly GDP growth rates of G7 countries, 2002Q4–2004Q4 (per cent change over previous quarter)

	2002	2003				2004			
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Euro zone	0.0	0.0	–0.2	0.6	0.4	0.7	0.5	0.2	0.2
G7	0.2	0.2	0.5	1.2	0.9	1.0	0.6	0.5	0.5
Canada	0.5	0.7	–0.2	0.3	0.8	0.7	1.1	0.7	0.4
Germany	0.0	–0.4	–0.2	0.3	0.3	0.5	0.4	0.0	–0.2
France	–0.3	0.1	–0.4	1.1	0.6	0.7	0.7	0.0	0.8
Italy	0.3	–0.2	–0.1	0.4	0.0	0.5	0.4	0.4	–0.3
Japan	0.3	–0.4	0.7	0.5	1.4	1.4	–0.2	–0.3	–0.1
United Kingdom	0.3	0.4	0.4	0.9	1.0	0.6	1.0	0.5	0.7
United States	0.2	0.5	1.0	1.8	1.0	1.1	0.8	1.0	0.9

Source: *OECD 2005*

government budget deficit deteriorated to roughly 3.6 per cent of GDP. Thus, waning of fiscal stimuli, tightening monetary policy and little recovery in employment may lower 2005 growth prospects.

In 2004 the euro area grew at a lacklustre 1.8 per cent, up from 0.5 per cent in 2003. Behind this slow recovery were the appreciation of the euro (which reduced export growth), weak consumer spending due to uncertainties in the labour markets and the absence of significant positive fiscal stimuli. Even though growth in private investment picked up after falling for three years, prospects for a strong recovery in 2005 are slim. In particular, an appreciating euro and continued weakening of domestic demand are likely to dampen euro area activities.

Box 1.1

The oil factor in the international and local economy

Oil prices shot up in 2004, with the average spot price for the year about $38 a barrel. Prices were highly volatile throughout 2004. By mid August the price per barrel had risen $14 from its price at the beginning of the year, driven by increasing demand for oil, low and declining inventories, limited spare capacity and the volatile security situation in the Middle East, which led to speculative activities in oil markets.

The initial economic impact of high oil prices-at the international level-occurs through a transfer of income from oil-importing countries to oil-exporting countries. For most oil importers, higher oil prices reduce their demand for imports of oil and other goods and services. By contrast, income gains by oil exporters increase demand in their countries, though the gains are not immediately spent. The consequent decline in global demand and output has hurt the external financial situation of oil-importing countries, particularly low-income countries with heavy foreign debt burden and precarious balance of payments.

Higher oil prices imply an increase in the costs of production, which are then passed on to final products. This may increase inflation, the severity of which will depend on the extent to which higher oil prices are reflected in the prices of final products, inflationary expectations and their consequences for wage formation, and the effectiveness of anti-inflationary policies. The negative impact of higher oil prices on income, business profits and inflation may cause negative wealth effects and a decline in business investment, affecting the real economy. Restrictive fiscal and monetary policy measures to fight inflation may have a further negative impact on the real economy.

Simulations of the impact of an increase in oil prices suggest that a 20 per cent rise would reduce gross world product by 0.2–0.3 percentage points a year (IMF 2000; International Energy Agency 2004). Among developing countries, oil-importing Sub-Saharan African countries stand to lose the most—more than one percentage point of GDP—because oil imports account for more than 10 per cent of GDP in most of these countries.

Source: *UN 2005*

Japan's economy recovered strongly in 2004, with a growth rate of 4 per cent, up from 2.5 per cent in 2003. Initially the recovery was driven by strong growth in exports, but other sectors, particularly manufacturing, gradually contributed to the growth momentum. The prospects for 2005 depend heavily on external factors. Growth in China and the United States, oil prices, global information and communication technology sector performance and exchange rate developments will largely determine these prospects. Economic activity in other parts of Asia was buoyant in 2004. Leading the pack was China, which continued to outperform expectations. The real GDP of China grew by more than 9 per cent in 2004, driven mainly by high investment supported by very robust retail sales and exports. Expected to remain the regional powerhouse, China's GDP is projected to grow at a lower rate of 8.7 per cent in 2005.

The world economy's growth rate is expected to slow to 3.2 per cent in 2005 thanks to the dampening effect of high oil prices, the end to the fiscal as well as monetary stimulus in the U.S. economy and the slowdown in the Chinese economy in response to deliberate measures to cool down the economy. Given China's growing importance as a driver of world trade growth, the anticipated slowdown in the Chinese economy could significantly dampen global economic activity, particularly for its major trading partners.

"Prospects for FDI inflows are favourable in 2005"

Recovery in foreign direct investment flows to Africa

While global foreign direct investment (FDI) inflows declined in 2003 for the third consecutive year, Africa registered an increase, from $12 billion in 2002 to $15 billion in 2003. And preliminary estimates for 2004 show that FDI inflows to Africa rose to $20 billion. High prices of key commodities attracted new exploration projects from overseas, mainly concentrated in diamond, gold, oil and platinum. In recent years improved investor perception and regulatory reforms in many African countries also helped attract foreign investments to the region (UN 2005).

Of the total increase in FDI flows to Africa in 2003, two-thirds went to North Africa, in particular, to Libya, Morocco and Sudan. FDI-friendly policies in Morocco, the end of international sanctions on Libya and the emergence of Sudan as an oil exporter were the main factors behind this development. In Sub-Saharan Africa Angola, Equatorial Guinea, Nigeria and South Africa were the main recipients of FDI. Africa's prospects for FDI inflows are favourable in 2005 largely due to investments in nonrenewable natural resource exploitation, a buoyant global commodities market, improving investor perceptions about Africa and such international initiatives as the African Growth and Opportunity Act, Everything But Arms, the Cotonou Agreement with the European Union and the New Partnership for Africa's Development (NEPAD).

FDI in natural resource exploitation is still dominant in Africa, but in recent years it has begun to shift towards services. Services accounted for about 60 per cent of world FDI stock in 2002 compared with only 25 per cent in the early 1970s (UNCTAD 2004b). The factors behind this shift are the increasing tradability of services (that is, the ability

Box 1.2

Nature, costs and benefits of foreign direct investment in services

As global FDI flows are shifting towards services, the composition of FDI in services has changed over time. For instance, trade and finance dominated FDI in services until very recently. Service industries such as electricity, water, telecommunications and business services are now becoming more prominent.

UNCTAD (2004b) identified several costs and benefits of FDI in services:

- FDI in services, like any other FDI, is an external source of finance for a host economy. However, it may affect the balance of payments through external payments such as repatriated profits. Moreover, in the absence of appropriate government policies and regulations, involving transnational corporations in the delivery of utilities and other basic services may lead to a rise in prices, an inequitable distribution of services and limited access for the poorest segments of society.

- FDI in services can encourage domestic service providers to become more competitive through demonstration and skills diffusions, thus helping them improve efficiency. On the downside, it may crowd out domestic firms that lack financing capacity and experience in doing business.

- FDI in services transfers both hard technology (plant, equipment, industrial processes) and soft technology (knowledge, information, expertise, skills in organization, management, marketing).

- FDI in services generates employment in host countries, although less per dollar invested than FDI in manufacturing does.

- FDI in intermediate services can directly and indirectly improve the efficiency of industrial products.

FDI in services can help boost national and export competitiveness when favourable conditions prevail in the host country. If the conditions are not right, three kinds of risk arise: systemic risk, structural risk and contingent risk. Systemic risk occurs when the absence of efficient regulation exposes a host economy to significant economic instability. Structural risk happens when institutions are weak and state-owned monopolies may be converted into private ones. Contingent risk exists when FDI in socially or culturally sensitive areas causes unintended harm.

Source: *UNCTAD 2004b.*

to produce in one place and consume in another) and the gradual liberalization of service industries such as telecommunications, electricity and retail (box 1.2).

The shift is also driven partly by privatisation of infrastructure and reduced restrictions for foreign investors in these areas. Most African countries have opened their mobile telecommunications sector to foreign companies, and competition among several providers has reduced user costs while expanding service to the more remote areas in many African countries (as in Ghana and Tanzania).

Foreign participation has also been increasing in the electricity subsector, though foreign companies tend to prefer management contracts because they reduce risks. Electricity is one sector where South African enterprises are expanding to the rest of Sub-Saharan Africa. Improvements in telecommunications and electricity provision have also laid the foundation for the spread of call centres and data processing in several African countries.

Another sector where FDI has been increasing and where prospects for 2004–05 are strongest is the retail and wholesale sector. Here again a number of South African firms are investing not only in members of the Southern African Development Community but also beyond. Furthermore, prospects are perceived as good for the tourism as well as the hotels and restaurants sectors. The tsunami disaster at the end of 2004 and the weakening of tourism infrastructure in Asia may encourage African tourism.

Rising commodity prices

Call centres spread with improved telecommunications

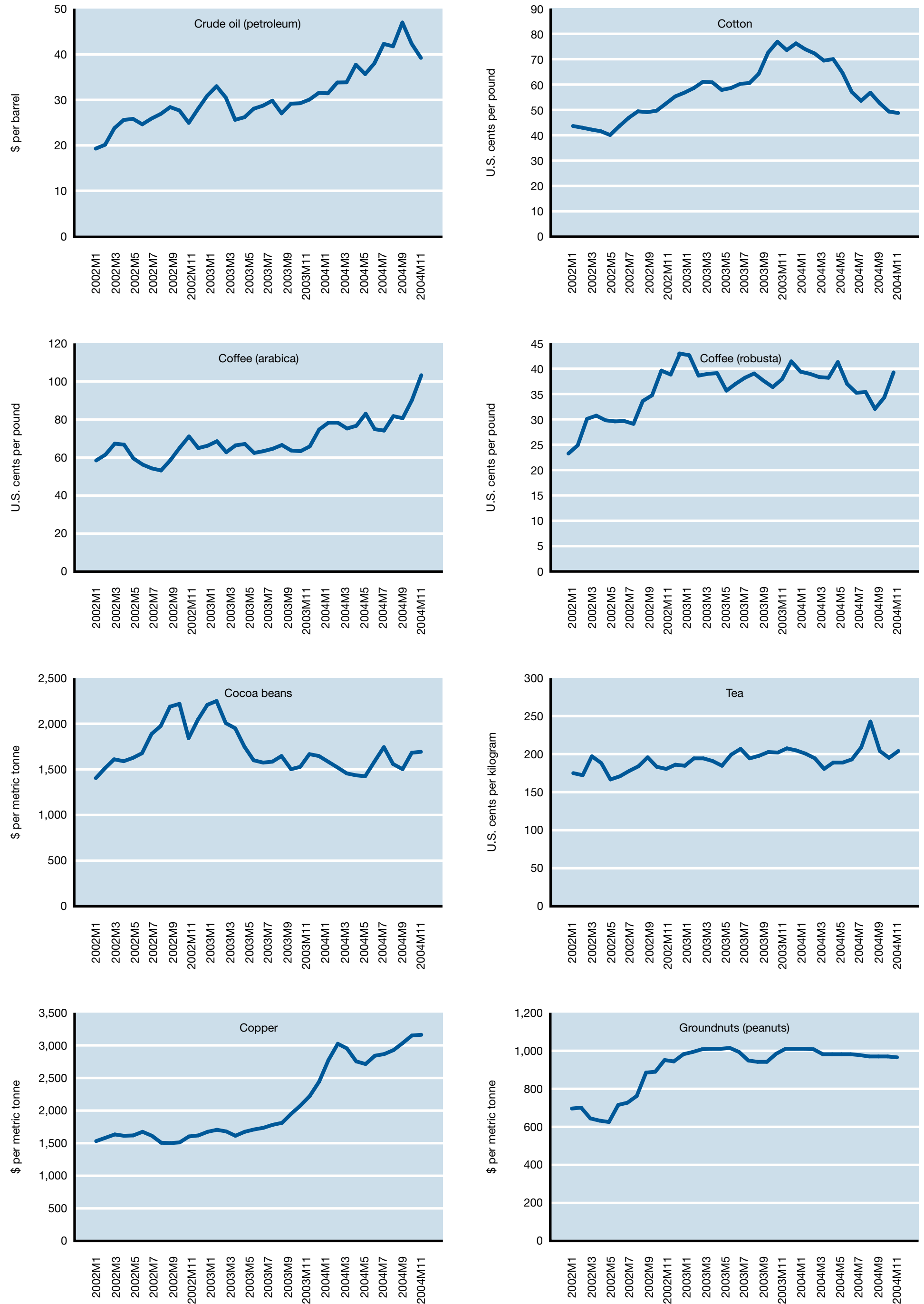
In 2004 Africa benefited from increases in oil and non-oil commodity prices, largely driven by strong demand from Asia. The commodity price index, denominated in U.S. dollars, went up 26.5 per cent in 2004, mostly thanks to a 31 per cent surge in the energy product price index. The nonenergy commodity price index went up more than 18.7 per cent from 2003, mostly due to the rise in the price indexes of metals and minerals (up 37.1 per cent) and fertilizers (up 19.2 per cent) from the previous year.

Of Africa's key nonoil export commodities, only cotton, cocoa, coffee (robusta) and groundnut oil recorded price declines in 2004. Good harvests of cocoa in West Africa, overproduction of coffee robusta in Latin America (Brazil and Colombia) and a good crop of groundnuts in Asia (India and China, in particular) drove down prices. However, the price of cocoa picked up later in the year, fuelled by fears that renewed political unrest in Côte d'Ivoire, the world biggest cocoa producer, could further disrupt supplies. The price of cotton dropped slightly, from 63.44 U.S. cents per pound in 2003 to 62.01 cents in 2004. The monthly price trend in 2004 was also clearly downward (figure 1.2). However, prices are expected to recover strongly in 2005 if WTO rulings lead to a significant reduction in U.S. cotton subsidies.

Crude oil: Between 2003 and 2004 the average spot price of crude oil increased 30.6 per cent to a decade high of $37.73 per barrel. Strong global demand, geopolitical tensions, limited spare production capacity and speculative activity were largely responsible for the oil price hike in 2004. Oil prices may fall slightly, but are expected to remain high in

Figure 1.2

Monthly prices of key African commodities, 2002–04



Source: *IMF 2005b.*

2005, thanks to expected growth in oil demand coupled with supply uncertainties and constraints.

Copper: Copper prices increased from $1,779 per metric ton in 2003 to $2,866 in 2004, contributing much to the rise in the metals and minerals subindex. The 61.1 per cent climb in the price of copper in 2004 was due to low stocks and increased demand from China, which as the world's biggest consumer of copper accounts for about a fifth of global consumption.

Gold: The price of gold climbed 12.6 per cent in 2004, from $363.50 per troy ounce in 2003. It was boosted by the continuing weakness of U.S. dollar, which made gold cheaper for foreign buyers. The rise in crude oil prices also increased investment demand for gold as a hedge against inflation.

Tea: Average tea prices increased 11.1 per cent from 2003 to $1.69 per kilogram in 2004, mostly thanks to low stock carried over from 2003

Coffee: Coffee arabica's 25 per cent price increase from 2003 levels contrasts with coffee robusta's price decline of 3 per cent. As a result, in 2004 the prices of coffee arabica reached $1.77 per kilogram and coffee robusta $0.79 .

Strong recovery in official development assistance to Africa

In 2003 net official development assistance (ODA) to Africa reached a record high of $26.3 billion, up from $21 billion in 2002 (figure 1.3). It exceeded high aid flows to Africa in the early 1990s, reversing the falling ODA trend since 1990. The strong performance in 2003 was driven largely by debt relief and emergency assistance: in particular, massive debt relief to the Democratic Republic of Congo and emergency aid from the United States to Ethiopia and Sudan. In fact, emergency aid to Africa sharply increased in the last two years. And the bilateral share of emergency aid jumped from less than 50 per cent in 1996 to almost 80 per cent in 2003.

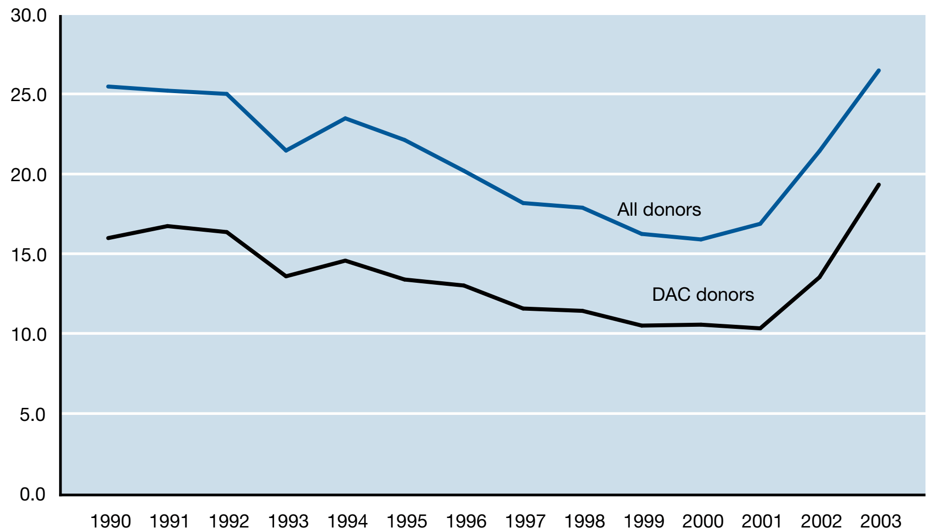
"Aid dependence varies across African countries"

About 73 per cent ($19.2 billion) of ODA in 2003 came from Development Assistance Committee (DAC) donors. Of the total ODA from DAC countries, more than 41 per cent came to Africa, showing the strong support from DAC donors.

While DAC donors as a group donates far below the pledged 0.7 per cent of GNI, four countries have exceeded this benchmark–Denmark spent 0.84 per cent of GNI on ODA in 2003, while Luxembourg (0.81 per cent), Netherlands (0.80 per cent) and Sweden (0.79 per cent) have also met the pledge. By 2006 ODA from DAC countries may increase from 0.25 per cent of GNI to about 0.30 per cent after delivery of commitments made at the International Conference on Financing for Development in Monterrey, Mexico, in 2002 and the G8 Summit in Kananaskis, Canada, in 2002.

Figure 1.3

Net ODA flows to Africa, 1990–2003 ($ billions)



Source: *OECD 2004-*

In Africa the recipients of the most aid from the DAC during 2001–03 were Egypt (an average of $1.17 billion a year), Mozambique ($0.96 billion), Tanzania ($0.91 billion), Democratic Republic of Congo ($0.63 billion) and Ethiopia ($0.57 billion). Most of these economies have been undergoing continuous economic reform.

Aid dependence, measured by total net ODA (excluding emergency aid and bilateral debt forgiveness) as a share of GNI, varies significantly across African countries. Of 49 African countries for which data are available, net ODA was more than 10 per cent of GNI for 17 countries in 2003. The top five aid-dependent economies in 2003 were São Tomé and Principe (51.8 per cent), Guinea-Bissau (27.5 per cent), Malawi (24.4 per cent), Sierra Leone (23.3 per cent) and Mozambique (21.8 per cent).

Better economic performance in Africa

Africa continued to perform strongly in 2004, with real GDP estimated to have grown at 4.6 per cent, thanks to external and internal factors. On the external front strong global recovery, higher commodity prices, higher oil production and prices, continued donor support in the form of aid and debt relief, growth in the tourism sector and rising FDI were contributing factors. The internal factors driving high growth were good macroeconomic management, better performance in agriculture across the continent, expansion in the industrial sector, particularly in construction and mining, and the improved political situation in many countries.

Table 1.2
Growth performance distribution in Africa, 2000–04 (number of countries)

Growth performance	2000	2002	2003	2004
Negative growth	2	5	7	2
Zero and positive growth	49	48	45	50
Low (0 per cent–3.9 per cent)	22	27	16	17
Medium (4 per cent–7 per cent)	20	16	24	27
High (more than 7 per cent)	7	5	5	6
Total number of countries	51	53	52	52

Source: *ECA, from official sources*

North Africa is estimated to have grown at 4.8 per cent in 2004, close to its growth level in 2003. Sub-Saharan Africa's growth improved to 4.5 per cent in 2004, up from the 3.9 per cent recorded in 2003. Both regions are projected to improve their performance in 2005-with North Africa expected to grow 5.2 per cent and Sub-Saharan Africa 4.8 per cent.

Only six countries realized 7 per cent or higher growth rate in 2004, required to meet the Millennium Development Goal of halving poverty by 2015: Chad (39.4 per cent), Equatorial Guinea (18.3 per cent), Liberia (15 per cent), Ethiopia (11.6 per cent), Angola (11.5 per cent) and Mozambique (8.3 per cent) (figure 1.4). Seventeen African countries registered positive but less than 4 per cent growth in 2004, while two countries, Zimbabwe (–6.8 per cent) and Seychelles (–2.0 per cent), contracted, albeit at a lower rate than in the preceding year (table 1.2). Zimbabwe has been contracting for the last five consecutive years. The poor performance in 2004 was attributed to droughts that hurt agricultural output, lack of coherent economic policy and the ongoing political crisis. Weak macroeconomic fundamentals were behind Seychelles' continued poor performance in 2004.

"The central challenge for Africa is achieving sustained growth"

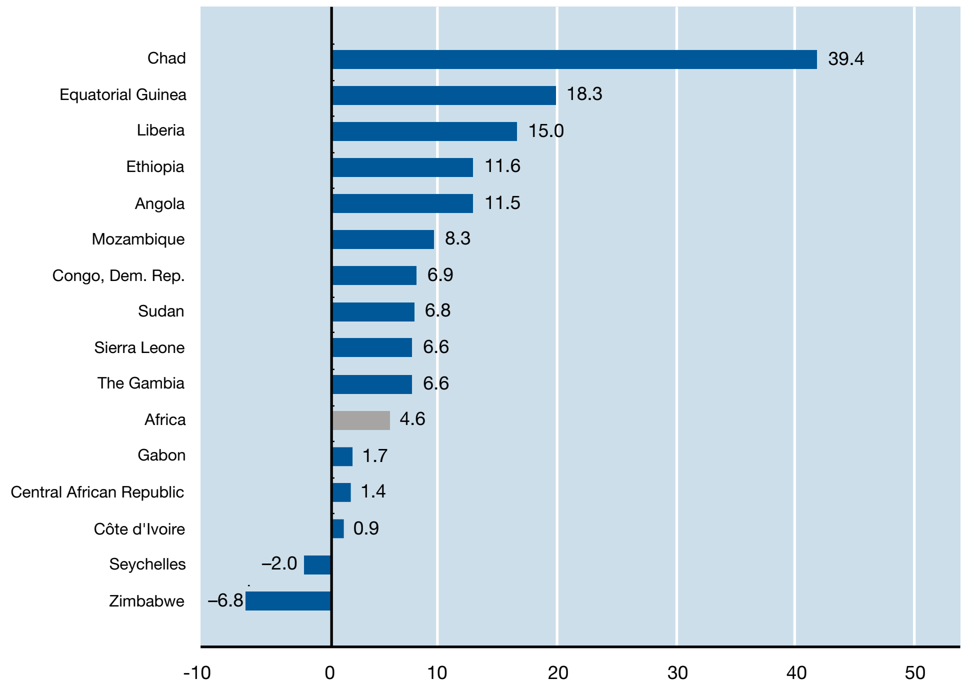
Of the six African countries that achieved 7 per cent or higher growth in 2004, only Chad, Equatorial Guinea and Mozambique have sustained growth of at least 7 per cent since 2001, and Angola since 2002.[1] The central challenge to Africa's economic performance is the ability to achieve sustained growth, attributed to some combination of adverse growth opportunities and inappropriate policy choices (Fosu and O'Connell 2005).

G5 performance mixed

The performance of the Group of Five (G5), the five biggest African economies, which account for close to 60 per cent of the region's output, was mixed. South Africa, the largest economy, accounting for a fifth of Africa's GDP, registered real GDP growth rate of 2.8 per cent in 2004, up from 2 per cent in 2003, thanks largely to high global demand, as well as strong domestic demand generated partly by the low interest rate environment. Egypt sustained its 3.2 per cent growth of 2003-a result of the expansionary fiscal stance and the growth in tourism, Egypt's most important industry, despite the bomb attacks on tourist facilities in Sinai.

Figure 1.4

Top 10 and bottom 5 performers in Africa, 2004 (per cent)



Source: *ECA, from official sources.*

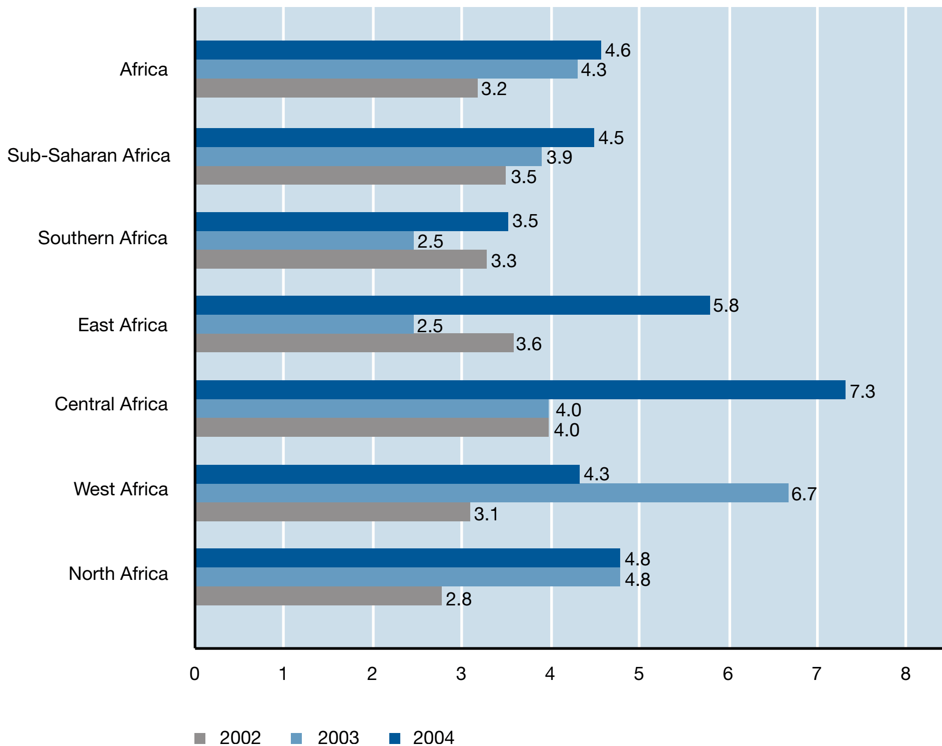
Continued gains from the oil sector's expansion sustained growth in North Africa at 4.8%

By contrast, Nigeria recorded 4.6 per cent growth, down from a high of 10.2 per cent in 2003, despite steady growth in the agricultural and services sectors. Similarly, growth in Algeria slowed from 6.9 per cent in 2003 to 6 per cent in 2004, despite continued high oil prices and production and fiscal expansion. Morocco's 4.2 per cent growth rate in 2004, down from 5 per cent in 2003, is attributed to the contraction in the textiles sector. The free trade agreement signed with the United States in July 2004 is expected to mobilize more investment, increasing the country's growth prospects in the near term.

Central Africa leads subregional performance

In 2004 Central Africa led the subregions with an average real GDP growth rate of 7.3 per cent, it was followed by East Africa (5.8 per cent) and North Africa (4.8 per cent). Southern Africa and West Africa lagged behind in 2004, with growth falling in West Africa as a consequence of a slowdown in the Nigerian economy, following a spectacular performance in 2003.

Figure 1.5
Real GDP growth, by African subregion, 2002–04 (per cent)



Source: *ECA, from official sources.*

North African growth fuelled by oil

Thanks to the continued gains from the oil sector's expansion in most of North Africa, growth remained firm at 4.8 per cent, close to that in 2003 (Figure 1.5). Growth picked up in Sudan (from 6.1 per cent in 2003 to 6.8 per cent in 2004, despite political instability), Libya (from 2.8 per cent to 4.5 per cent) and Tunisia (from 4.2 per cent to 5.6 per cent), though it slowed in Algeria (down from 6.9 per cent in 2003 to 6 per cent in 2004), Mauritania (from 4.5 per cent to 3.8 per cent) and Morocco (from 5 per cent to 4.2 per cent). A plague of locusts also seriously affected Mauritania's agricultural sector. Egypt maintained the 3.2 per cent output growth achieved in 2003.

Agriculture recovers in East Africa

In East Africa growth picked up sharply to 5.8 per cent in 2004 from 2.5 per cent in 2003, making it the second fastest growing subregion in 2004. Eight of the 13 countries in the subregion posted higher growth over 2003, led by Ethiopia (11.6 per cent), Democratic

Republic of Congo (6.9 per cent), Tanzania (6.1 per cent) and Madagascar (5.3 per cent). In addition to the robust recovery in the agricultural sector that helped Ethiopia and Tanzania, several other factors underpinned good growth performance, including strong donor support in Burundi, Democratic Republic of Congo, Ethiopia, Madagascar and Uganda, accelerated tourism activity, an increase in global and regional demand in Kenya and deeper policy reforms in the Democratic Republic of Congo. However, poor economic policies marred growth in Eritrea and Seychelles, while ongoing political instability affected Comoros.

High oil prices and production help Central Africa

Central Africa's leading growth performance of 7.3 per cent in 2004 was fuelled by exceptionally high oil prices supported by higher oil production in all oil-producing countries of the subregion except Gabon. Cameroon, which accounts for more than half the subregion's output, grew 4.7 per cent in 2004, compared with 4.2 per cent in 2003, mainly because of gains from high oil prices, sustained domestic demand and debt relief under the HIPC Initiative and other non-HIPC sources. Chad and Equatorial Guinea recorded the fastest growth in the continent in 2004. Though oil was the principal factor in Chad, cattle and cotton production also contributed to the impressive growth. Improved political stability coupled with donor support helped the recovery in the nonoil sector of the Republic of Congo. Growth in Gabon was slowed by a decline in oil production due to limited investment in upgrading existing fields.

"The cost of a civil war is estimated in reduced economic growth"

Sharp fall in growth in West Africa

In West Africa real GDP growth averaged 4.3 per cent in 2004, a sharp fall from 6.7 per cent in 2003. However, 6 of the 15 countries in the subregion grew at more than 5 per cent, with Liberia emerging from conflict leading the group with 15 per cent, followed by The Gambia (6.6 per cent), Sierra Leone (6.6 per cent), Burkina Faso (5.4 per cent), Cape Verde

Box 1.3

The economic cost of civil wars

The cost of a civil war can be estimated by the reduction in economic growth, increase in military expenditures, deterioration in health status and "conflict trap" effect for the country in war as well as its neighbours. The cost of the loss of GDP is estimated at 105 per cent of initial GDP for the country directly affected and 115 per cent for neighbouring countries. The additional military spending is equivalent to 18 per cent in the country directly affected and 12 per cent in neighbouring countries. Therefore, the loss of GDP and the extra military spending sum up to approximately 250 per cent of initial GDP of the affected countries. Civil wars have also important global effects, but they are more difficult to cost. These include HIV/AIDS, international terrorism and hard drug production. The benefits of reducing the incidence of civil wars should be felt globally.

***Source:** Collier and Hoeffler 2004.*

(5.4 per cent) and Ghana (5.3 per cent). Output growth slowed in Benin, Burkina Faso, Guinea, Senegal and Togo in 2004. Nigeria, which accounts for nearly half of subregional output, grew 4.6 per cent in 2004, down from the exceptionally high 10.2 per cent in 2003. Ongoing political crisis in Côte d'Ivoire led to yet another year of poor performance (0.9 per cent in 2004, up from a 2.3 per cent contraction in 2003) (box 1.3).

Ghana benefited from rising prices and production of gold and an increase in cocoa production. Though instability in Côte d'Ivoire continued to affect Burkina Faso, the increase in the cotton harvest improved agricultural sector performance there. The locust invasion seriously affected the agricultural sectors of Mali, Niger and Senegal. The end of conflict and the transition to peace coupled with donor support boosted growth in Liberia to 15 per cent in 2004, up from 4.5 per cent in 2003.

Southern Africa's growth is up

In Southern Africa real GDP growth picked up from 2.5 per cent in 2003 to 3.5 per cent in 2004, mainly due to steady growth in South Africa. Strong global demand and robust domestic demand created partly by the low interest rate environment contributed to the higher growth in South Africa. Growth in Angola, which emerged from conflict to become the second largest and the fastest growing economy in the subregion, was buoyant, 11.5 per cent in 2004—the result of high oil prices and output. While strong agricultural production helped the economies of Mauritius and Mozambique, relatively poor performance in Lesotho, Malawi, Swaziland, Zambia and Zimbabwe affected the overall economic performance of these countries in 2004. Growth in the service sector in Botswana and Mauritius helped expand output. The ongoing political crisis in Zimbabwe contributed to the contraction of the economy for the fifth consecutive year, though the rate of contraction slowed to 6.8 per cent in 2004 from 11.2 per cent in 2003. Growth remained strong in Mozambique (though the country experienced a slight easing from 8.6 per cent in 2003 to 8.3 per cent in 2004) due to recovery in agriculture and expansion in the industrial sector. As a result of uncertainties in the diamond-mining sector, Botswana's growth slowed significantly to 4.2 per cent in 2004, compared with 6.4 per cent in 2003.

Savings and investments remain low

The average rate of investment in Africa barely exceeded 20 per cent of GDP during 2000–02. Only 11 of 50 countries for which data are available experienced average investment rates above 25 per cent during 2000–02: Lesotho (42.7 per cent), Mozambique (40.8 per cent), Equatorial Guinea (39.3 per cent), Chad (37.9 per cent), Angola (34 per cent), São Tomé and Principe (32.6 per cent), Seychelles (32.5 per cent), Gabon (28.3 per cent), Mauritania (27.1 per cent), Tunisia (28 per cent) and Algeria (25.9 per cent). Most of these countries are oil producers, implying that countries with natural resources, especially oil, invest more compared with economies poorly endowed with natural resources. The other countries in the high investment category are those that underwent substantial policy reforms and as a result have improved the economic environment and investor perception.

The low level of investment in Africa is due partly to the low savings rate of the region (see chapter 7). On average, Africa had a savings rate of 21.1 per cent of GDP during 2000–02. Only 11 of the 50 countries registered savings rates above the average for the region: Equatorial Guinea (82.2 per cent), Republic of Congo (53.6 per cent), Angola (45.7 per cent), Gabon (42.4 per cent), Algeria (41 per cent), Botswana (39.5 per cent), Mauritius (25.3 per cent), Nigeria (25.1 per cent), Seychelles (25.2 per cent), Tunisia (24.9 per cent) and Mozambique (22.8 per cent).

Only three countries reported higher savings and investment rates (above 25 per cent) and high growth (real GDP growth rate 5 per cent or higher) during 2000–02: Angola, Equatorial Guinea and Tunisia—all of them oil exporters. Algeria, Gabon and Seychelles had both high savings and investment rates but growth rates of less than 5 per cent.

Sub-Saharan Africa saw increasing private investment combined with falling public sector investment. However, public investment remains high and important in many African countries. During 2000–02 gross public investment exceeded private investment in 12 African economies: Botswana, Burundi, Cape Verde, Central Africa Republic, Eritrea, Guinea-Bissau, Malawi, Niger, Nigeria, São Tomé and Principe, Sierra Leone and Zambia. In 2002, private investment exceeded 30 per cent of GDP in Chad, Lesotho and Mozambique, while it was less than 5 per cent in Burundi, Malawi, Sierra Leone, and Zambia.

Fiscal deficit down

Africa continued to consolidate fiscal positions, with the average fiscal deficit down from 1.5 per cent of GDP in 2003 to only 0.8 per cent in 2004. Strong oil revenues for oil producers largely contributed to this drop. Overall, fiscal surplus was achieved in 13 countries, 8 of them oil-producing economies: Equatorial Guinea (28.5 per cent), Gabon (8.2 per cent), Nigeria (6.7 per cent), Libya (6.3 per cent), the Republic of Congo (5.1 per cent), Algeria (3.3 per cent), Cameroon (1.9 per cent) and Sudan (0.5 per cent).

Table 1.3

Distribution of overall fiscal deficit in Africa, 2003 and 2004 (number of countries)

Range	2003	2004
Countries with a deficit	38	35
Less than 3 per cent	13	13
3 per cent–5 per cent	12	12
More than 5 per cent	13	10
Countries with a surplus	10	13
0 per cent–3 per cent	6	5
More than 3 per cent	4	8
Total number of countries	48	48

Source: *IMF 2004.*

Fiscal policy remains a challenge for many African countries. In 2004, 35 of 48 African countries for which data are available recorded an overall fiscal deficit, including grants, though 19 of them improve over 2003 levels (table 1.3). The deficit exceeded 5 per cent of GDP for 10 countries: São Tomé and Principe (–17.2 per cent), Guinea-Bissau (–14.7 per cent), Malawi (–12.7 per cent), Zimbabwe (–9.7 per cent), Egypt (–7.5 per cent), Swaziland (–6.6 per cent), Morocco (–5.9 per cent), Sierra Leone (–5.9 per cent), Mauritius (–5.5 per cent) and Angola (–5.4 per cent).

The major causes of the high fiscal deficits in 2004 were the increase in public spending in anticipation of oil revenues in São Tomé and Principe, the payment for salary arrears (since 2000) to public sector workers in Guinea-Bissau, the need to satisfy social demands for food security in Malawi and the preparation for the upcoming election in both Malawi and Zimbabwe. Moreover, lower corporate tax rates, poor budget management and expenditure decisions in Swaziland, pressure to increase spending to rehabilitate war-torn Sierra Leone, increased spending on the education and social sectors in Mauritius and increased spending on reconstruction and the social sectors in Angola contributed to high fiscal deficits in these economies.

In some countries, prudent macroeconomic management restrained inflationary pressures

Inflation–down to single digits

Despite the pressure from high oil prices, the inflation rate in Africa dropped to 8.4 per cent in 2004 from 10.3 per cent in 2003. Higher agricultural output coupled with prudent macroeconomic management in many African countries restrained inflationary pressures. Inflation fell in 29 of the 51 African countries for which data are available, while it increased in 20 countries. In Madagascar and Malawi it increased more than 10 percentage points, thanks to a poor maize harvest in Malawi and higher import costs in Madagascar brought about by the fall of the Malagasy franc against the euro and the U.S. dollar.

Twelve countries experienced double-digit inflation in 2004: Angola (56.1 per cent), Eritrea (21.5 per cent), Malawi (19.9 per cent), Zambia (18.5 per cent), Guinea (16.6 per cent), Nigeria (15.8 per cent), The Gambia (14.5 per cent), São Tomé and

Table 1.4
Distribution of inflation in Africa, 2000–04 (number of countries)

Range	2000	2001	2002	2003	2004
Less than 0 per cent	5	3	4	6	1
0 per cent–4.9 per cent	20	23	23	18	24
5 per cent–9.9 per cent	15	16	10	15	13
10 per cent–19.9 per cent	4	3	10	7	10
20 per cent–50 per cent	4	3	2	3	1
More than 50 per cent	3	3	2	2	2
Total number of countries	51	51	51	51	51

Source: ECA, from official sources.

Principe (13.3 per cent), Mozambique (12.9 per cent), Sierra Leone (12.4 per cent), Ghana (10.8 per cent) and Madagascar (10.5 per cent) (table 1.4). Zimbabwe has had triple-digit inflation since 2002; it declined by 82 percentage points from 2003 to 350 per cent in 2004 as a result of a modest recovery in food production. Chad was the only country that experienced deflation in 2004 because of the boost in agricultural production and the relatively tight monetary and fiscal policies imposed by the regional central bank.

The inflation rate for Africa is projected to drop further to 8.1 per cent in 2005. This trend may be reversed if the price of crude oil remains high.

Risk of currency appreciation

As a result of the continued weakening of the U.S. dollar, 30 African countries' currencies appreciated against the dollar in 2004. Gabon, with about 60 per cent of exports destined for the United States, and Lesotho, with 51 per cent of exports going to the United States, were most affected. The Liberian dollar showed the sharpest appreciation of all African currencies due to increased donor inflows, capital investment and remittances inflow, and the fall in capital flight as the country emerged from conflict. Higher gold and platinum prices, the weak U.S. dollar and attractive real interest rates were the main factors behind the South African rand's strong performance in 2004. Three Southern African countries' currencies pegged to the rand–the Namibian dollar, the loti of Lesotho and the lilangeni of Swaziland–showed rapid appreciation. The CFA franc, pegged to the euro, also gained against the U.S. dollar in 2004.

Twenty-one countries' currencies depreciated against the U.S. dollar. Zimbabwe, Madagascar, Comoros and Guinea had the fastest weakening against the U.S. dollar in 2004, thanks to the auction exchange rate in the face of the ongoing foreign exchange shortages in Zimbabwe, the continued high demand for imports and speculative activities by currency traders in Madagascar, the fall in official and private transfers coupled with weak performance of external and tourism sectors, poor perceptions of political stability in Comoros and the fall in international reserves in Guinea (owing mainly to weak export revenue).

Balance of payments developments

In 2004 trade performance improved in Africa. Exports continued to grow at high rates: 8 per cent in volume and 23.5 per cent in value. Oil-exporting countries boosted exports by expanding production capacity in gas and oil fields in response to high international prices. The increase in the prices of most nonoil commodities also improved several countries' export performance. Moreover, international initiatives such as the African Growth and Opportunity Act (AGOA) and Everything But Arms contributed substantially to the region's improvement in exports in 2004. For instance, the combined value of the 37 eligible AGOA countries' exports to the United States grew 38.1 per cent in 2004, up from $24.4 billion in 2003. However, the rules of origin conditions and time-bound preferential treatment attached to these preferential trading arrangements have limited their benefits (box 1.4).

Box 1.4
Tariff preferences are a double-edged sword for Ghana's tuna factories

All Sub-Saharan countries except South Africa have preferential access to the markets of Organisation for Economic Co-operation and Development (OECD) countries through such schemes as the Generalized System of Preferences, the Everything But Arms initiative of the European Union and the Cotonou Agreement or African Growth and Opportunity Act. In principle, these agreements allow Sub-Saharan countries to deliver nontraditional exports to OECD markets without paying tariffs to help them compete with Asian and Latin American exports, despite Sub-Saharan Africa's poorer infrastructure and productivity.

However, all of these preference schemes come with strings attached: rules of origin. To prevent third countries from passing their goods through countries that receive preferences, a minimum amount of processing of a product in the country with preference is necessary—otherwise the preferences would be meaningless. But the rules of origin for many products are very difficult to meet. If production requires inputs that are not domestically available, they usually need to be imported from the preference-giving region, where they are more expensive than in third countries. For example, fish exported to the European Union under the Cotonou Agreement must be caught with a vessel that is registered in an EU or African, Caribbean and Pacific country. In addition, the captain, officers and half the crew must be nationals of these countries.

For a Ghanaian tuna cannery that employs 1,000 mainly female workers these strict rules of origin pose serious threats. The company must prove that every single tin contains only fish caught according to the rules of origin in order to benefit from the 24 per cent preference margin. With Asian trawlers dominant on the coast, this is not easy. The costs for monitoring and documenting the processing of tuna from the trawler to the tin add considerably to production costs, and the uncertainty of the preferences created by the rules of origin reduces their value considerably.

Source: *ECA, from official sources.*

"Merchandise trade has shown considerable improvement"

Moreover, the textiles and clothing sector–a key labour-intensive growth-promoting sector in Africa–is facing a challenge from China's accession to the World Trade Organization (WTO). This comes at a trying time, given the negative impact of the phasing out of the Multi-Fibre Arrangement, which will limit the benefits of AGOA and Everything But Arms initiative (box 1.5).

Africa's increased imports in 2004 reflect an improvement in domestic incomes as well as higher oil and food prices. In many oil-exporting countries increased investment to expand productive capacities and develop infrastructure was the main factor behind import growth. Meanwhile, the adverse impact of the locust invasion and weather conditions in the Sahel led to a poor cereal harvest and increased imports of food staples in Burkina Faso, Chad, Mali, Mauritania, Niger and Sudan.

As a result of higher growth in the value of exports than of imports, Africa's trade surplus increased to $16.8 billion in 2004, up from $7.8 billion in 2003 (table 1.5). The breakdown

Box 1.5
Will the garment industry survive the Multi-Fibre Arrangement?

Until the end of 2004 trade in textiles and garments was restricted by the Multi-Fibre Arrangement and its predecessor, the Agreement on Textiles and Clothing, which allowed importing countries to impose limits on the volume of textiles and apparel mainly from the most competitive Asian suppliers, and China in particular. Together with tariff preferences under the Cotonou Agreement, and more recently AGOA, the arrangement enabled African countries such as Kenya, Lesotho and Madagascar to dramatically increase their garment exports.

Under AGOA African countries are exempt from the 10 per cent–20 per cent tariffs paid by most competitors. In 2004 the U.S. Congress decided that until 2007 cheaper fabrics from "third countries", even Mauritius, which was originally exempted, could be used by African producers. This is a significant advantage over the original rules of origin, which allow only textiles produced in Africa or the United States.

The end of the Multi-Fibre Arrangement poses a threat for African garment producers. An estimated $40 billion of textile and apparel production will be transferred to China from the developing world, which will result in China supplying half the world's market. Other beneficiaries will be India and Pakistan, producers of high quality linens. By combining low wages with the efficient use of modern equipment and management, these countries make competition difficult. In addition, it is much cheaper for big retailers to source their products from a limited number of countries, which further increases China and India's competitive advantage. In sum, prices for garments are expected to decline by about 20 per cent.

However, to prevent the flooding of EU and U.S. markets with Chinese textiles, special safeguard measures were agreed upon during negotiations for China's accession to the WTO. Restrictions can be re-imposed much more easily than normal WTO rules would allow. As a result, China has imposed a temporary export tax on clothing, with the intention of slowing down the relocation process, not changing it.

To compete in more liberal clothing markets, it is necessary for African producers to improve management practices in order to increase productivity. They could also try to occupy niche markets, for example, garments with African design, where size is less important. But the decline in prices has already led the government of Lesotho to exempt apparel and textile factory owners from paying a mandatory cost-of-living increase.

Source: *AllAfrica.com 2004; Marshall, Iritani and Dickerson 2005; EIU 2005.*

of the trade balance reveals that merchandise trade has shown considerable improvement, while services further deteriorated thanks to external debt payments and the cost of transport and financial services. In 2004 trade in goods reached $33 billion, up from $21.4 billion in 2003. By contrast, trade in services registered a deficit of $16.3 billion in 2004, compared with a $13.6 billion deficit in 2003.

Table 1.5

Africa's balance of payments, 2000–04 ($ billions)

	2000	2001	2002	2003	2004
Current account balance	6.3	–1.3	–6.7	–0.4	2.8
Trade	18.1	6.1	1.2	7.8	16.8
Goods	29.2	17.7	13.1	21.4	33.0
Services, net	–11.1	–11.6	–11.9	–13.6	–16.3
Income, net	–23.5	–20.2	–21.9	–26.0	–33.4
Current transfers, net	11.6	12.8	14.1	17.8	19.4
Capital account balance	1.9	2.8	2.4	2.7	3.0
Financial account balance	–7.3	–2.4	5.3	–3.9	–6.6
External financing, net	16.3	19.9	18.7	20.6	22.9
Non-debt-creating inflows	11.5	20.6	15.2	16.8	18.8
External borrowing, net	4.8	–0.7	3.5	3.8	4.1
From official creditors	0.4	–1.5	2.4	3.3	1.0
From banks	0.5	–0.2	1.0	0.7	1.0
From other private creditors	3.9	1.0	0.1	–0.3	2.1
Change in reserves[a]	–12.8	–12.3	–7.6	–20.0	–22.9

Note: *Values may not sum to totals due to rounding.*

a. *Negative sign indicates increase.*

Source: *IMF 2004.*

Africa's current account balance recorded a five-year surplus

The regional current account balance improved from a deficit of 0.1 per cent of GDP in 2003 to a surplus of 0.4 per cent in 2004 thanks to stronger performance in merchandise exports, mainly oil. However, the imbalance in services continued to put downward pressure on the current account balance. Twenty-six of 51 countries have improved over 2003. Except Algeria and Côte d'Ivoire, all oil-producing countries (including emerging oil exporters) improved their current account balance. Moreover, eight of the 14 countries that registered a current account surplus in 2004 were oil economies: Libya (21.3 per cent), Equatorial Guinea (18.3 per cent), Algeria (13.1 per cent), Gabon (11.6 per cent), Angola (9.2 per cent), Egypt (3.2 per cent), Nigeria (2.9 per cent) and the Republic of Congo (1.6 per cent).

The remaining six countries with a current account surplus in 2004 were Botswana (6.4 per cent), Namibia (5.5 per cent), Mauritius (2.6 per cent), Seychelles (1 per cent), Ghana (0.3 per cent) and Morocco (0.2 per cent). The main factors behind the surpluses were higher export earnings from diamond, copper and nickel in Botswana, diamond, zinc and uranium in Namibia, sugar and manufactured goods in Mauritius, canned tuna in Seychelles, and gold and cocoa in Ghana.

Of the 37 African countries that recorded current account deficits in 2004, only 7 had a deficit greater than 10 per cent of GDP (table 1.6): São Tomé and Principe (–59.9 per cent), Mauritania (–23.1 per cent), Chad (–18.3 per cent), Burundi (–15.1 per cent), Sierra Leone (–12.1 per cent), Zambia (–10.8 per cent) and Djibouti (–10.7 per cent).

The capital account balance for Africa recorded a surplus for the fifth year in a row, with a slight increase from $2.7 billion in 2003 to $3 billion in 2004, while the continued deficit in financial accounts worsened considerably: $6.6 billion in 2004 compared with $3.9 billion in 2003 (see table 1.5). Net external financing increased 11.2 per cent to

Table 1.6

Distribution of current account balance as a share of GDP, 2000–04 (number of countries)

Range	2000	2001	2002	2003	2004
Countries with a deficit	42	39	38	40	37
0 per cent–3 per cent	10	5	7	9	10
3.1 per cent–5 per cent	6	10	6	8	2
5.1 per cent–10 per cent	13	8	15	16	18
More than 10 per cent	13	16	10	7	7
Countries with a surplus	9	12	13	11	14
0 per cent–3 per cent	1	6	6	4	6
3.1 per cent–5 per cent	0	2	2	3	1
5.1 per cent–10 per cent	3	0	4	1	3
More than 10 per cent	5	4	1	3	4
Total number of countries	51	51	51	51	51

Source: *ECA, from official sources.*

$22.9 billion in 2004 from $20.6 billion in 2003 mainly because of a significant increase in non-debt-creating inflows. Net external borrowing increased marginally to $4.1 billion, up from $3.8 billion in 2003. And official reserves rose about 15 per cent in 2004, up from $20 billion in 2003.

Tourism picked up

Tourism is one of the main sources of foreign exchange earnings for many African countries, accounting for more than 2 per cent of GDP or 5 per cent of exports in 27 African countries (Christie and Crompton 2001). International tourist arrivals grew a spectacular 10 per cent worldwide in 2004 and 14 per cent in Africa–to 41.6 million, up from 36.5 million in 2003 (table 1.7). However, the region shared only 7.4 per cent of the global increase of 69 million tourists, and almost all the increase was concentrated in North Africa. Outside North Africa, South Africa and Tanzania led in terms of total earnings, while Tanzania, Benin, Ghana and Seychelles led in receipts per tourist.

Africa's earnings from the tourism sector were $18.6 billion in 2003 (the latest year for which data are available), an increase of 19.2 per cent over 2002. The region's receipt per tourist arrival was the lowest worldwide, $510 in 2003, less than half of the average for the United States ($1,029).

Table 1.7
Africa's benefits from tourism, 2000–04

	2000	2001	2002	2003	2004
International tourist arrivals (millions)	32.5	32.7	34.0	36.5	41.6
International tourism receipts ($ billions)	15.1	15.5	15.6	18.6	—
Receipts per arrival ($)	465	474	459	510	—
World market share (per cent)					
Tourist arrival	4.7	4.8	4.8	5.3	5.5
Tourism receipts	3.2	3.4	3.3	3.6	—

— not available.

Source: *WTO 2005.*

Most tourists to Africa come from European countries while the second most important source is the region itself. Travel for leisure and recreation purposes was particularly important, followed by visiting friends and relatives and visiting for health and religious purposes. Travelling for business and professional activities accounted for only 15 per cent of all travel purposes (WTO 2005).

Despite tourism's growing importance as a source of foreign exchange earnings for Africa, the industry remains undeveloped mostly because of political and social instability, combined with poor tourism infrastructure (or weak capacity for accommodation). Moreover, inadequate information and marketing (measured by Internet use) and high health risk (such as malaria) are also serious deterrents to tourism's growth (Naude and Saayman 2004).

"In 2004, under HIPC, 12 African countries qualified for debt relief"

Still many challenges to the HIPC Initiative

The HIPC Initiative may have provided greater scope for increased social spending without necessarily compromising the fiscal position of eligible African countries, but several challenges remain. By the end of 2004, 12 African countries had reached the HIPC completion point, qualifying them for debt relief (table 1.8). Another 11 countries reached the decision point, qualifying them for interim debt relief. In 2004 alone five African countries reached the completion point of the enhanced HIPC Initiative: Ethiopia, Madagascar, Niger, Ghana and Senegal. While no country reached the HIPC decision point in 2004, Burundi and the Republic of Congo are expected to reach the decision point in 2005.

Regardless of the progress made so far, the HIPC Initiative faces many challenges:

- ***Slow pace.*** The pace of implementation of both the original initiative and the enhanced framework has been slow.

- ***Difficulty maintaining longer term debt sustainability.*** The beneficiaries of the HIPC Initiative are unlikely to achieve debt sustainability in the long term after reaching the completion point.

- ***Deficiencies in the methodology.*** The initiative has been criticized for arbitrary choice of discount rate to calculate the net present value of debt, the narrowness of the eligibility criteria, the use of unrealistic debt sustainability criteria and the exclusion of domestic debt in determining debt sustainability thresholds.

- ***Problem remaining on track after reaching the decision point.*** HIPCs are getting off track with economic reforms and poverty reduction programmes during the interim period, causing delays in reaching the completion point.

Table 1.8

Commitments and disbursements of HIPC assistance, as of February 10, 2005

Country	Decision point	Completion point	Amount committed (millions of special drawing rights)	Amount disbursed (millions of special drawing rights)
Benin	July 2000	March 2003	18.4	20.1
Burkina Faso	July 2000	April 2002	27.7	29.7
Ethiopia	November 2001	April 2004	26.9	28.1
Ghana	February 2002	July 2004	90.1	94.3
Madagascar	December 2000	October 2004	14.7	16.4
Mali	September 2000	March 2003	34.7	38.5
Mauritania	February 2000	June 2002	34.8	38.4
Mozambique	April 2000	September 2001	13.7	14.8
Niger	December 2000	April 2004	21.6	24.1
Senegal	June 2000	April 2004	33.8	38.4
Tanzania	April 2000	November 2001	89.0	96.4
Uganda	February 2000	May 2000	68.1	70.2
Cameroon	October 2000	Floating	28.5	5.5
Chad	May 2001	Floating	14.3	7.2
Congo, Dem. Rep.	July 2003	Floating	228.3	2.3
The Gambia	December 2000	Floating	1.8	0.1
Guinea	December 2000	Floating	24.2	5.2
Guinea-Bissau	December 2000	Floating	9.2	0.5
Malawi	December 2000	Floating	23.1	6.9
Rwanda	December 2000	Floating	33.8	14.4
São Tomé & Principe	December 2000	Floating	—	—
Sierra Leone	March 2002	Floating	98.5	62.0
Zambia	December 2000	Floating	468.8	351.6
Total enhanced HIPC			1,385.6	945.0

— indicates lack of information

Source: *IMF 2005a.*

- ***Insufficient interim relief.*** Although provision of interim debt relief has improved under the enhanced HIPC Initiative compared with the original initiative, the amount of assistance seems insufficient to meet poverty reduction needs.

- ***Financing problems.*** Financing the total cost of the initiative has been problematic because resources for such purposes have yet to be secured. This problem is likely to be aggravated if estimates of funding requirements are included for post-conflict countries that have not yet reached the decision point and for which there are no current estimates of the cost.

- ***Lack of full creditor participation.*** Although the initiative has witnessed a marked increase in the number of participating creditors, not all creditors are participating as much as expected—nor have they indicated their willingness to do so.

- ***Doubtful "additionality"***. Ensuring that HIPC debt relief supplements existing aid is unlikely, despite the fact that some recent trends in aid flows indicate some aid reallocations towards eligible HIPCs.

- ***Many countries are at pre-decision point.*** Several other equally poor African countries have been left out of the process mainly because of internal conflict. Almost all African countries at the pre-decision point are affected by conflict, are still in conflict or are just emerging from conflict. Also, lack of political consensus on such issues as revenue sharing, lack of effective implementation of economic and financial policies and the existence of protracted arrears have prevented some countries from reaching their decision points.

Medium-term outlook

Africa is projected to grow 5 per cent in 2005, driven by the upturn in growth prospects of 32 of the 52 countries for which data are available (including the largest five economies, except Nigeria).[2] Continued good macroeconomic fundamentals, increased agricultural output aided by continued good weather conditions and growth in services, tourism and mining are projected to drive this growth. On the downside, however, the projected slowdown in growth in China, the United States and European Union is likely to weaken global demand, with negative consequences, particularly for non-oil-producing African countries.

"In North Africa, real GDP growth should pick-up to 5.2%"

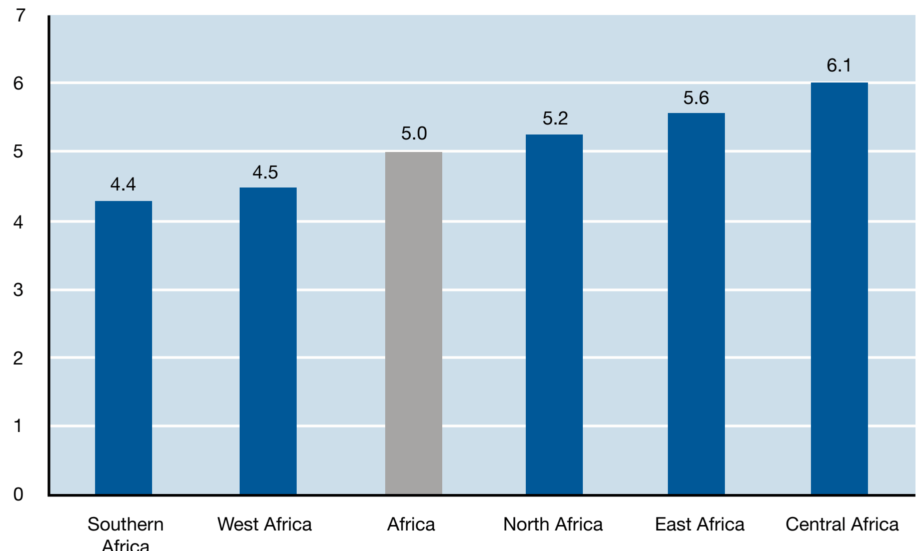
Prospects for G5 economies in 2005 are expected to improve in general. Algeria is projected to lead with real GDP growth of 6.6 per cent, followed by Morocco (4.4 per cent). Tax cuts in Egypt are expected to boost private consumption and stimulate investment. South Africa is projected to grow 3.4 per cent in 2005, mainly because of strong domestic demand due to tax relief measures, growth in tourism and increased foreign investment.

Economic performance set to improve in North Africa, West Africa and Southern Africa

Prospects for North Africa are good, with real GDP growth projected to pick up to 5.2 per cent, led by growth in the agricultural sector, assuming good weather conditions and continued gains from oil (figure 1.6). Tax cuts in Egypt are expected to boost private consumption and investment; strong growth in tourism in Morocco and Tunisia, more foreign investment inflows to oil-related activity in Libya, Mauritania and Sudan (if peace is secured) and strong growth in services in Mauritania and Tunisia are other factors behind the positive outlook for North Africa. Aided by the expanded capacity in the oil sector and improvement in the political situation, Sudan is projected to grow 8 per cent in 2005, followed by Algeria (6.6 per cent), Mauritania (5.4 per cent) and Tunisia (5.1 per cent).

Growth in East Africa is expected to remain strong in 2005, notwithstanding a slight decline to 5.6 per cent. Good harvests in Burundi, Ethiopia, Kenya, Madagascar, Tanzania and Uganda are anticipated to drive growth in 2005. Almost all countries of the subregion are expected to receive increased donor support. Strong growth in the tourism industry is anticipated to benefit Kenya, Seychelles and Tanzania. Other factors contributing to growth include increased FDI flows to Madagascar and Uganda; good macroeconomic management in Uganda (in addition to strong export sector performance), Democratic Republic of Congo and Tanzania; and improved political stability in Burundi and Comoros.

Figure 1.6
Projected real GDP growth by African region, 2005 (per cent)



Source: *ECA, from official sources.*

In Central Africa the oil sector will continue to dominate growth prospects in 2005. GDP growth is projected to slow to 6.1 per cent in 2005, largely due to a sharp drop in Chad's growth rate, from 39.4 per cent in 2004 to only 13 per cent in 2005. This is because construction activities related to the Chad–Cameroon oil pipeline are winding down. Cameroon's growth is expected to remain unchanged from its level in 2004. A further decline in oil production in Gabon is projected to slow growth to 0.8 per cent in 2005. Robust expansion in nonenergy sectors is expected to strengthen growth outlook in the Republic of Congo and São Tomé and Principe.

West Africa is projected to grow 4.5 per cent in 2005, with 8 of the 15 countries expected to record improvements over 2004: Benin, Burkina Faso, Cape Verde, Côte d'Ivoire, Guinea, Guinea-Bissau, Mali and Senegal. Liberia is again projected to lead subregional performance with a growth rate of 15 per cent. Factors behind this growth include agricultural growth in Benin, The Gambia, Guinea, Mali, Senegal, Sierra Leone and Togo; donor support for Guinea-Bissau, Liberia and Sierra Leone; expansion in mining in Burkina Faso, Guinea, Ghana, Mali and Sierra Leone; foreign investment inflows to Cape Verde and Liberia (in response to anticipated improvement in political stability); and growth in tourism in Cape Verde and The Gambia.

Southern Africa is projected to expand at a much faster 4.4 per cent in 2005. Growth is expected to reach 3.4 per cent in South Africa in 2005 thanks to anticipated strong global demand for its output, growth in tourism, increase in FDI inflows and expansion in domestic demand in response to new tax relief measures and low interest rate environment. Developments in the oil sector will continue to influence Angola's economy in 2005. Growth in services in Botswana, Mauritius and Namibia, an increase in mining activities in Botswana, Mozambique, Namibia and Zambia, agricultural expansion in Mauritius, Mozambique and Zambia, increased tourist activity in Mauritius and Zambia and donor support in Zambia will be the main factors behind the expansion of the subregion in 2005. However, Zimbabwe's economy is projected to contract in 2005 (though the contraction will sink to 1.6 per cent in 2005), due to the ongoing political crisis and weak performance in both agriculture and manufacturing.

"High oil prices pose another risk to the regional outlook"

There are several downside risks to the continent in 2005. The continued momentum in the global economy is marred by significant international imbalances, in terms of the large current account deficit in the United States and the matching surpluses concentrated in a few EU countries. A sharp depreciation of the U.S. dollar continues to be a possibility and could lead to a drastic decline in consumption, import demand and foreign investment in the United States, which could affect the pace of the global economy. Uncertainty in the direction of oil prices, already at a historically high level, poses another risk to the regional outlook. In addition, ongoing political instability in Sudan and Côte d'Ivoire may affect neighbouring countries.

Implications for employment creation and poverty reduction

The rosy picture depicted by the trends in the preceding analysis can be misleading. Limiting the analysis to the macroeconomic dimension of growth omits information on the effect of growth on employment creation and poverty reduction. Ideally, growth should reduce the

pervasive extent of poverty in Africa. This report argues that employment-creating growth is the best way out of poverty (see chapters 2 and 3). Unemployment and poverty remain high in Africa despite the relatively high levels of economic growth. However, the recovery in economic growth in several African countries has not translated into higher income and employment for poor people. One of the reasons is that growth has been achieved through capital-intensive technologies and sectors.

Three of the four countries that sustained growth of 7 per cent or more since 2001 or 2002 are oil producers and hence, growth of these economies is driven largely by the oil sector. In general, oil-exporting African countries grew faster than nonoil exporters in 2003 and 2004. However, because the oil sector is highly capital intensive, its direct contribution to poverty reduction through employment generation is quite limited. Therefore, sustained high growth by itself may not translate into meaningful poverty reduction in these countries. This argument is also supported by the declining trend in Sub-Saharan Africa's employment growth rate during 1998–2004 at a time when real GDP growth was rising (see chapter

Box 1.6

Does strong growth in Tanzania help to achieve poverty reduction goals?

Tanzania averaged economic growth of about 5 per cent during 1996–2003, thanks to market-oriented economic reforms that began in the early 1990s and intensified in 1996, as well as macroeconomic stabilization policies. These in turn triggered large inflows of official assistance—in a virtuous cycle—that further supported growth and the continuation of reform efforts. Key reforms focused on:

- Large-scale privatization. Almost all state-owned enterprises have been privatized since 1992.
- Liberalization. Current account transactions, the exchange market, agricultural prices and marketing boards have been gradually liberalized.
- Macroeconomic stabilization. Inflation was brought down from as high as 25 per cent in 1992 to single-digit levels in 1999 and further declined to below 5 per cent in 2002 as a result of prudent fiscal and monetary policies.

How did this growth translate into poverty reduction? So far, overall poverty shows a modest decline. There is a marked difference between rural and urban performance. An analysis of the incidence of poverty from 1990 through 2000 shows that declining GDP per capita in the early 1990s led to a steep rise in poverty, while the country's improved growth trajectory in more recent years has steadily reduced poverty in urban centres. In Dar es Salaam poverty was rising during 1990–2000 and falling in recent years. However, in rural areas there has been no effect of growth on poverty. Given the weight of the rural sector in the Tanzanian economy, there has been no overall positive effect of growth on poverty in the country.

Source*: Treichel 2005*

2). Tanzania illustrates this disconnect between economic growth and poverty reduction (box 1.6). Chapters 2 and 3 discuss in more detail why growth in Africa has not resulted in lower levels of poverty.

In conclusion, recent improvements in macroeconomic conditions in Africa need to be translated into employment and poverty reduction among African households, which is necessary for the long-run sustainability of macroeconomic and social stability in Africa.

Endnotes

1 Fourteen African countries-most of them nonoil producers-have been able to sustain average growth rates of at least 5 per cent since 2000: Angola, Botswana, Burkina Faso, Chad, Equatorial Guinea, Ethiopia, Liberia, Mauritius, Mozambique, Rwanda, Senegal, Sudan, Tanzania and Uganda.

2 The medium-term prospects for Africa are based on the information obtained from official sources, Sub-Regional Offices of UNECA, the United Nations Department of Economic and Social Affairs, the Economist Intelligence Unit and the International Monetary Fund.

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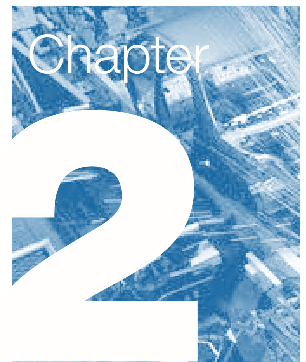


Ensuring decent employment for Africa's poor: key challenges

Interest in Africa's employment challenge is not new. On several occasions over the past three decades African governments have identified employment creation as the key to the fight against poverty.[1] Despite political agreement on the centrality of employment creation in African countries' development strategies, the employment content in Poverty Reduction Strategy Papers (PRSPs) remains weak. Because employment issues have not received the priority they deserve, detailed and reliable labour data are difficult to find for Africa. This could explain the rarity of systematic analyses of African labour markets. By devoting *Economic Report on Africa 2005* to this topic, the United Nations Economic Commission for Africa (UNECA) has acknowledged the need for a thorough analysis of employment issues to inform poverty reduction policies implemented in African countries.

> *In Africa, rates of unemployment are among the highest in the world*

Understanding employment issues is particularly important in Africa, where the rates of unemployment are among the highest in the world: 10.9 per cent in Sub-Saharan Africa and 10.4 per cent in North Africa in 2003, the second and third highest in the world. However, these official figures do not fully reflect the extent of unemployment in Africa.

- Working poverty is very high, with 56 per cent of people employed in Sub-Saharan Africa not earning enough to provide for their families' basic needs.
- The number of discouraged workers is large.
- Unemployment is unevenly distributed across age and gender groups. The youth unemployment rate in Africa is twice the total unemployment rate. Generally underestimated, female unemployment rates are higher than male unemployment rates in North Africa but lower in Sub-Saharan Africa.
- Variations in regional and country unemployment rates are large. Western Africa had the lowest unemployment rate in 2003 (6.7 per cent), while Southern Africa the highest rate (31.6 per cent). Uganda had an unemployment rate of 7 per cent in 1997 and Lesotho 39 per cent. Even in the same country there are disparities, with the rural-urban split often the most visible.

How can Africa's labour markets create more and better paid jobs to reduce poverty? Why has the formal sector failed to create more and better paid jobs? And why has the informal sector failed to increase productivity and earnings? Nine answers:

- ***Slow employment-generating growth.*** Despite some recovery in Africa's growth rates, poverty has not decreased for two reasons. The 4–5 per cent economic

growth rates may appear high by international standards, but they are not high enough to have a noticeable impact on the level of poverty, especially in relation to population growth. Using the benchmark of a minimum yearly average of 7 per cent growth rate to cut poverty by half by 2015, the current rates in Africa are well below what they should be. So far, growth appears to have been fuelled by capital-intensive industries rather than labour-intensive ones. Particularly in the last two years, growth has been largely influenced by oil exports, which in many African countries are highly capital-intensive.

- ***No structural economic transformation.*** African economies are still dominated by a low productivity agricultural sector. Low productivity and earnings account for the lack of structural economic transformation and diversification into higher productivity sectors, within agriculture or in the industrial and services sectors.

- ***High demographic pressure.*** The lack of demographic transition in Africa results in high demographic growth, exacerbating youth unemployment. The labour force has grown at 2.3 per cent a year in North Africa and 2.9 per cent a year in Sub-Saharan Africa, putting intense pressure on the labour market. Sub-Saharan African countries need to create 8 million new jobs each year to absorb the ever-increasing number of job seekers. This is a tall challenge in view of the continent's relatively slow economic growth.

- ***Inappropriate education and training policies.*** Inappropriate education and training policies result in both skills mismatch and low skill supply. Africa's functional literacy, defined as the ability to read and write in one's mother tongue or a foreign language, is low relative to other developing regions. In 2000 North Africa's 58.6 per cent literacy rate and Sub-Saharan Africa's 61.2 per cent literacy rate were the second and third lowest–and well below the world average of 79.1 per cent. However, there are signs of improvement: in 2000 youth literacy in Sub-Saharan Africa was 16.3 per cent higher than adult literacy. But there is also a mismatch between the skills offered and those required by th°e job market, due mainly to an education and training system tailored to suit the needs of the civil service because few graduates are employed in the private sector. Unfortunately, private sector expansion in many African countries has not yet been accompanied by appropriate changes in curricula to emphasize vocational training for practical and marketable skills.

- ***Failed labour regulations.*** With respect to labour policies, a balance is needed between job protection to ensure the welfare of employees and labour flexibility to cope with the effects of economic shocks—and the right balance is often difficult to find. For instance, minimum wages should be set high enough to minimize the number of working poor but not so high that they severely affect firm profitability and reduce employment. In Africa labour policies are neither sufficiently flexible to encourage employment creation nor effective for worker protection and equity. While the average effect of these policies on employment and job protection is small due to limited coverage and enforceability, the marginal impact could be large if they prevented potential investors from investing or forced them to go into

the informal sector. This is the case when labour policies are generally perceived as increasing transaction costs.

- ***No enabling environment for investment.*** Investment in the private sector is still too low to result in sizable job creation, despite progress towards restructuring African economies. Macroeconomic volatility, political uncertainty, the lack of access to affordable credit and high transaction costs have been major impediments to investment. Consequently, Africa has the lowest investment rate of all developing regions—just 20 per cent of the foreign direct investment flows to Latin America and 9 per cent of the flows to Asia and the Pacific.

- ***Stiff competition facing firms in export markets.*** Coupled with low investment, the share of firms producing for the export market is small. The failure of African firms to significantly increase their exports is a key factor explaining why they remain small. As economic globalization intensifies, African firms will have more and more difficulty competing in the global market. At the same time, however, globalization has opened windows of opportunity to competitive firms, as developed countries delocalize their activities to low-cost economies in the developing world.

- ***Economic choices motivated by politics.*** Politics also shapes African economies, but economic choices guided by political considerations may result in inefficiencies and political instability. Distributive politics in Africa have often led to imbalances in resource allocation, especially for public goods. For instance, unequal distribution of land, the key asset supporting employment in agrarian economies, has increased unemployment and inequality. In some countries social imbalances have resulted in civil unrest, which in turn has destroyed these countries' economies.

- ***High HIV/AIDS prevalence and brain drain.*** The rate at which the prevalence of HIV/AIDS and brain drain are destroying human capital in Africa is unprecedented. Sub-Saharan Africa accounts for 75 per cent of global AIDS deaths, and the people affected are among the population's most productive workers. For example, schools, hospitals, the civil service and the mining and construction sectors are losing a large number of their personnel due to AIDS and its related infections. Additionally, human capital flight is an important concern for African economies. Brain drain reduces the supply of skilled and professional workers, which reduces employment opportunities for semiskilled and unskilled labour given the complementarity between skilled and unskilled labour in the production process. Moreover, the workers leaving Africa are usually young and highly educated, so the continent loses its most creative force. This loss hampers the creation of a more dynamic private sector, confining most work opportunities to the civil service.

“Low-productivity agriculture dominates Africa's economies”

Later chapters analyse in more detail these key issues to provide appropriate policy recommendations.

Employment-generating growth for poverty reduction

Africa and the transition economies are the only regions where poverty has been rising in the recent past (see chapter 3). So the consensus now is that eliminating poverty is the overriding objective of development in Africa. But the question is how. Most analysts argue that poverty reduction in Africa will result from a combination of sustained high levels of economic growth and drastic reductions in inequality to allow poor people to benefit from and contribute to the growth process (World Bank 2000).

> Poverty is concentrated in rural areas

The most direct and arguably most important channel through which growth will reduce poverty in Africa is employment. For a given level of technology, labour and capital are two key inputs required in the production process. An increase in aggregate demand increases the demand for labour and capital–and vice versa. During periods of economic decline firms tend to reduce their labour force, and during periods of economic growth they tend to increase their hiring. It is generally accepted that employment income is the main source of revenue for poor people.[2] Whether members of the household in Africa are wage earners or self-employed, they earn a living from the fruit of their labour, given the limited number of alternative assets they could depend on. This is particularly the case in rural areas in Africa, where poverty is concentrated. In other words, the observed unemployment, underemployment and low returns to labour in Africa can be considered as immediate causes of poverty. In this context, policies encouraging growth and employment are expected to be "essential for any poverty reduction strategy" (World Bank 2000, p. 99). This view is supported by cross-country empirical evidence showing that expanding remunerative employment reduces the incidence of poverty (Islam 2004).

That Africa's growth recovery has not been associated with poverty reduction may be explained by the fact that the growth rates have not been large enough (Soludo and Kim 2003). Moreover, the source of most of the growth in Africa in recent years has been from capital-intensive sectors rather than labour-intensive ones.

The scope of the impact on poverty of growth through employment goes beyond the income dimension of poverty. Employment-intensive growth increases the consumption potential of the population, especially food consumption, reducing malnutrition, which is particularly rampant in poor rural communities. Moreover, the additional resources generated by growth can be used to improve the accessibility of basic services essential for a decent living, such as education and health. There are several non-income aspects of poverty, particularly those related to the capabilities of poor people, who require specific measures; economic growth can, at best, act as a catalyst. For instance, the "human capital" dimension of poverty can be addressed by enhancing the employability of poor people through better nutrition, health, training and education. Where low human capital is due to unequal distribution of resources within a society, greater equity is the solution. Meanwhile, improving governance can contribute to alleviating exclusion, marginalisation and insecurity of poor people. Special targeting policies are also required in certain cases. For example, the gender dimension of poverty may be addressed by targeting employment opportunities towards women. Similarly, the spatial aspect of poverty is best tackled by targeting marginalised areas.

Labour markets in Africa: facts and figures

Africa's employment problem is severe and multidimensional. Unemployment, underemployment, informal employment and working poverty are high compared with other regions (see box 2.1 for definitions of these terms). Furthermore, these patterns display wide variations across countries and regions. Even within the same country there are splits between rural and urban groups, youth and adult, and male and female groups. These aspects are discussed in detail to provide a comparative picture of African labour markets relative to the rest of the world. The formal-informal split represents the most important distinctive feature of labour markets in Africa. The key issue in the formal sector is unemployment, whereas the main problem in the informal sector is the increase in income through, among other things, higher productivity. This is discussed later in this section.

Improving governance can contribute to alleviating exclusion

Unemployment in Africa remains high—and unevenly distributed

In 2003 the average rate of unemployment was 10.9 per cent in Sub-Saharan Africa and 10.4 per cent in North Africa (ILO 2004a). These rates are high compared with other developing regions. Sub-Saharan Africa and North Africa have the second and third highest unemployment rates after the Middle East. Regional trends show that African unemployment has not improved over the last 10 years—in fact, unlike most regions the rate has remained stable around 10 per cent (figure 2.1). In 1999 unemployment in South America was slightly higher than in Sub-Saharan Africa, but it has since declined. Unemployment has also declined slightly in the Middle East and North Africa, but it is still higher than in Sub-Saharan Africa.

Box 2.1
Key terms

Unemployment
Unemployed people are working-age people without work, seeking work in a recent past period and currently available for work. In other words, individuals age 15 or older are counted as unemployed if they are actively looking for work but not finding any. This means that they are neither discouraged nor voluntarily staying in education and training. The unemployment rate is calculated as the number of unemployed people (for an economy or a specific group of workers) divided by the total number of people in the labour force.

Discouraged workers
Discouraged workers are working-age people who are not currently looking for work but may have looked for it in the past and clearly desire a job "now". Even though they want to work, these people do not actively seek work because they view job opportunities as limited, because they have restricted labour mobility or because they face discrimination or structural, social or cultural barriers.

Box 2.1 *(continued)*

Youth unemployment

The four measurements of youth unemployment are the youth unemployment rate (youth unemployment as a share of the youth labour force), the ratio of the youth unemployment rate to the adult unemployment rate, youth unemployment as a share of total unemployment and youth unemployment as a share of the total youth population.

Employment

The employment-to-population ratio is defined as the share of an economy's working-age population that is employed. As an indicator, the employment-to-population ratio provides information on the ability of an economy to create jobs. Although a high overall ratio is typically considered "good", the indicator alone does not provide information on labour market problems such as low earnings, underemployment, poor working conditions or the existence of a large informal economy.

Decent employment

Decent employment is an integrative concept that refers to both quality and quantity of labour. Decent employment should be productive and secure work, ensure respect of labour rights, provide an adequate income, offer social protection and include social dialogue, union freedom, collective bargaining and participation.

Time-related underemployment

Time-related underemployed people include all workers, who, during a short reference period, were willing to work additional hours, available to work additional hours and had worked less than a threshold relating to working time.

Working poverty

Working poor refers to people whose income from work is below the poverty line. These people usually do not benefit from the other items that define decent work, such as social protection or representation rights (voice).

Informal sector

The labour market in developing countries may be clustered in four sectors: formal urban, informal urban, formal rural and informal rural. The informal rural sector consists mainly of small operations involving self-employed persons and unpaid family members, most of whom are unskilled. The informal urban sector is characterized by self-employed individuals and privately owned enterprises producing mainly services or other nontradables. This sector is generally unregulated, wages and job security are low, and fringe benefits such as health insurance, life insurance or pension are usually nonexistent. Union activity is rare, legal minimum wages do not apply, and wages are flexible.

Source: *ILO 2005a; Fosu 2002.*

Although high compared with other regions, the unemployment rate in African might seem unrealistically low. First, the collection of employment data in Africa is fraught with difficulty. Many countries do not report information, reporting countries give incomplete data, and not all the reported information is comparable across countries (box 2.2).[3]

Box 2.2

Comparability problem

Labour market indicators may not be comparable across economies for several reasons:

- *Conceptual variation.* National statistical offices, even when using International Labour Organization conceptual guidelines, do not measure employment and unemployment the same way. For example, countries adopt different age limits in their definition of the labour force. Lower age limits in available data vary from age seven in Uganda to age 18 in Tunisia. And some countries use upper age limits in estimating unemployment rates: age 64 in Egypt and age 69 in Namibia. Moreover, countries such as Lesotho, Zambia and Zimbabwe estimate unemployment rates using the civilian labour force rather than the total.

- *Different sources.* National labour market estimates are based on information from different sources. These differences generate substantial discrepancies in unemployment rates. In South Africa the unemployment rate derived from employment office records was 5.4 per cent in 1997, while the rate from the 1999 household survey was as high as 25.3 per cent. Unemployment rates in Algeria, Burundi, Mauritius and Nigeria are obtained from official estimates, making them not comparable with unemployment rates in Egypt, Kenya, Uganda and Zimbabwe, which are derived from household surveys.

- *Changing number of observations per year.* Due to seasonality, statistics for a given year may differ depending on the frequency: monthly, quarterly, semiannually or annually. In some countries estimates are based on two observations a year: March and September for Mauritius and May and November for Egypt.

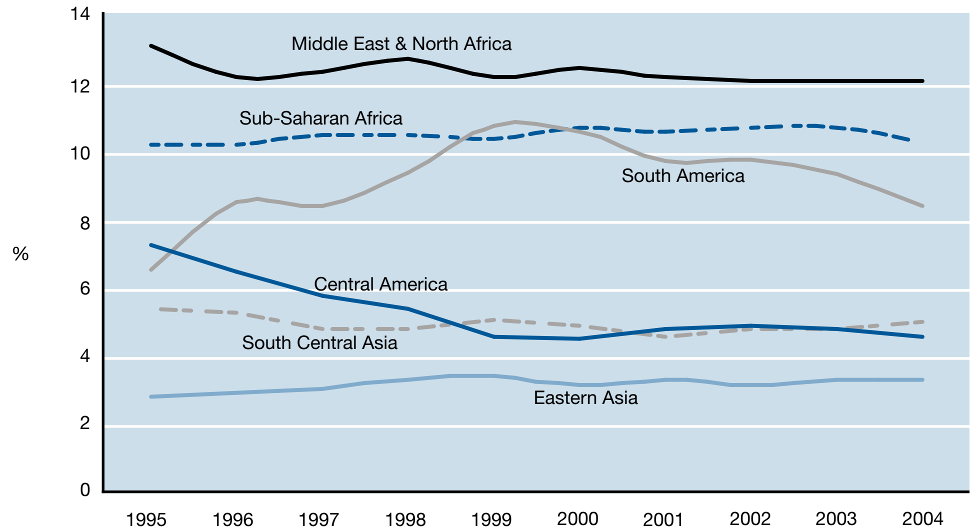
Source: *ILO 2005a, 2005b.*

There is limited demand for formal jobs

Second, the average unemployment figure does not capture discouraged job seekers. The limited demand for formal jobs in Africa discourages large numbers of potential workers from seeking employment. By definition they are not counted as unemployed. This problem is thought to affect educated people in African cities in particular because they have high expectations of formal jobs.

Third, the figure masks a high level of working poverty. The computation of unemployment rates considers all informal sector workers as employed, although most are either seasonally employed or earn wages below the poverty line. Up to 56 per cent of people

Figure 2.1
Unemployment rates by region, 1995–2004 (%)



Source: *Tarantino 2003.*

employed in Sub-Saharan Africa are working poor. The average unemployment rate does not convey this reality. Although people are employed, their jobs do not qualify as decent employment.

Fourth, the rate of unemployment conceals large variations across regions and countries. In 2003 Western Africa had the lowest unemployment rate (6.7 per cent), while Southern Africa had the highest (31.6 per cent) (table 2.1).

Unemployment in Uganda, for example, affected 7 per cent of the labour force—low compared with Lesotho's 39 per cent in 1997 (table 2.2). All these dimensions of the

Table 2.1
Variations in unemployment rates across regions, 2003 (%)

Region	Unemployment rate
Western Africa	6.7
Central Africa	9.4
Northern Africa	10.4
Eastern Africa	11.0
Southern Africa	31.6

Source: *ECA, from official sources.*

Table 2.2
Variations in country unemployment rates

Country	Year	Unemployment rate (%)	Working age
Zimbabwe	1999	6	15+
Uganda	1997	7	7+
Egypt	2000	9	15–64
Zambia	1996	15	12+
Botswana	2000	16	12+
Kenya	1994	21	15+
Morocco	1999	22	15+
South Africa	2001	30	15–65
Namibia	2000	34	15–69
Lesotho	1997	39	15+

Source: *ILO 2005b, based on most recent household surveys.*

labour market in Africa must be kept in mind to fully grasp the meaning of the average unemployment rate. Most particularly, unemployment and the excessively high number of working poor should be considered together.

Youth and gender dimensions of unemployment

Unemployment of youth is a particular problem in Africa (figure 2.2). At 21 per cent in Sub-Saharan Africa and 22.8 per cent in North Africa, the unemployment rate for youths ages 15–24 was twice that of the overall labour force in 2003 (ILO 2004b). These youth unemployment rates were the second and third highest in the world after the Middle East and barely changed between 1993 and 2003. In 2003 unemployed youth as a share of the total unemployed was 63 per cent in Sub-Saharan Africa, even though youths made up only 33 per cent of the labour force. Furthermore, in 2003 the youth-to-adult unemployment ratio of 3.5 in Sub-Saharan Africa meant that young people were much more likely than their adult counterparts to be unemployed.

"Unemployment of youth is a particular problem"

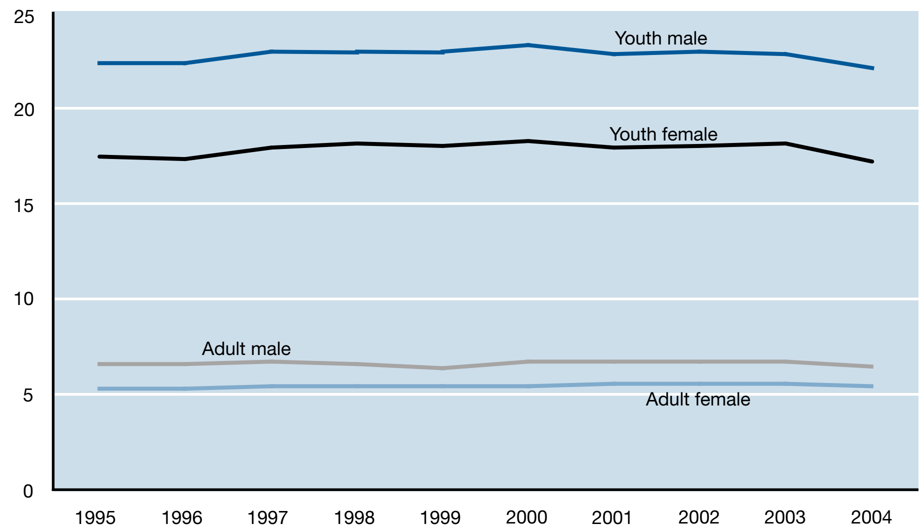
Youth unemployment is high not only because there are no jobs at all but also because youth, especially well educated youth, face a costly search process early on in their career. They may prefer to wait for well-paid jobs in the formal sector instead of going into low-level jobs in the informal sector. In Nigeria at least 17 per cent of the country's educational output is not absorbed into the labour market (Boateng 2001). Aware of the particular challenge faced by youth, UNECA is bringing youth issues to the forefront of the policy debate in Africa—for example, by hosting a Youth Symposium during the Fourth African Development Forum in 2004. Chapter 5 deals exclusively with the issue of youth unemployment.

In addition to the adult-youth split, a gender gap in favour of women is found in Sub-Saharan Africa and East Asia (see figure 2.2). The gap does not reflect the dire situation of women in the labour force because the rate of female unemployment is underestimated for a number of reasons. First, social norms tend to require women to declare themselves as housewives involved only in unpaid domestic work, which places them outside the coverage of the labour force. Second, women are more likely to be discouraged workers in the context of limited opportunities because men are usually served first. Third, the criterion requiring availability for employment during the reference period penalizes more women than men because women need more time to make the necessary arrangements such as care of children or elderly relatives or other household affairs before starting a job. Female unemployment rates in Africa also mask the fact that female workers are mostly in informal employment, where they are more likely among the working poor. In Sub-Saharan Africa 84 per cent of female nonagricultural workers are in the informal sector compared with 63 per cent of male nonagricultural workers.

Challenges differ in formal and informal sectors

The employment problem in the formal sector is distinct from the problem in the informal sector. As noted earlier, the main issue in the formal sector is how to create more jobs to absorb the increasing number of jobless people. In the informal sector, by contrast, the problem seems to be how to increase incomes.

Figure 2.2
Unemployment rates in Sub-Saharan Africa, by gender and age group, 1995–2004 (%)



Note: *Youth refers to people ages 15–24 (or the closest available ages); adult refers to people ages 25–64.*

Source: *Tarantino 2003*

Employment generation is the key issue in the formal sector

The structure of formal employment in Africa reveals two major facts. First, formal employment in the public and private sector is a small share of total employment. Data covering 1994–2000 show that Sub-Saharan Africa has the lowest share of formal employment in non-agricultural areas (38 per cent) (ILO 2002b). This share would be even lower if agriculture were included. There are, however, important differences across countries. In Ethiopia, for example, formal employment represented only 7.2 per cent of total employment in 1999, while 28.4 per cent of Kenya's working labour force was in the formal sector in 2000 (ILO 2002a). The formal sector is also less dynamic than the informal sector. The formal sector accounts for only 7 per cent of new non-agricultural jobs in Sub-Saharan Africa (Xaba, Horn and Motala 2002).

> *The relative size of the public sector has been declining*

Second, the relative size of the public sector has been declining for some time. In Ethiopia the share of the public sector declined from 4 per cent of total employment in 1984 to 2.9 per cent in 1999. The decline was more dramatic in Kenya, where the share dropped from 36 per cent in 1990 to just 11.4 per cent in 2000. Ethiopia and Kenya, like most African countries, have gone through a transformation aimed at reducing the size of the public sector to cope with ever-increasing budget deficits and other economic imbalances, especially since the late 1980s. What is more striking, however, is the trend in the size of the private sector. The reduction of the public sector may have pushed more workers into the private sector in Ethiopia, where the share of workers in the private sector doubled from 2.2 per cent of total employment in 1984 to 4.3 per cent in 1999, but this did not occur in Kenya, where the private sector still shrank from 36.5 per cent of total employment in 1990 to 17 per cent in 2000.

The "twin decline" phenomenon observed in Kenya can be explained by the informalisation of economies across the continent in the 1990s. As the formal sector shrank in Kenya, the informal sector was booming, tripling in size to 70.4 per cent of total non-agricultural employment from 1990 to 2000. If these two countries' experiences can be generalized, it becomes clear that the key employment challenge in the formal sector is to create more jobs to address the unemployment problem. The formal private sector is where these jobs should be created, given the characteristic inertia of public sectors in Africa. To this effect, as chapter 7 discusses, providing an enabling environment for private sector development is probably the most important service African governments can offer their citizens seeking decent employment in the formal sector.

Since in the formal sector creating employment is more imperative than increasing productivity, should African countries adopt policies that decrease capital-labour ratios in production? Empirical evidence suggests that the incremental capital-output ratio in Africa is among the highest in the world. The key policy question is therefore whether African countries should change the relative input prices to encourage producers to adopt the "appropriate technology", meaning labour-intensive technologies. Most governments pursue policies that subsidize capital through interest rate, credit, trade and exchange rate policies, while increasing the cost of production through labour market regulations. In the end, producers in the formal sector have no incentive to hire more labour when capital is subsidized.

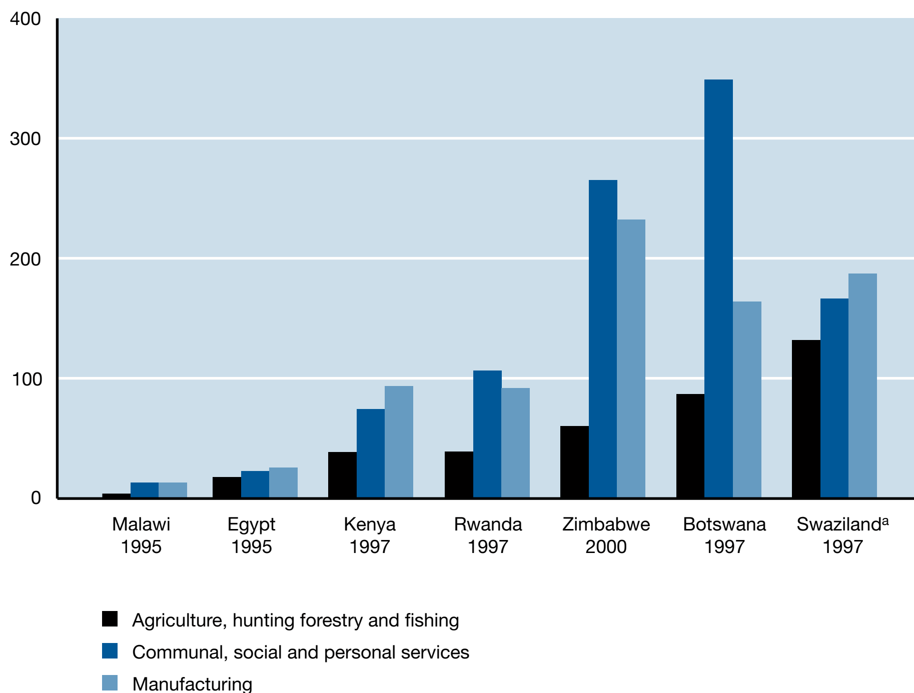
Low earnings and low productivity are the key issues in the informal sector

The informal sector in African economies has been acting as the "employer of last resort". As formal public employment declined in the 1990s in countries without welfare benefits or unemployment insurance for workers searching for other decent jobs, many were forced into the informal sector. The formal private sector is usually not an option because it is too small or because it is shrinking along with the public sector, as in Kenya. The informal sector is dominated by self-employment. Self-employment in non-agriculture represents 70 per cent of non-agricultural employment in Sub-Saharan Africa and 62 per cent in North Africa.

Low productivity and low earnings characterize informal employment in Africa. Sub-Saharan Africa is the only region where labour productivity decreased over the past decade. Productivity declined 0.2 per cent a year between 1993 and 2003 (ILO 2004c). Low and declining labour productivity is particularly pronounced in agriculture. The annual decline in agricultural labour productivity was 0.4 per cent between 1980 and 1990 and 1.5 per cent between 1990 and 1994 (Khan 1997). This has repercussions across the whole

Figure 2.3

Monthly wages by sector for seven African countries, various years ($)



a. Data are for unskilled workers only.

***Source:** ILO 2005b.*

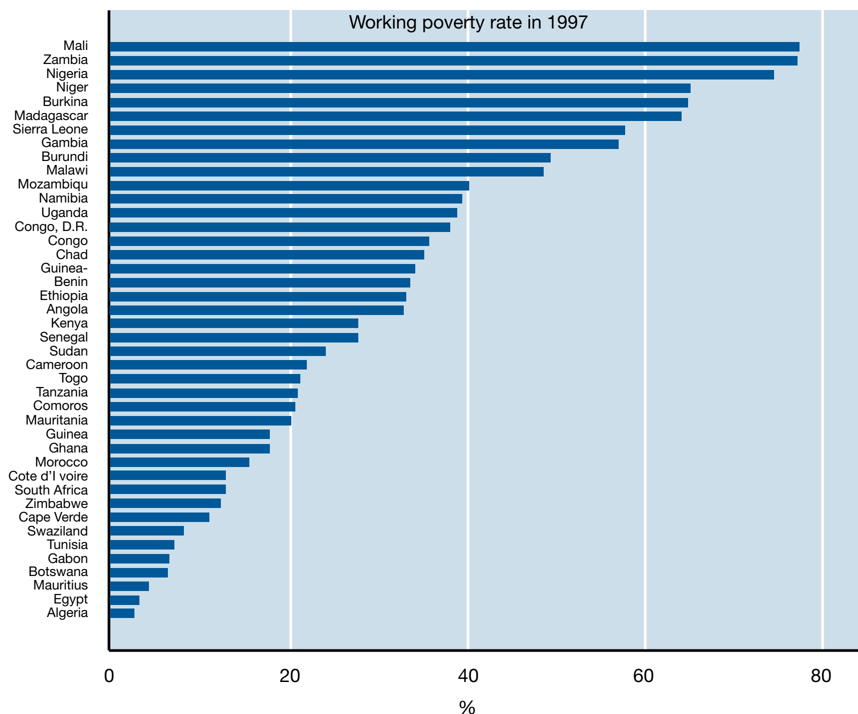
economy, given agriculture's importance in Africa. It can be argued that the dependence on low productivity agriculture is the key factor that explains the low levels of earnings of the people employed in the sector (figure 2.3).

Low earnings also characterize the non-agricultural informal sector. Survey evidence based on five African cities shows high proportions of informal sector workers earning less than the minimum wage (Charmes 1990). The share of unskilled informal sector workers earning less than the minimum wage is 66.7 per cent in Yaounde, 43.1 per cent in Bamako, 32.9 per cent in Lomé and 22.5 per cent in Kigali. Econometric evidence shows that after controlling for other determinants of wages formal employment wages are 27 per cent higher than informal wages in Burundi's manufacturing sector (Nkurunziza and Ngaruko 2002).

As a result of low productivity and low earnings, workers in the informal sector have a substantially higher incidence of poverty in the sense that their daily income is below $1 a day. Some 56 per cent of total employment earned less than $1 a day, and 89 per cent earned less than $2 a day (ILO 2004c). However, these regional averages mask significant differences among African countries. In 1997, for example, the rate of working poor was about 75 per cent in Mali, while only 3 per cent of workers in Algeria lived on less than $1 a day (figure 2.4).

Most informal sector workers earn less than one dollar a day

Figure 2.4
Working poverty rates, by country, 1997 (%)



Source: *Majid 2001.*

In addition to low earnings and high poverty incidence, informal sector workers are exposed to high risk for at least three reasons (Chen 2000). First, they live and work under harsh conditions, which are associated with shocks such as illness, loss of assets, loss of income, death of the breadwinner and the like. Second, they tend to have little or no access to formal risk-coping mechanisms such as insurance, pensions and social assistance. They also lack the resources to pay for proper housing and education. Third, given their low levels of income, on average, they are less likely to cope with these contingencies.

In summary, the key issues of concern to employment in the formal sector are different from those in the informal sector. For the formal sector, creating more well paid jobs is most important. But formal sector workers account for only a small share of the total number of workers. The issues facing the informal sector seem to be low productivity and low earnings, which keep most informal sector workers in poverty–a problem of paramount concern to policymakers.

Determinants of the African employment challenge

Nine determinants of the African employment challenge are identified here as the reasons behind Africa's failure to create more and better paid jobs and reduce poverty in the formal sector and to increase productivity and earnings in the informal sector.

Growth has failed to generate employment in Africa

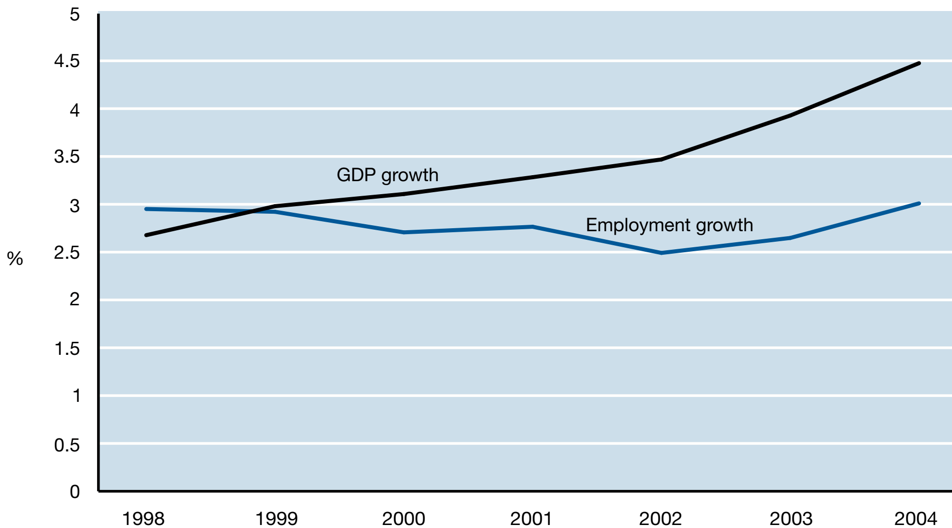
Despite the recovery in the rates of economic growth in Africa over the last few years, growth has failed to generate employment (figure 2.5). One reason is that the growth rates are still well below those required to have an impact on poverty through higher employment. For example, the current growth rate of 4.6 per cent is 2.4 percentage points below the minimum average needed to halve the continent's poverty rate by 2015, as advocated by the Millennium Development Goals. A second reason is that even observed growth is concentrated in the capital-intensive enclave industries that have few or no links to the rest of the economy. Chapter 1, for instance, shows that most of the growth in 2004 was realized in oil-exporting countries. On average, non-oil-exporting countries had a growth rate of 2.9 per cent in 2003 and 3.8 per cent in 2004—much lower than those in oil producing countries (5.4 per cent in 2003 and 5.3 per cent in 2004).

> *"Informal workers are exposed to higher risk"*

The slow growth of African economies can be attributed to two factors: low factor accumulation, namely physical and human capital, and low productivity growth. Over the last 20 years the average ratio of gross investment to GDP has been 18 per cent in Africa compared with 33 per cent in East Asia and the Pacific. Microeconomic data on the manufacturing sector show that in Africa human capital investment has been much higher than physical capital investment (Bigsten and others 2000). In view of the complementarity between physical and human capital in the production process a continued focus on the supply of labour without an accompanying increase in physical capital may be counterproductive. Chapter 7 discusses the conditions under which investment in physical capital can be increased.

Figure 2.5

Economic growth and employment growth in Sub-Saharan Africa (%)



Source: *UNECA calculations based on Tarantino 2003.*

However, factor accumulation alone will not allow Africa to reach growth rates observed in other fast growing regions (Easterly 2001). Growth accounting shows that only half the difference in growth between Africa and other developing regions is due to slower accumulation of physical and human capital (Collins and Bosworth 1996). The other half is explained by slower growth in productivity, implying that productivity is as important as factor accumulation in explaining Africa's slow growth. As discussed in the previous sections dealing with informal employment, the need to increase productivity in Africa cannot be overemphasized.

Low productivity has resulted in the lack of a structural economic transformation

The lack of a structural economic transformation to diversify away from unproductive agriculture may be explained by low productivity in the agricultural sector. Most African economies have not achieved high enough productivity in the manufacturing and services sectors to absorb excess labour in agriculture. This transformation would increase wages—and thus incomes–in the agricultural sector. Manufacturing productivity has traditionally led agricultural productivity. In addition, transforming economies from agriculture to the expanding labour-intensive industrial and services sectors may increase formal employment in the nonagricultural sectors (Chenery and Syrquin 1975; Belser 1999).4 And, even within the agricultural sector, a shift from traditional nonmarket agriculture to high value marketable crops could help raise overall incomes and reduce poverty in rural areas. Chapter 4 discusses these issues in more detail.

One of the most important factors behind the lack of Africa's agricultural transformation is the bias observed against the agricultural sector in many countries. Pricing and resource allocation are made in favour of the sectors that are easy to tax, so agricultural productivity has remained very low over the decades. And the little investment made within the agricultural sector favours exportable cash crops at the expense of the other products, despite the fact that the majority of the population depends on the other products. Bates (1983) argues that cash crops generate rents through tax revenue and income from exports and that the policymakers who appropriate these rents have vested interests in the cash crop sector.

Demographic pressure exacerbates employment problems

Demographic pressure remains a serious concern for labour markets in Africa. With a labour force growth rate of 2.9 per cent in Sub-Saharan Africa and 2.6 per cent in North Africa between 1993 and 2003, an ever-increasing number of people are competing for a limited number of jobs in the formal economy. In Sub-Saharan Africa the annual rate of growth of the labour force is projected to be 2.5 per cent between 2003 and 2015. Absorbing new entrants in the labour force will require the creation of about eight million additional jobs every year. The urban labour force is projected to grow faster than the rural labour force and to account for half of the total labour force by 2015 (ILO 2004a). In Sub-Saharan Africa the youth labour force is projected to grow 28 per cent between 2003 and 2015, despite the effect of the HIV/AIDS pandemic that seems to have a disproportionate impact on young people. As Chapter 4 discusses in detail, this situation is largely explained by the lack of a demographic transition in Africa. These trends will be more damaging to the youth labour force than to any other part of the population, as Chapter 5 explains.

"Increasing productivity in Africa is urgent"

Inappropriate education and training policies hinder the productivity of supplied labour

There are two key issues regarding the supply of skills in the African labour market: low literacy and skills mismatch.

Individuals are functionally illiterate if they cannot, with understanding, read and write a short, simple statement about their everyday life (World Bank 2004b). However, this standard definition does not reflect the changing pattern of a globalized labour market where a competitive worker must know how to do more than read and write. For instance, literacy in information technology is becoming a basic requirement in today's competitive world.

There are substantial regional differences in literacy, and Africa's literacy rate is lower than that of other developing regions (table 2.3). North Africa's 58.6 per cent and Sub-Saharan Africa's 61.2 per cent literacy rates are the second and third lowest in the world—just above South Asia but below the world average of 79.1 per cent in 2000. There are large differences across and within Sub-Saharan African countries. Younger males in urban areas tend to have higher literacy rates than older rural females.

Table 2.3

Youth and adult literacy rates, by region, 2000 (%)

Region	Adult literacy rate	Youth literacy rate
Europe and Central Asia	97.1	98.9
East Asia and Pacific	90.2	97.9
Latin America and the Caribbean	88.5	94.5
World	79.1	86.6
Middle East and North Africa	68.4	86.5
Sub-Saharan Africa	61.2	77.5
North Africa	58.6	—
South Asia	55.8	69.5

— not available

Note: *Adult refers to people age 15 and older; youth refers to people ages 15–24.*

Source: *World Bank 2004b.*

Literacy rates for youth in Sub-Saharan Africa are 16.3 percentage points higher than those for adults, suggesting that recent efforts to strengthen the supply and quality of basic education programmes have been successful in raising literacy rates, even though they remain relatively low by international standards (Blunch and Verner 2000).

Low literacy is a compelling problem in Africa because functional literacy is a prerequisite for entering the formal labour market. In their analysis of the Ghanaian labour market, Blunch and Verner (2000) defined individuals as functionally literate if they can read or write in English, or any Ghanaian language, and perform arithmetic calculations. They found that literacy rates vary significantly across sectors. Opportunities for job seekers with none or limited formal education are mainly confined to the informal sector. As a result, low functional literacy is associated with low productivity and low earnings. For example, according to the 1991/92 Ghana Living Standards Survey, almost 60 per cent of people in the highest earnings quintile are literate, against a mere 14 per cent of people in the lowest earnings quintile.

Notwithstanding improvements in educational attainment in Africa, there is a mismatch between the skills workers possess and those required by the market. This problem is driven by changes in labour demand and the inability of the education system to adapt to them. One explanation for the changes in labour demand is the declining role of the public sector in recent years. Until recently, the public sector had been almost the only source of formal employment. The public sector's share of non-agricultural employment in Sub-Saharan Africa was 32.9 per cent in the 1990s (Fosu 2002). Because the public sector in Africa has traditionally placed a premium on educational achievement rather than on marketable skills, university graduates, absorbed primarily by the public sector, have overwhelmingly had a background in the social sciences and lacked specific marketable skills. With the role of the public sector declining in many African countries, the demand for employment is shifting towards the private sector. The private sector is looking for individuals with specific and practical skills who can operate in an evolving workplace. In Ghana, for example, 47

per cent of social sciences and liberal arts graduates are unemployed (Boateng 2001). The skills mismatch, in turn, increases pressures on the public sector to absorb graduates unable to find jobs in the private sector.

"Demand for employment is shifting from the public to the private sector"

Unfortunately, the education and training infrastructure in Africa is not responding quickly enough to these changes, and it is hard to see how this will improve in the short-term without changing the structure of incentives that motivate those providing formal training. What incentives are given to institutions of formal training to adopt the appropriate curricula? Moreover, what incentives are given to students to pursue difficult but more developmental subjects when they know that pay and remuneration do not discriminate on the basis of one's specialization? These are questions that policymakers will need to consider in order to come up with innovative policies to reform Africa's education system.

Without appropriate supply-side adjustments, the employment problem becomes even more serious as the workplace increasingly becomes upscale-service-oriented, requiring employee participation and the use of information and communication technology (Bresnahan, Brynjolfsson and Hitt 2002; Smith 1997). In the short-term skills can be upgraded through on-the-job and vocational training programmes. So far these programmes have remained rare and not carefully designed to respond to the specific needs of the labour market in many African countries. These programmes should target the informal sector not only because of the relative importance of the sector but also because of the low level of skills of those employed in the sector. Chapter 5 discusses these issues in detail.

Labour regulations fail to protect the majority of workers

Economists differ as to the costs and benefits of labour regulations such as minimum wage, nonwage compensation and hiring and firing rules. Proponents of labour policies view them as important for the social protection of workers to ensure that their rights are respected, that they work in a safe environment and that they are paid a living wage. Those holding this view advocate strict adherence of employers to these policies.

An opposing view emphasizes that these regulations raise the cost of labour and thus discourage job creation while favouring privileged insiders (Freeman 1993). Proponents of this view advocate flexibility of employment policies to help facilitate adjustments to economic shocks. They further argue that rules to protect job security may increase the number of stable jobs at the expense of higher long-term unemployment because policies usually result in fewer opportunities for regular employment in the formal sector, which penalizes certain groups of workers (women, youth and the unskilled or poorly educated) who are less likely to get the few jobs available. Many of these workers would remain jobless or move to the informal sector, where job protection policies do not apply. The net effect of these policies in Africa is the question of interest in this section. Do they protect workers or do they hamper employment creation? To answer this question, it is useful to distinguish between the average and marginal effects of these policies.

The average effect of labour regulations is small. Labour regulations in Africa are considered to be the most rigid in the world (World Bank 2004a). However, the average effect of these policies on workers' protection and employment levels is small for several reasons. First, the effect of these regulations is limited to the formal sector, which accounts for only a small share of the labour force. For example, in the countries forming the Communauté financière d'Afrique (CFA) only about 5 per cent of the labour force is effectively covered by labour regulations, which are some of the most inflexible regulations in Africa (Rama 1998). Second, even when the regulations are in place, they often are not enforced (box 2.3). For example, workers in the formal sector are entitled to nonwage compensation that includes medical, death and retirement insurance in most countries, but in practice these policies are poorly enforced and limited in scope. As a consequence of limited coverage and poor enforcement, very few workers are effectively protected by labour regulations.

Third, some regulations provided for in the labour code are not binding. Case in point: minimum wage in the formal sector. In many countries minimum wages are set at levels below actual starting wages, which may explain why individual as well as cross-country studies have found no significant effect of the minimum wage on employment in Africa. In Ghana, for example, real minimum wages have remained below starting wages in the manufacturing sector, despite substantial increases since the early 1980s, and there is no strong evidence of the minimum wage setting a binding floor for private sector wages in the country. The idea that fixed public sector wages or minimum wages prevent labour market adjustments in Africa is inconsistent with empirical evidence from Ghana and Kenya (Teal 2000). Along the same lines, contrary to common perception, minimum wage policies are

Box 2.3

Labour regulations are poorly enforced

In many developing and transition countries enforcement of labour market regulations is weak, hampering their effectiveness. Even in countries with labour regulations employers can easily avoid them, in practice, because of a lack of proper enforcement. In Côte d'Ivoire, for example, firms use alternative arrangements such as subcontracting and apprenticeship to bypass the most constraining labour regulations. In Cameroon only 2 per cent of managers of manufacturing firms in 1994 reported that labour regulations were a big or severe problem, compared with 85 per cent who considered them a slight or nonexistent problem. Similar results were found for wage costs, rules regarding layoffs and the cost of layoffs. In Senegal most managers did not view labour market regulations as a constraint, even before most regulations were dismantled. Developing countries typically do not allocate significant amounts of resources to enforce labour market regulations, even to police the most visible employers (for example, the public sector). Therefore, labour regulations should be realistic and encourage self-compliance to moderate the enforcement challenge. It is good practice to resolve as many disputes as possible through prejudicial arbitration. Indeed, many countries are relying increasingly on alternative dispute resolution mechanisms that emphasize fact-finding, mediation and conciliation as opposed to costly binding decisions made by government inspectors, arbitrators or judges.

Source: *Rama 1998.*

not the source of high wages observed in CFA countries (Rama 1998). Also, the level of the minimum wage has no significant effect on the level of employment in 31 developing countries, including 12 from Africa (Saget 2001). Moreover, hiring and firing rules have no statistically significant effect on the level of unemployment in developing countries (Lindauer 1999; Freeman 1993).

The marginal effect of labour regulations might be large. It is incorrect to conclude that labour regulations have no impact on the labour market based only on the average effect. It is very likely that potential new employment is influenced by labour market regulations. Especially since many developing countries compete to attract export-oriented foreign investors, a small difference in labour costs may have a large impact on the location of investment. Foreign employers will likely consider these regulations before deciding whether to enter the market or not. Once they enter, the level of these variables may not be a constraint. In the current context of globalisation, where African countries face fierce competition from other countries to attract foreign investment, the perception of rigidity of African labour markets might be particularly detrimental.

The choice a local entrepreneur faces is whether to invest in the formal or the informal sector. One reason that an entrepreneur may choose to invest in the informal sector is to avoid bureaucratic red tape and excessive costs. If the formal labour market is overly regulated, the informal sector provides an alternative to those who cannot or do not want to support the cost. In India, for example, a recent study found that the states that amended labour regulations in favour of workers experienced a decline in output, employment, investment and productivity in formal manufacturing firms, while output increased in informal manufacturing firms (Besley and Burgess 2002). By contrast, changes in the ratio of the minimum wage to average wage do not seem to have a significant impact on the share of the informal economy in Latin America (Saget 2001). These results suggest that labour regulations might be partly responsible for informalisation in India but not in Latin America. The role of labour regulations needs to be investigated with regard to the increase of employment in the informal sector at the expense of the more regulated formal sector in many African countries.

> *"Marginal effects of labour regulations might be large"*

One aspect that may have an indirect effect on labour market outcomes is the level of unionisation. An expansive literature on the effect of unions on wages, investment and job creation in developed economies exists. Empirical studies generally find that unionisation increases labour costs and reduces investment, with a negative effect on job creation. Very little is known about these relationships in Africa. The limited empirical evidence shows that unionisation generates a wage premium and increases nonwage benefits. But these effects depend on the price elasticity of the demand and supply of labour (box 2.4).

These findings suggest a trade-off between job protection and the guarantee of a living wage on one hand, and flexibility of the regulations governing the labour market not to scare off potential investors on the other. The key policy challenge is to strike the right balance between these contradictory objectives. In this light, labour regulations can be used to reduce the high level of working poverty observed in Africa. They should ensure workers an income over the poverty line and other basic aspects of decent employment. However, they should not constrain firm profitability, essential for employment expansion, or discourage informal firms from becoming formal. To have a noticeable impact, labour

Box 2.4
What is the effect of unions on Africa's labour markets?

The limited empirical evidence shows the following. First, unionisation generates a wage premium. For example, South Africa experienced an increase in union wages during the period of rapidly increasing membership between 1985 and 1993. The wage premium was as high as 18.5 per cent of non-union wages (Hofmeyr and Lucas 1998). Given that South Africa has one of the highest rates of unionisation of wage employees in the developing world, unionization is expected to have an important impact across the economy. For example, industrial councils or wage boards, whose collective agreements are extended to the whole industry and areas where they have been negotiated, agree on minimum wage floors. These agreements become binding even to employers who did not participate in their negotiation (Teal 2000). In Ghana unions appear to have a positive impact on workers' earnings. Unionised firms pay 32–34 per cent more than non-unionised firms (Teal 1996, 1998). In the same context, full unionisation in Ethiopia's public sector in the 1990s resulted in job queues of private sector workers for public employment (Mengistae 1999).

Second, unionisation increases nonwage benefits, such as insurance and pension plan coverage, which are often provided at the discretion of the employer. As a result, the coverage of these policies should be higher for unionised workers depending on their negotiating power (Akyeampong 2002).

Third, trade unions are less effective when the price elasticity of the demand and supply of labour is high. Unions are also less effective when labour and capital are highly substitutable, as the case of South Africa's forestry sector shows (Goedecke and Ortmann 1993).

These results suggest that the power of unions in countries such as South Africa may be contributing to high unemployment rates. Investors wary of losing control over the cost of labour could opt for more capital-intensive technologies. Therefore, although unionisation may benefit those already employed, it limits firms' propensity to create new jobs, exacerbating the problem of unemployment.

"Labour regulations roles remain uninvestigated in most of Africa"

regulations need economic and regulatory incentives that transform the economy in a way that reduces the relative size of the informal sector (see chapter 7).

Lack of an enabling environment constrains investment and job creation

Investment has been shown to be an important determinant of economic growth and hence job creation. However, administrative barriers, lack of access to factors of production and poor infrastructure remain critical constraints to private investment in Africa, both domestic and foreign (box 2.5). As a result, the level of investment is particularly low in Africa. In 2002 gross private investment was only 15.3 per cent of GDP. With respect to FDI flows, only $15 billion of foreign direct investment was invested in Africa in 2003, compared with $39 billion in Latin America and $89 billion in Asia and the Pacific (UNCTAD 2004).

Box 2.5
Constraints to doing business in Africa

Compared with other regions, Africa has the highest regulatory obstacles to business activities. First, African countries have lengthy and costly procedures for starting a business: an average of 11 procedures, each costing 225.2 per cent of per capita income—high enough to drive many entrepreneurs into corruption or informality. Second, hiring and firing regulations in Africa are the most rigid in the world. The top 10 countries in the employment rigidity index are all African. Third, registering property is far more costly in Africa than in any other region. Complex procedures to register property also lead to more informality and corruption. Fourth, access to credit is limited by lack of credit information and weak legal protection of lenders. Fifth, without reliable financial information and effective protection of shareholders investment in business partnerships and publicly listed companies is relatively low. Sixth, contracts enforcement in Africa is weak because courts are often slow, inefficient and corrupt. The average cost of recovering a debt through administrative channels amounts to 43 per cent of the value of the debt. Seventh, inefficient bankruptcy regulations prevent viable businesses from reorganizing and unviable ones from closing. Claimants recover an average of only 17 cents on the dollar from insolvent firms—and the process takes an average of 3.5 years. This is the lowest recovery rate in the world.

Source: *World Bank 2004a.*

Whether economic agents choose to invest or consume their resources depends on the structure of incentives an economy gives to investors (Easterly 2001). One way to create an enabling environment for future private investment is through public investment in basic sectors such as infrastructure. This type of investment increases the productivity of private investment, particularly in developing countries (Agénor and Montiel 1996). Empirical studies have also clearly shown that growth is more responsive to private investment than to public investment (Agénor and Montiel 1996; Khan and Reinhart 2000). In this regard, policies that constrain private investment may have an important impact on job destruction. For instance, volatility in exchange rates, capital flows, interest rates, and inflation, compelled firms to freeze hiring, downsize or even close down in the 1990s in a number of African countries (box 2.6). Recent progress in stabilizing African economies has not eliminated these challenges.

“Small firms are more credit-constrained”

Although increasing investment may not necessarily increase employment directly, there could be an indirect effect because of the complementarity between human and physical capital noted earlier. Moreover, it is not just the level but also the character of investment that matters. Investing in sectors using labour-intensive technologies, particularly those that use unskilled labour, is probably the best way to generate employment. Policymakers could help by reducing the high levels of uncertainty prevailing in many countries to create strong investment opportunities, the missing link between the supply and demand of labour in many African countries (see chapter 7).

For small firms in the informal sector investment could be constrained by the lack of financial resources. Although studies have shown that small firms are more credit constrained than larger ones (Bigsten and others 2003), the use of credit could have, on average, a

Box 2.6

The effect of macroeconomic instability on firms in Kenya

Macroeconomic instability in Kenya during the 1990s resulted in high inflation, high interest rates and large devaluations that destabilized manufacturing firms. Uncertainty induced more and more suppliers to require cash payments instead of the usual trade credit. Firms relying on imported raw materials saw costs skyrocket because prices were quoted in dollars rather than in Kenyan shillings. Moreover, the doubling of interest rates in a context of economic decline forced many firms to collapse. It is not surprising, therefore, that the two most important problems identified by Kenyan firm managers in the 1990s were inadequate access to credit and low demand.

Source: *Nkurunziza 2004.*

> *Some economies are managed on the basis of patronage and rent seeking*

positive effect on firm growth. If credit to small firms in the informal sector could help them raise their productivity, it would probably induce them to grow and graduate to the formal sector, where they would be able to create even more jobs. For example, an econometric study of the Kenyan manufacturing sector shows that the number of jobs created by surviving firms using bank credit was 93 per cent higher than that of firms not using credit (Nkurunziza 2004).

Globalization is a challenge for firms in export markets

Most African countries' domestic markets are so small that firm growth, defined as the increase in the total number of workers, can be realized only through exports. However, with the current trend towards globalisation of markets, exporting African firms face stiff competition from other regions. The failure of African firms to enter the export market of labour-intensive manufactures may explain the limited growth in labour demand (Teal 2000). For example, data on manufacturing in Ghana show that only 11 per cent of firms export any of their output, and only 4.2 per cent of total output is exported (Teal 1998). Exporting firms in Ghana are larger than non-exporting firms, but their size remains relatively small compared with firms in Mauritius, the only Sub-Saharan African country that has successfully grown through labour-intensive manufactures. The average size of a firm in Mauritius' textiles and garments sector (181 workers) is 11 times larger than that in Ghana (17 workers). The difference in firm size between the two countries is mostly attributed to different efficiency levels.

Why is globalisation a challenge in Africa when it is an opportunity in other developing regions? Generally, globalisation hurts African firms because of their low productivity and inefficiencies. A few African countries, such as Mauritius and Morocco, where productivity levels are comparable to those in other developing regions, have been able to tap into the opportunities brought about by globalisation (see chapter 6). To be able to export, firms need to reach a minimum level of competitiveness. Encouraging the creation of large, efficient and labour-intensive firms in Africa seems to be the right policy to develop the export sector. How to achieve this objective depends to a larger degree on the nature and structure of incentives put in place to create an enabling environment, as chapter 7 discusses.

Politics drive economic decisions that worsen unemployment

This topic is hardly covered in the empirical literature on labour markets in Africa, but unemployment has a political dimension in many African countries. Unequal or restricted access to key economic assets such as land, education and training determines who is and is not employed. The control of a country's wealth by a small group may result in a phenomenon of jobless growth, where economic growth benefits only a small part of society. These distributive inefficiencies are thought to be the root of high unemployment rates and poverty in several African countries.

> *Unequal access to opportunity creates inequities and frustration*

One of the consequences of a distributive system based on politics rather than economic fundamentals is that it creates large inefficiencies. First, marginalizing a large part of the population implies that productive human resources are not allowed to fully contribute to the economy, which creates widespread unemployment or underemployment. Second, economies managed on the basis of patronage and rent seeking are usually focused on distributing rents rather than producing them. This is especially the case when the size of the elite is small relative to available rents to be shared (Adam and O'Connell 1999). Therefore, the economy declines with ensuing widespread unemployment. Third, predatory regimes impose high taxes on economic activities, discouraging production and increasing unemployment. Fourth, in predatory economies both human and financial capital tend to flee, reducing the stock of productive resources. In addition, unequal access to opportunities creates inequities and frustrations that can lead to social unrest and all sorts of destructions with a high economic cost.

Unequal distribution of a country's resources and its impact on the level of unemployment result from two different phenomena: the first relates to historical factors. In a few countries–Namibia, South Africa and Zimbabwe, for example– colonisation dispossessed indigenous people of their ancestral land. In these countries unemployment and poverty are widespread among the landless black population. Unemployment rates are particularly high in Namibia (34 per cent) and South Africa (30 per cent). These countries also have some of the highest rates of income inequality in the world. The Gini index is 50 in Zimbabwe, 59 in South Africa and 74 in Namibia, while the Sub-Saharan Africa average is 42.8 (Fosu 2005) and the world average is 40.0 (UNDP, 2004). Such deep social imbalances have contributed to cause civil unrest in some countries.

The second phenomenon generating inequalities has to do with the patrimonial systems adopted by several countries, especially in the post-colonial period. Many governments instituted systems of governance where the distribution of public goods is truncated in favour of a privileged group or region at the expense of other groups or regions within the country. The distribution of education infrastructure is a good example. In some instances, leaders build the best schools in their own region, also employing the most qualified teachers. Mechanisms to filter access to education by other members of society may also be adopted. Commonly in these countries most jobs are in the public sector, where having an education is sine qua non to obtaining a post in the civil service. Since these jobs are often reserved for people from one privileged group, unemployment levels are disproportionately higher among the remaining portion of the population.

Imbalances in resource allocation, especially public goods, have been observed in many African countries. In Sudan Arabic-speaking northerners receive a disproportionately larger share of the country's resources than do southerners. In Rwanda under the reign of President Juvenal Habyalimana people from Gisenyi, the president's hometown, were more privileged in terms of employment, access to credit, scholarships and the like. In Burundi people from the south benefited from the fact that southerners controlled power for most of the post-colonial period. These few examples are relevant for most African countries. In these countries unemployment and poverty rates among marginalised groups are higher than among the privileged, leading some observers to postulate that poverty and inequality in Africa may be politically determined (Milanovic 2003).

Some 40 per cent of Sub-Saharan African countries experienced at least one episode of civil war over the past 40 years (Elbadawi and Sambanis 2000). This has created the simplistic perception that wars in Africa are caused by tribalism and ethnic hatred. However, careful analysis and comparison with other regions reveal that African political instability

Box 2.7
The impact of war on employment

War in Angola caused at least 1.5 million deaths and displaced another 2–4 million people, whose participation in the country's productive activities was severely curtailed. In an environment of insecurity and economic meltdown, the majority of the population – even those not displaced - witnessed a severe reduction in its capacity to engage in productive activities. Moreover, the destruction of infrastructure in war economies wipes out the foundations of employment generation. For the 470,000 Angolans who returned from neighbouring countries at the end of the country's 30-year war, chances are slim for finding jobs that can provide for their family's basic needs.

As a result of the current war in Burundi, manufacturing production declined by 13 per cent a year between 1993 and 1997. A firm survey showed that just one year after the start of the conflict only 45 per cent of firms had maintained their pre-crisis size or had reduced it by less than 10 per cent, 15 per cent shrank by 10 per cent–25 per cent, and 21 per cent declined by more than 25 per cent. These figures suggest a high rate of job destruction. Burundi witnessed disinvestments rather than investment during the war. Gross investment declined from 17.5 per cent of GDP in 1990 to a mere 5.6 per cent in 1998, implying important losses in potential jobs. The war wiped out 31 per cent of livestock, the main form of physical capital held by rural households. Not only did the war disrupt production, but it also profoundly affected the stock of human capital. Many Burundian professionals have been killed, and a large number of survivors have left the country.

In Liberia conflict has destroyed much of the country's infrastructure. The war claimed an estimated 150,000 lives (6 per cent of the population), and most skilled human capital emigrated. During the war in the 1990s employment in the formal sector was cut in half. Employment in alluvial diamond mining, a key sector of the Liberian economy, dropped from 60,000 before the war to a mere 6,000 in 2001 as a result of the war and the UN sanctions on Liberian diamonds.

Source: *ILO 2004a; Nkurunziza and Ngaruko 2002; Davies 2005.*

"Deep social imbalances have contributed to civil unrest"

is caused by serious failures in economic and political governance. As discussed earlier, different forms of discrimination against large sections of the population by leading elites have sometimes led to violent revolts, which eventually resulted in civil wars. Civil wars, therefore, are more likely the result of a combination of greed of the elites and grievances of those marginalized (Collier and Hoeffler 2004).

The relationship between economic factors, including unemployment, and political instability is complex. These factors may be seen as both causes and consequences of political instability. The elites' greed implies that a small share of the population appropriates most economic opportunities, excluding large sections of the population. For instance, the regions with the highest density of education infrastructure produce more educated people, who have a higher chance of obtaining employment in the public and private sectors. These regions thus experience disproportionately lower rates of unemployment. Marginalized groups become unemployed and have no voice—and hence no peaceful way to convey their grievances. Because they are usually made to believe that they stand to gain more if they are successful, joining a rebellion becomes a tempting alternative. It is in this context that Collier and Hoeffler (1998) use the level of education to proxy for the opportunity cost of joining a rebellion. Other studies such as those in Fosu and Collier (2005) use unemployment rather than education as the proxy for the opportunity cost of joining a rebellion. This offers a direct relationship between greed, unemployment, grievances and political instability.

Wars destroy physical and human capital and create uncertainty that depresses investment, as argued in chapter 7. This blights employment opportunities for a long time (box 2.7).

Loss of human capital due to HIV/AIDS and brain drain

The emergence of HIV/AIDS and the resurgence of old diseases such as malaria and tuberculosis have resulted in drastic deterioration of health in Africa in the 1990s. HIV/AIDS is one of the deadliest diseases in Africa. More than 75 per cent of global AIDS deaths, 22 per cent of tuberculosis deaths and 90 per cent of all malaria deaths occur in Sub-Saharan Africa (UNECA 2004).

The negative effect of HIV/AIDS on the accumulation and productivity of human capital in Africa is astounding (see Hamoudi and Birdsall 2004). HIV/AIDS is concentrated in the most sexually active group (25- to 45–year-olds), which happens to be the most productive part of the population, as also discussed in chapter 5. For example, there is mounting evidence that teachers, health workers, civil servants, construction and mining workers and other professionals are being lost in Sub-Saharan Africa to HIV/AIDS and related infections. The attrition rate is so high that some countries cannot train new professionals fast enough (UNECA 2004). By forcing skilled workers out of the labour force, the HIV/AIDS epidemic not only hampers production capacities but also results in the loss of jobs for the unskilled workers in the labour force.

Table 2.4
Estimates of brain drain from Sub-Saharan Africa

Period	Total emigration of highly skilled migrants from Africa	Average per year
1960–75	27,000	1,800
1975–84	40,000	4,400
1984–87	70,000	23,000
1986–90	50,000–60,000 middle- and high-level managers emigrated from the continent.	
1960–87	100,000 trained and qualified Africans abroad, 30 per cent of them highly skilled.	
1960s	More than half of the Africans who went overseas to study physics and chemistry in the 1960s never returned home.	

Source: *Haque and Aziz 1998.*

An additional problem in Africa is rising human capital flight (table 2.4). Brain drain is viewed as a negative externality imposed on the population remaining behind that results in slower economic progress and living standards (Bhagwati and Hamada 1974). First, because it reduces the supply of skilled and professional labour, which is a necessary complement to semiskilled and unskilled labour, brain drain results in job losses for semiskilled and unskilled workers (Piketty 1997; Miyagiwa 1991). Second, as discussed in chapter 6, brain drain results in the loss of the potentially most enterprising and ambitious young population. This stifles the development of a more dynamic private sector, therefore reducing work opportunities (Ndulu 2002).

Human capital flight measured by educated emigrants as a share of the educated adult population, which for most of Africa's post-independence history has not been a significant problem, is rapidly increasing (Collier, Hoeffler and Pattillo 2004). For a sample of 24 African countries in 1990, 74.4 per cent of the emigrants to the United States had received tertiary education in their home countries (Carrington and Detragiache 1998). The emigration of the educated is projected to strongly intensify over the next few decades because emigration is subject to a powerful momentum effect. Migrants assist subsequent migrants, making it very difficult to reduce human capital flight once it has started.

In the context of globalisation brain drain can be explained as the failure of African countries to compete for their own citizens in international markets. Slowing human capital flight or reversing it by attracting back those who have left is extremely difficult. The causes of the high and increasing human capital flight are mostly within Africa itself: lower returns on education investments, lack of complementary facilities for practicing specialized professions and high political and economic risks that affect the ability to use human capital. Because the causes of brain drain are internal, the solutions should be, too. African countries should pursue policies that not only allow them to retain their highly skilled citizens but also make use of those who have already left. For example, a general improvement in the political and economic environment could reduce the number of potential new emigrants. For those who have already left, targeted incentives to those with the needed capital or skills could attract them back to invest or work for a limited period of time (Ndulu 2002). Ethiopia seems to be doing this with some success.

Conclusion

The fundamental issue in Africa's labour markets is the failure to create more and better paid jobs. The key challenge in the formal sector is the limited number of jobs or unemployment, whereas the main problem in the informal sector is low earnings and low productivity. This chapter has discussed nine factors explaining these two issues. First, slow employment-intensive growth limits job creation in the formal sector. Second, the lack of a structural transformation of African economies results in continued overreliance on an unproductive agricultural sector. Third, demographic pressure exacerbates the problem of youth unemployment. Fourth, inappropriate education and training policies result in both low skill supply and skills mismatch. Fifth, labour regulations are limited to the formal sector and are poorly enforced, making them ineffective in protecting the rights of the majority of workers, who are in the informal sector. Even though the average effect of these regulations on the level of employment might not be high, labour regulations may prevent investment or divert it to the informal sector. Sixth, a business-unfriendly environment inhibits investment, with an adverse impact on private sector development. Seventh, globalisation amplifies the challenges faced by firms in the export market. Eighth, economic choices guided mostly by political considerations lead to economic inefficiencies and contribute to political instability. Ninth, HIV/AIDS and brain drain destroy human capital within the economy.

Later chapters analyse in more detail these key issues in order to provide appropriate policy recommendations. Chapter 3 discusses the extent of poverty in Africa and shows that employment is the major route out of poverty. Chapter 4 addresses the problem of structural economic transformation to increase the demand for labour. Chapter 5 deals specifically with the issue of youth unemployment, focusing on education and demographic problems identified in this chapter. Chapter 6 analyses the impact of globalization on employment and proposes the best ways to take maximum advantage of the current trend towards globalization. Chapter 7 focuses on institutional and policy adjustments needed to promote investment, private sector development as well as economic and labour market and economic efficiency.

Endnotes

1 In 1979 the Lagos Plan of Action for the Economic Development of Africa, 1980–2000, noted that the lack of productive employment was a key factor in explaining high levels of poverty in Africa. It called for a number of measures, including more effective use of the continent's human resources. More recently, African leaders at the highest political level have adopted several declarations on employment promotion, including the 1991 Declaration on Employment Crisis in Africa, adopted by the 27th Ordinary Session of the Assembly of African Heads of State and Government; the 1994 African Common Position on Human and Social Development in Africa, adopted at the World Summit for Social Development; the 2002 Declaration and Framework for Action on Youth Employment; and the 2004 Plan of Action for the Implementation of the African Union Declaration on Employment Promotion and Poverty Alleviation in Africa.

The Treaty Establishing the African Economic Community, the Constitutive Act of the African Union and the New Partnership for Africa's Development have important provisions on promoting employment, developing human resources and fighting poverty. All these initiatives consider employment promotion the linchpin of poverty reduction strategies in Africa. But the long list of political declarations contrasts with the lack of tangible results in terms of employment creation in Africa over the years. Why the absence of progress? The declarations have not been implemented by their signatories because of a lack of commitment at the country level. More fundamental constraints may also explain the persistent high rates of unemployment in Africa, among the highest in the world.

2 However, microeconomic empirical studies generally do not find a strong statistical relationship between poverty and employment. This does not necessarily mean that the two variables are not related. The weak relationship may be explained by a host of factors, including the way both variables are defined as well as the problems of measurement (see boxes 3.1 and 3.2 in chapter 3).

3 To overcome the issue of incomplete information, interpolation techniques are used. To compute regional indicators, missing observations are dealt with by weighting the sample of respondent countries. To address country heterogeneity, the fixed effects technique is used to estimate unemployment rates. These adjustments provide the best data available for making international comparisons. In this light, the regional statistics used in this chapter are based on this data set, while national statistics are derived from the International Labour Organization's LABORSTA database. See Tarantino (2003) for more information on addressing data shortcomings in Africa.

4 In the case of the so-called enclave economies, where capital is concentrated in a specific sector with limited spillovers, employment is not guaranteed to increase.

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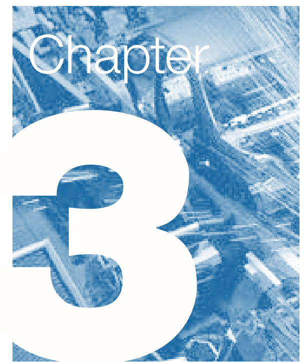


The poverty challenge in Africa: placing decent employment at the heart of the battle

The high incidence of poverty in Africa is the primary development challenge facing the continent today. This chapter examines the salient features and characteristics of the poverty challenge in Africa and articulates the analytical links among growth, employment and poverty to show that employment is a major route out of poverty. It then identifies the employment gaps of Poverty Reduction Strategy Papers. Finally, it provides recommendations for strengthening the employment intensity of the growth process and for mainstreaming employment policies in poverty reduction strategies.

"In Africa, 46 per cent live on less than one dollar a day"

Sub-Saharan Africa has the highest incidence of poverty in the world, and unlike almost all other regions of the world, poverty in Sub-Saharan Africa has been rising over the last decade.[1] The share of people living on less than $1 a day in Sub-Saharan Africa exceeds that in the next poorest region, South Asia, by about 17 percentage points. In 2003 about 46 per cent of the population in Sub-Saharan Africa lived on less than $1 a day—slightly more than in 1980 and in 1990. At the global level, however, the incidence of poverty is much lower—and it is declining, from 40 per cent in 1980 to 20 per cent in 2003.

The share of people below the poverty line tells only part of the story. Many people in Africa are not only below the poverty line, but also poor for long and sustained periods. They are chronically poor, emerging only briefly from poverty. Indeed, the incidence of chronic poverty in Sub-Saharan Africa is the highest among all regions.

Poverty is multidimensional and self-reinforcing. Poor people have low incomes and consumption levels, and many depend for their livelihoods on (low productivity) subsistence agriculture or on the informal sector. Wage-earning workers have low salaries, limited protection and frequent bouts of unemployment. The poor are inadequately educated and tend to be less healthy than the rest of the population.

Poverty is not gender neutral. Access to and control of productive assets by women is limited by the social norms ingrained in African societies. Women are often restricted from product and labour markets. These inequalities result in higher poverty for women and are often accompanied by higher poverty for children, which reduces health and educational outcomes.

Poverty in Africa is often described as mostly a rural phenomenon not only because the majority of the population live in rural areas but also because of the pattern of distribution of economic activity between rural and urban areas. In Africa rural-urban differentials in the incidence of poverty are large and persistent.

The incidence of "working poverty" is high in Africa. Low returns to labour due to low productivity, widespread underemployment and vulnerability to shocks are central to the high incidence of poverty among the employed and self-employed. In fact, the working poor accounted for more than half the employed in Africa in 2003.

What is compelling about the poverty trend is that in recent years it has occurred in the context of positive growth. The failure of growth to reduce the incidence of poverty in general, and working poverty in particular, suggests the need to critically re-examine the nexus of growth, employment and poverty reduction. Curiously, little analytical work has been done in this area. In contributing to the literature on this subject, this report argues that given the dearth of credible formal social insurance programmes in Africa, most poor people tend to be either employed or underemployed. Thus, as evidenced by the high incidence of "working poverty", poverty in Africa is largely a function of poor jobs and low returns to self-employment. Reducing poverty will therefore require a growth process that is accompanied by more "decent jobs", created by improvements in labour productivity, rising wages and better work conditions. Given the low skill levels and productivity of Africa's labour force, addressing the poverty challenge in Africa will require measures to improve poor people's human capital and facilitate their access to the newly created employment opportunities. Other factors that limit poor people's access to employment opportunities include limited access to markets, gender discrimination, restrictive labour regulations and unequal distribution of assets, particularly land.

Because decent employment is a major route out of poverty, it should be placed at the heart of the poverty battle in Africa. This means that employment needs to be effectively mainstreamed in Africa's development programmes, including poverty reduction strategies. However, a 2004 review of the employment content of all full Poverty Reduction Strategy Papers in Africa, including the annual progress reports, found considerable scope for strengthening their employment content. Specifically, the analysis revealed that although most Poverty Reduction Strategy Papers address job creation through a variety of policies (for example, agriculture and rural development, credits and loans, and education and training), very few countries provide specific measures to counter the adverse employment effects of globalization, liberalization and privatization. Furthermore, while all the dimensions of decent employment (except work freedom) are reflected in most Poverty Reduction Strategy Papers, the degree to which decent employment is addressed varies considerably across countries.

Given the current jobless growth trend in Africa, the importance of decent employment to poverty reduction and policymakers' apparent failure to adequately reflect employment policies and programmes in their development plans, this report proposes measures that stimulate employment growth through the adoption of labour-friendly production technologies, improve productivity through human capital development and strengthen the employment focus of development programmes in Africa through the adoption of international best practices, among other strategies.

The poverty challenge in Africa

Africa faces the daunting challenge of lowering its high levels of poverty (see box 3.1 for poverty measures).[2] Unlike most regions of the world, poverty in Africa has been on the rise, despite an upward trend in the real growth rate over the last five years. Poverty in Africa is pervasive, intensive, chronic, gender-biased and largely a rural phenomenon. But most important, current forms of wage employment in Africa provide little refuge from poverty.

"Even with higher growth rates, poverty is on the rise"

Box 3.1
Definitions of poverty measures

Three different methods are generally employed to measure different aspects of poverty. They all refer to an income threshold, the so-called poverty line that separates the poor from the nonpoor. The interpretation of each measure is different, with the more sophisticated measures also more difficult to interpret.

Headcount ratio

The first and simplest measure of poverty is the headcount ratio—the ratio of people living below the poverty line to the total population. The headcount ratio gives a quick and easy-to-understand first look at the incidence of poverty. A discrete measure, it does not indicate the depth of poverty or the distribution of income below the poverty line. In particular, the headcount ratio remains unchanged even if all the poor get richer without anyone crossing the poverty line.

Poverty gap index

The poverty gap index measures the magnitude or depth of poverty. Expressed as a percentage of the poverty line, it is calculated as the poverty headcount ratio multiplied by the difference between the poverty line and the average income of the population living under the poverty line. The poverty gap index reflects some of the movements within the group of people living below the poverty line. However, it does not change when income is redistributed from the very poor to the less poor and all the poor stay below the poverty line.

Severity of poverty index

The severity of poverty index is calculated as the poverty headcount ratio multiplied by the squared difference between the income of a poor person and the poverty line, aggregated over all poor people. The severity of poverty index not only measures poverty and depth of poverty but also reflects the distributional effects of the people living below the poverty line. The headcount ratio and the poverty gap index, do not change when income is redistributed from the very poor to the less poor and all the poor stay below the poverty line. However, the severity of poverty index increases indicating that poverty has become more severe for the poorest. The severity of poverty index is more sensitive to the income changes of the poorest and less sensitive to the income changes of those living close to the poverty line. This mitigates the discrete nature of the poverty measures, especially the headcount ratio.

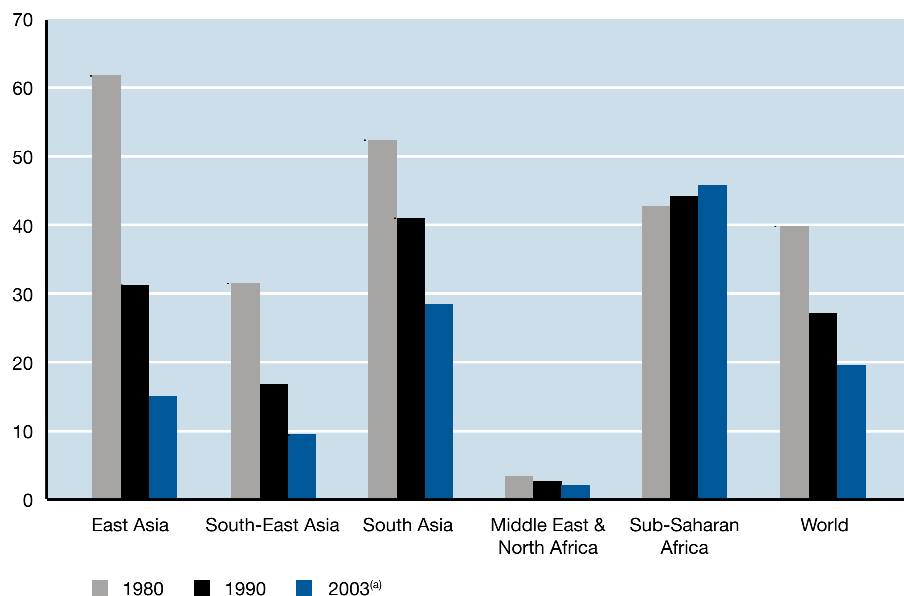
Source: *Ravallion 1992.*

Poverty is extensive, intensive and rising

Poverty (as measured by the headcount ratio) stagnated at high levels in Sub-Saharan Africa, while it declined in most parts of the world (Figure 3.1). In 2003 about 46 per cent of the Sub-Saharan Africa population lived on less than $1 a day—slightly more than in 1980 and 1990. At the global level, however, the share of the population living on $1 a day declined from 40 per cent in 1980 to 20 per cent in 2003. The $1 a day headcount ratio in Sub-Saharan Africa now exceeds the next poorest region, South Asia, by about 17 percentage points (ILO 2004c). Thus, while East, South-East and South Asia and North Africa are broadly on track to meet the Millennium Development Goal of halving poverty by 2015, there has been no progress in Sub-Saharan Africa towards achieving this goal (UN 2004).

Figure 3.1

$1 a day poverty headcount, by region, 1980–2003 (% of population)



Note: *$1 a day estimates are based on purchasing power parity.*

a. *Estimated.*

Source: *ILO 2004c.*

The poverty gap index in Sub-Saharan Africa was 20.5 per cent in 2001 after stagnating at a high level since the 1990s, when other regions succeeded in reducing their poverty gap index. In 2001 it was almost three times as high as in South Asia, the next most impoverished region (Table 3.1).

Table 3.1
Poverty gap index, by region, 1990–2001 (%)

	1990	1999	2001
East Asia	8.9	4.2	3.9
South-East Asia	3.8	2.0	1.7
South Asia	10.3	7.1	7.1
North Africa	0.5	0.3	0.3
Sub-Saharan Africa	19.5	18.6	20.5

Source: *UN 2004.*

Chronic and transient poverty

The share of people below the poverty line tells only part of the story. Many people in Africa are not only below the poverty line, but they are also chronically poor, remaining poor over time or only emerging briefly from poverty from time to time. Most chronically poor people live in South Asia, but the incidence of chronic poverty in Sub-Saharan Africa is the highest (Grant et al 2004).

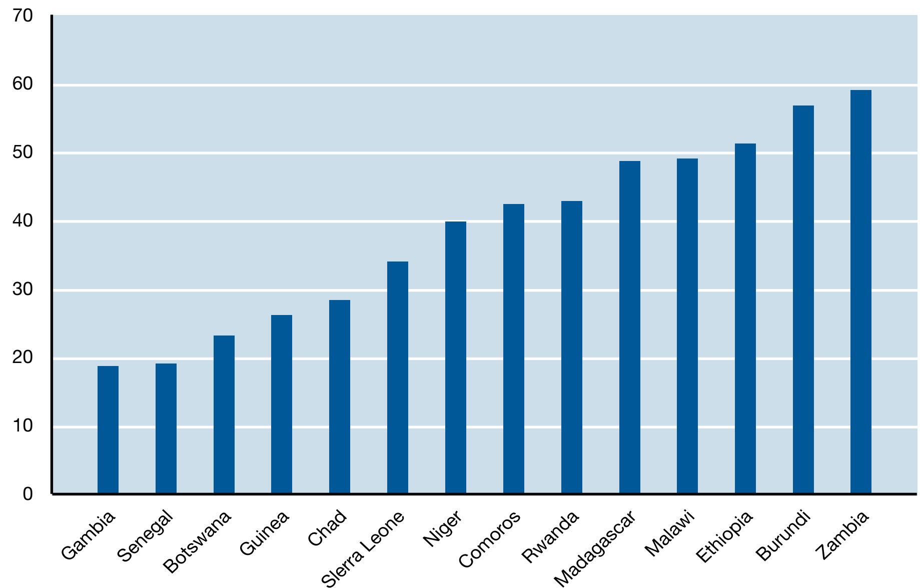
> *SSA has the highest incidence of chronic poverty in the world*

No directly comparable quantitative indicators of the incidence of chronic poverty exist for most African countries because they require longitudinal household data. Studies based on the few data sets of this nature indicate that the share of poor people who are chronically poor is substantial. In Ethiopia 25 per cent of urban households were found to be chronically poor in 1994–97. Similarly, 20.5 per cent of rural households and 10.2 per cent of urban households in Uganda were found to be poor in both 1992 and 1999 (Grant and others 2004).

Without precise data chronic poverty is usually estimated using such proxies as extreme poverty and indicators of long-term nutritional status, including prevalence of stunting. Defined as a height-for-age ratio that is significantly lower than the median for the corresponding age group, stunting is an indicator of sustained malnutrition, which is a sign of continued low-income levels (Grant and others 2004; Ravallion 1992). Using prevalence of stunting as an approximate measure of chronic poverty produces estimates that are close to those provided above. The prevalence of stunting for Sub-Saharan Africa countries was 40 per cent during the period 1992-2000. Countries with a high incidence of income poverty have a very high prevalence of stunting. Zambia leads the group, with a prevalence rate of 59 per cent, followed by Burundi with 56.8 per cent and Ethiopia with 51.2 per cent (Figure 3.2).

Many households experience transitory poverty in addition to chronic poverty. These households fall just above or just below the poverty line and tend to become poor when a climatic or economic shock hits; they tend to be pulled out of poverty once conditions improve. Transiently poor households are an important subgroup of poor households in African countries.

Figure 3.2
Stunting in Africa, 1999–2000 (% of children under age 5)



Source: *Grant and others 2004.*

Different interventions are needed to support the chronically poor and the transiently poor. For example, mechanisms that manage risk by smoothing income and consumption would benefit households falling in and out of poverty, but they would do relatively little for households far below the poverty line, which can only be improved by tackling the deep structural problems that keep them in severe poverty.

Income poverty and human capital

Poverty and its consequences are multidimensional and self-reinforcing. Poor people have low incomes and consumption, and many depend on low productivity subsistence agriculture or on the informal sector for their livelihoods. Informal sector wage-earning workers tend to have low salaries, limited protection and frequent bouts of unemployment. The poor are inadequately educated and less healthy than the rest of the population—deficiencies that prevent obtaining the capabilities needed for a fulfilling life (UNDP 2004).

In 2000 the average primary completion rate for Sub-Saharan Africa was slightly above 50 per cent, while the net enrolment rate was 61.2 per cent. To achieve universal primary education (Millennium Development Goal 2), Sub-Saharan Africa would need to register uninterrupted annual growth of 3.9 percentage points in net enrolment for the period 2000–10, but the average observed growth rate is much less (UNECA 2005). At the cur-

rent rate of progress only 10 countries from Sub-Saharan Africa and 3 from North Africa are likely to achieve universal primary education by 2015 (UNESCO 2002).

The possibility of halting the spread of HIV/AIDS is constrained by the low level (less than 50 per cent) of condom use in most African countries. Countries that have a high prevalence of condom use among men ages 15–24 may have a better chance of halting the spread of HIV/AIDS. Condom use in this age cohort was as high as 88 per cent in Botswana, 69 per cent in Zimbabwe and 62 per cent in Uganda during 1998–2001.

Ill health and long-term sickness (such as HIV/AIDS) are key contributors to poverty in Uganda. Declining levels of income are associated not only with the loss of wage income but also with the sale of assets such as livestock and land. The disposal of assets seems to be a major way for Uganda's poor to cope with economic shocks (Lawson 2004).

Poverty is intergenerational. Poor people often come from poor families, and their children are more likely to stay poor when they grow up. This applies to traditional income and consumption measures of poverty but also to broader nonincome dimensions. Children of poor people have limited access to schooling and health services, which reduces their future chances in the labour market. Furthermore, like their parents, it makes them part of a politically and socially marginalized class. Higher education in Africa mostly benefits upper-class children, who tend to live in urban areas and whose parents have above average levels of education (Schultz 2004).

> *"The poor cope by disposing of assets: livestock and land"*

Poverty is not gender neutral

Gender differences are ingrained in the social, economic and political patterns of African societies. They manifest themselves in access to and control of productive assets, such as credit, land and education. Furthermore, women are more likely to be restricted in their

Table 3.2
Female literacy, income and government employment, by country, 2001 and 2002

Country	Adult female literacy rate, 2002 (% of male rate)	Estimated earned female income PPP US$, 2002 (% of male income)	Women in government at ministerial level, 2001 (% of total)
Benin	47	69.1	10.5
Ghana	80	74.5	8.6
Kenya	87	90.7	1.4
Morocco	61	40.2	4.9
Senegal	61	55.0	15.6
South Africa	98	44.9	38.1
Uganda	75	65.9	27.1

Source: *UNDP 2004.*

access to product and labour markets. These inequalities result in a higher incidence of poverty among women—often accompanied by rising poverty among children and invariably lower health and educational outcomes (World Bank 2001).

Literacy is lower among women than men

Literacy is lower among women than among men (table 3.2). Education of women has a significant impact on their bargaining power within the household and thus on resource allocation and their chances in the formal labour market.

Educated women tend to have more economic leverage, which can positively influence the nutrition and education levels of their female offspring (Duncan 1991). Differences in bargaining power also partly explain the important variations in the consumption patterns of men and women living in the same household. Women tend to spend more on daily household consumption, such as food, healthcare and clothing. Men spend more on personal consumption, luxury goods (alcohol and tobacco), household maintenance and social investments (Smith 1994).

Having less education also makes women more likely to be involved in unstable and low-paying jobs and economic activities, which translates into significantly lower incomes for women in all countries. The picture is not any better for women's political influence: women are substantially underrepresented in public service employment, limiting their chances to introduce, promote and defend gender-sensitive policies (World Bank 2001).

Spatial dimension—the rural-urban divide

Poverty in Africa has been described as mostly a rural phenomenon not only because the majority of the population live in rural areas but also because of the distribution of economic activity between rural and urban areas. In Africa rural-urban differentials in incidence of poverty are large and persistent (figure 3.3).

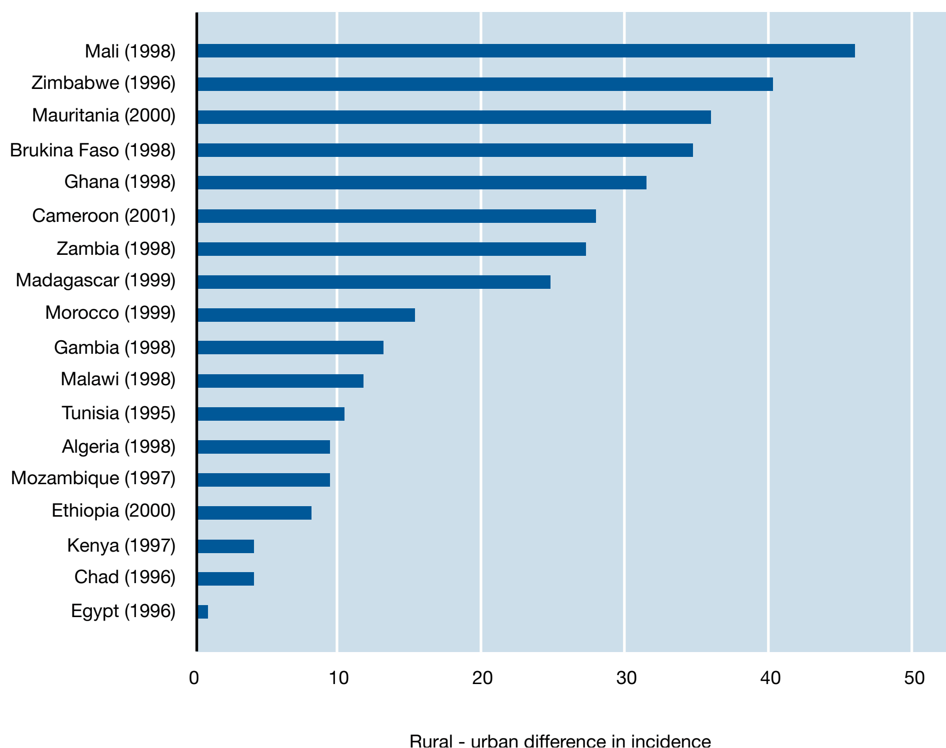
Using national poverty lines, the mean difference between incidence rates in urban and rural areas was 19.6 percentage points during 1995–2000. There are large intercountry differences in rural-urban differentials, ranging from 0.8 percentage points in Egypt in 1996 to 45.8 percentage points in Mali in 1998, 40.1 percentage points in Zimbabwe in 1996 and 35.8 percentage points in Mauritania in 2000. Rural-urban differentials are generally high regardless of the overall level of incidence rates.

Observed rural-urban differentials in poverty tend to be persistent. In Cameroon, for instance, the incidence of poverty in urban areas (using the national poverty line) was halved in only five years—from 41.4 per cent in 1996 to 22.1 per cent in 2001. The corresponding change in incidence rates in rural areas (from 59.6 per cent to 49.6 per cent), though commendable by African standards, was significantly lower than the change in urban areas (World Bank 2004b).

When rural-urban differentials have declined, it has been because of a sharp hike in the incidence of poverty in urban areas rather than improvements in rural areas. In Kenya the rural-urban differential declined from 18 percentage points in 1994 to four in 1997—but

urban poverty increased by a staggering 20 percentage points while rural poverty increased by only five. Similarly, a decline of about 9 percentage points was observed in Zambia between 1996 and 1998 as a result of a 10 percentage point rise in urban poverty, while rural poverty remained at a very high level of about 83 per cent. In Zimbabwe rural-urban differences increased as a result of sharper increases in rural poverty (World Bank 2004b).

Figure 3.3
Rural-urban differentials, by country, various years (percentage points)



Note: *Data are from household surveys, which were not conducted in the same years in every country. Data refer to national (urban, rural and total) poverty lines.*

Source: *World Bank 2004b.*

Working poverty is widespread in Africa

When the incidence of poverty is so high that two-thirds of a country's population are poor, the poor population will likely include workers whose incomes are so low that they cannot provide their families a decent standard of living. Estimates of working poverty in 2003 show that about 56 per cent of workers in Sub-Saharan Africa earn incomes that do not allow them and their families to reach the consumption level of $1 a day per person (Table 3.3). Only 11 per cent of the working population earn incomes above the $2 a day

poverty line. As with overall poverty, working poverty has been declining continuously in most regions of the world, and the incidence of $1 a day working poverty worldwide in 2003 was half its 1980 level. By contrast, in SSA, working poverty stagnated during the same period, making it the sub-region with the highest incidence of poverty on the continent in 2003 (ILO 2004c).

Table 3.3
Working poverty shares in total employment, by region, 1980–2003

Region	$1 a day poverty			$2 a day poverty		
	1980	1990	2003[a]	1980	1990	2003[a]
East Asia	71.1	35.9	17.0	92.0	79.1	49.2
South-East Asia	37.6	19.9	11.3	73.4	69.1	58.8
South Asia	64.7	53.0	38.1	95.5	93.1	87.5
Middle East and North Africa	5.0	3.9	2.9	40.3	33.9	30.4
Sub-Saharan Africa	53.4	55.8	55.8	85.5	89.1	89.0
World	40.3	27.5	19.7	59.8	57.2	49.7

Note: *$1 and $2 a day estimates are based on purchasing power parity.*

a. *Estimated.*

Source: *ILO 2004c.*

"Despite rising real GDP growth, employment is stagnant"

Decent employment as a major route out of poverty in Africa

Real GDP growth in Africa has generally been on an upward trend since the late 1990s. However, economic growth has neither been associated with a decline in poverty nor an increase in employment. On the contrary, poverty has increased, while employment growth has been virtually stagnant. Empirical evidence nevertheless shows that growth does not necessarily lead to poverty reduction. Indeed, the pattern and sources of growth as well as the manner in which its benefits are distributed are critically important.

This section shows that reducing the incidence of working poverty is critical to reducing poverty because unemployment is not an option for the majority of poor people. It argues that low returns to labour, particularly due to underemployment and low productivity, are the cause of poverty among workers. Furthermore, it shows how employment-intensive growth reduces poverty through the widespread adoption of labour-intensive technologies. Finally, it discusses measures to help poor people capitalize on the benefits of an employment-intensive growth process.

The importance of labour markets in poverty reduction

The impact of employment growth on poverty reduction depends on the extent to which the poor derive their livelihoods, directly or indirectly, from the labour market. Thus, to understand why employment is critical to poverty reduction, it is useful to start by analyzing the key sources of livelihood for poor people. From there, one can distinguish poor people in the labour market from those outside the labour market.

To survive outside the labour market poor people need to be supported by either formal social insurance mechanisms or informal social networks. Because most African countries lack formal social insurance schemes, however, most poor people are employed, underemployed or dependent on employed people through informal social networks for their livelihood. Thus, even people outside the labour market tend to be dependent on individuals in the labour market. In effect, labour markets are central to the livelihoods of poor people in Africa both in and outside of the labour force.

Both self-employed and wage-earning workers tend to be poor because of low returns to their labour. Wage earners may suffer from low returns because they are underemployed or because they receive low wages despite full employment. Underemployment can result from the inability to find a full-time job (open underemployment) or from working full-time but at low intensity (disguised underemployment). Open underemployment is observed more in the informal sector, which acts as a refuge for surplus labour in Africa, while disguised underemployed is observed more in the formal sector, especially the public sector. Full-time workers may also receive low wages due to excess supply of labour relative to vacancies, low productivity or adverse terms of trade (Osmani 2003).

The significance of low returns to labour as a cause of poverty suggests that to reduce poverty, employment-intensive growth must be associated with an increase in the returns to labour. This in turn requires increasing the productivity of labour. However, there is a tradeoff between employment growth and productivity growth: the rate of employment growth declines as productivity rises. For instance, evidence from Ethiopia shows that labour productivity declined in the sectors for which employment growth exceeded the rate of growth of output (that is, where employment elasticities were greater than 1) (Demeke, Guta and Ferede 2003). Therefore, the policy challenge is to minimize the decline in employment growth associated with rising labour productivity by choosing appropriate technologies and investing in complementary factors of production.

The mere availability of good jobs will not necessarily reduce poverty unless poor people can capitalize on the employment opportunities, so decent job creation must be complemented by measures to ensure that poor people benefit from newly created jobs. The impact of growth on poverty reduction depends on two main factors:

- The degree of employment intensity (defined in terms of quantity and quality of employment) of the growth process.

- The ability of the poor to integrate into the growth process and benefit from the employment opportunities created.

Demand-side factors: employment intensity is the key link between growth and poverty

Employment-intensive growth benefits poor people by creating strong demand for their services. Hence, this section examines the conditions that generate strong and sustainable employment opportunities for poor people. These conditions are likely when poor people are disproportionately represented in sectors characterized by strong domestic and external demand and when the technologies adopted by these sectors are largely labour-intensive (Osmani 2003). In addition, the total number of jobs created as a result of increased demand is likely to be higher when the economy has strong intersectoral linkages. Finally, the source of growth also matters. Whether job growth emanates largely from the public or private sector will affect the quality and quantity of jobs created. Following the conceptualization in Osmani (ibid), the employment intensity of growth depends on:

- Which sectors are experiencing growth.
- The choice of technology in the growing sectors.
- Trends in the commodity terms of trade.
- The extent to which labour benefits from higher terms of trade.
- The presence of strong intersectoral linkages within the economy.
- Whether growth is driven by the public or private sector.

There is failure in employment-friendly investment

Sectoral composition of growth. The impact of economic growth on employment depends on which sectors lead the growth process. When growth is spurred by labour-intensive sectors that employ a significant share of the labour force, such as smallholder agriculture, the growth's effect on employment and poverty is greater than when growth is concentrated in capital-intensive sectors such as mining.

In Ethiopia, for example, relatively slow growth in the labour-intensive agricultural sector accounted in part for the limited impact of growth on employment in the post- reform years of the 1990s. Agriculture grew by only 1.9 per cent, while manufacturing, which is largely capital-intensive, grew by 5 per cent a year over 1992/93–1999/2000. However, improvements in productivity and wages in the manufacturing sector had a limited impact on overall employment and poverty because the sector accounted for only 4.4 per cent of wage employment in 1999 compared with 79.6 per cent for agriculture (Demeke, Guta and Ferede 2003). In Uganda, by contrast, high growth in the labour-intensive agricultural sector contributed to a decline in unemployment—from 56 per cent in 1992 to 35 per cent in 2000. About half the poverty reduction between 1992 and 1995/96 can be attributed to higher earnings and wages for farmers (Appleton 1999).

Choice of technology. The impact of economic growth on employment and labour productivity growth also depends on the extent to which the economy consciously adopts labour-friendly techniques across all sectors. Unfortunately, policymakers in many African countries have

in the past favoured capital-intensive techniques or failed to promote employment-friendly technologies in all sectors (see chapter 2).

Kenya, for example, used tractors and heavy-duty machines instead of less mechanized techniques such as ox-drawn ploughs and hand tools in the agricultural sector during the 1980s (Khan 1997). Large machines were exempt from import duty and sales taxes and classified in the less restrictive import category, while ploughs and hand tools were subject to high import duty and the most restrictive import category. These policies have displaced labour from large farms and discouraged small farms, which are more productive and labour-intensive. Therefore, it is necessary to promote technologies that maximize employment without unduly compromising productivity. In the agricultural sector, for instance, ensuring access to basic inputs such as seeds and fertilizer, infrastructure such as roads and irrigation, and research and development through extension services can have a favourable impact on productivity.

In Mozambique failure to promote labour intensity in either the composition of output across sectors or the choice of technology within sectors is undermining the country's ability to reduce poverty despite high economic growth (box 3.2).

Box 3.2
Will Mozambique's "mega projects" deliver jobs and reduce poverty?

The key objectives of Mozambique's poverty reduction strategy are to grow by an average annual rate of 8 per cent and to reduce the poverty rate from 70 to 50 per cent by 2010. To achieve these objectives, the strategy has a pipeline of mega projects with projected investments of about $10 billion, or almost 2.5 times current GDP. These large projects have generated interest among foreign investors and will help Mozambique reach its growth objective by increasing manufacturing output and exports.

However, these mega projects might not be sufficient for Mozambique to meet its poverty reduction objective. A review of the projects shows that they will not create enough jobs: the projected $10 billion mega projects investment would generate only about 20,000 jobs—only 5,000 of them directly within the companies involved and the remaining 15,000 among suppliers and services providers. Because 3.7 million new job seekers are expected in Mozambique's labour market by 2010, the 20,000 jobs to be created through the mega projects would absorb less than 1 per cent of these new job seekers. In addition, each job created by the mega projects would cost $1–$2 million in initial investment compared with an average capital per worker of $15,000 in existing firms, meaning that with the same amount of investment funds the average existing firm in Mozambique could create about 100 times as many jobs as the mega project.

Source: *Nasir et al 2003.*

> *Mozambique will have 3.7 million new jobseekers by 2010*

Terms of trade. Another factor that affects the employment intensity of growth is the terms of trade. Favourable external terms of trade in labour-intensive sectors will improve the

performance of these sectors and consequently improve the quality and quantity of employment. Uganda's high agricultural growth was driven by favourable trends in the terms of trade in general and the prices of cash crops in particular. Coffee, for example, benefited from the boom in prices in the world market. The export price of coffee rose from $0.86 per kilogram in 1991/92 to $2.55 in 1994/95 (Demeke, Guta and Ferede 2003).

However, improvements in terms of trade have not generally been a sustainable source of growth due the volatility of commodity prices over the years. Many Sub-Saharan Africa countries have experienced sharp declines in the terms of trade of many of their primary commodities, which decreased or reversed previous gains from exports. This has decreased employment opportunities and reduced returns to the labour force engaged in the production of these commodities. To reduce exposure to commodity price shocks, exporters must be encouraged to diversify production either by increasing their range of exportable commodities or by producing a mix of commodities for both local and foreign markets.

Price structure. Improvements in the terms of trade will translate into higher returns to labour and improve the livelihood of workers only if the benefits are passed on to producers. This was the case in Uganda, where producer prices as a share of the world price of coffee, increased by at least 50 per cent between 1991 and 1997 thanks to a more liberalized marketing regime. Unfortunately, many African countries have a long tradition of subjecting agricultural exports to low producer prices (IFAD 1992). Low ratios of producer prices to export prices for major agricultural exports reflect an implicit tax on agricultural exports, which constrains productivity and therefore discourages production and employment. Promoting exports and enhancing the livelihoods of cash crop farmers therefore require policymakers to minimize the implicit tax on producer prices.

Intersectoral linkages. The employment-generating effects of growth are more likely to be magnified in economies characterized by strong intersectoral linkages because these links create jobs both directly and indirectly by stimulating demand in related sectors of the economy. For instance, promoting agroindustries is likely to create additional jobs both within and outside the agricultural sector by stimulating the demand for agricultural commodities to feed the agroindustries and by increasing the demand for workers to staff the agroindustries.

Growth led by the public sector or the private sector. The quality and quantity of jobs created through growth will be influenced by the the public and private sectors' roles in driving the growth process. Globally, government employment has been negatively associated with wages and positively associated with fiscal deficit and per capita income. Indeed, the global results stem almost entirely from strong results for Africa and Latin America (Schiavo-Campo, de Tommaso and Mukherjee 1999). Sustainable employment growth will therefore require credible reforms aimed at improving the overall efficiency of the public sector to ensure that job growth is associated with rising productivity. Indeed, when public enterprises are overstaffed, increasing productivity may require downsizing, at least in the short run, which conflicts with the objective of reducing poverty. Minimizing the adverse effects of job losses that may accompany public sector reforms will require employment-intensive growth in the private sector to absorb displaced workers in the public sector. In addition, social safety nets will be required to cushion workers who fail to gain employment in the private sector.

Supply-side factors: poor people's ability to take full advantage of the jobs created

Even a combination of rapid growth and high employment expansion does not guarantee poverty reduction if poor people's capabilities do not match those required by the job opportunities generated and if poor people face barriers to entry into the labour markets either as wage earners or entrepreneurs. So, from the supply side the key factor is poor people's ability to integrate into the growth process, specifically gaining access to the jobs that are created. This is termed the integrating factor by Osmani (2003). The factors that limit access to employment opportunities by the poor include:

- Lack of human capital.
- Limited market access.
- Restrictive labour regulations.
- Gender discrimination.
- Limited access to assets (Osmani ibid)

Human capital. Human capital, broadly defined, has several aspects, including education and health. Modern growth theory suggests that human capital, including health and education, has a strong impact on economic growth and poverty reduction by improving poor people's chances of securing a job, raising the productivity and earnings of the working poor and increasing the efficiency of entrepreneurs.

"Human capital strongly impacts poverty reduction"

The education component of human capital can be acquired through formal education or through vocational and skills training acquired either on or off the job. Several studies confirm the productivity-enhancing effect of human capital, but some suggest a more nuanced relationship between human capital and productivity. Pritchett and Filmer (1997) identify several conditions under which human capital, as measured by years of schooling, will have no impact on the growth rate of output per worker. First, schooling will not necessarily create human capital if it does not raise cognitive skills or productivity. Hence, the process of human capital acquisition is important; formal education must be relevant to the workplace if it is to translate into increased productivity. Moreover, when the skills acquired by the labour force are inconsistent with the requirements of employers, structural unemployment results.

Second, increasing the supply of educated workers may not increase wages or productivity if the demand for workers is stagnant due to a recession or a shift to labour-saving technologies. Therefore, human capital development must be associated with employment-intensive growth to reduce poverty.

Finally, the productivity of a skilled labour force is likely to be compromised in bureaucratic, overstaffed and generally inefficient institutions—for example, state enterprises in countries where government is the employer of last resort. Thus, the source of employment

growth matters because it influences the productivity of labour and the sustainability of employment growth.

Improving poor people's human capital will require investments in health as well as education because health is an important determinant of productivity. Furthermore, health and education are interrelated: poor people may experience low levels of education due to poor health, and the low health status of the poor may, in turn, be explained by their inability to access health services because low educational attainments compromise their employment and earnings potential. The absence of financially sustainable safety nets such as health insurance programmes and the adoption of cost-recovery pricing measures in several developing countries have left poor people out of health delivery systems. Furthermore, the growing prevalence of HIV/AIDS in Africa has diverted resources from other health services normally provided by governments and contributed to the lack of adequate resources for health-related infrastructure and subsidies. Indeed, in high prevalence countries HIV/AIDS has reduced GDP by an estimated 0.9 per cent (ILO 2004b).

Market access. Improving access to markets is critical to ensuring that poor entrepreneurs capitalize on the benefits (such as increased consumer demand) of employment-intensive growth. Constraints to market access can result from a lack of infrastructure (for example, feeder roads and bridges) or the presence of institutional barriers (restrictive rules and regulations governing market access) and oligopolistic marketing structures that limit access to favoured groups (for example, the phenomenon of market queens in Ghana).

Labour regulations. Improving access to formal wage employment by ensuring that labour regulations do not unduly restrict entry to labour markets will improve the employment opportunities of the poor. Avoiding the so-called "insider-outsider" problem, for example, is critical for poor job seekers. Labour regulations may create asymmetric power between insiders (people already in the formal sector) and outsiders (people seeking entry into the formal sector) (Lindbeck and Snower 1989). In this case, the outsiders, who are more likely to be poor, are effectively prevented from entering the formal sector, and growth benefits the insiders through higher returns to labour (Osmani 2003).

Gender. Gender discrimination limits women's access to productive assets such as land and consequently constrains their options for engaging in sustainable livelihood activities. A study of the influence of rural institutions in determining access and returns on primary assets in Cameroon found that land inheritance is gender biased because women have only user rights not ownership rights to the land (Baye 2002).

Another aspect of gender discrimination in employment is defining certain types of jobs by gender, a form of cultural stereotyping. This is relevant in much of Africa, where cash crops are often identified as men's crops and subsistence food crops as women's crops. Because of this gender pattern of crop production, women hardly benefited from the increased employment potential of the cash crop sector following trade liberalization and greater commercialization. Given that women constitute a predominant share of poor people, the poverty-reducing impact of this agricultural boost is limited. Formulating policies that address the disadvantages suffered by females in the labour market should therefore be a critical step in minimizing the incidence of poverty among women.

Distribution of assets. Asset inequality plays a significant intervening role in the growth-poverty nexus. High inequalities reflect differences in access to public endowments (such as infrastructure, education and health facilities) and private endowments (such as land and capital) in African societies. In turn, limited access to both types of endowments reinforces intergenerational poverty and prevents poor people from sharing in the limited wealth generated on the continent.

Informational asymmetries in the formal credit market, for example, often lead to credit rationing that discriminates against poor people who lack assets. Poor entrepreneurs are compelled to pay exorbitant interest rates in the informal market and are consequently unable to take advantage of increasing economic opportunities generated by a growing economy (Osmani ibid).

Land distribution also determines the extent to which growth in agriculture translates into higher earnings for workers in the sector. When land distribution is highly unequal, the benefits of the growth process might be captured by only a few large landholders, with no impact on the employment and wages of the many workers in the sector. By contrast, when land distribution is relatively egalitarian, many smallholders can benefit from the growth process. In Uganda, for example, growth in the 1990s benefited a large segment of coffee producers because smallholders dominate the sector. By contrast, the poverty-reducing impact of the boom in the tea sector was not as great because the sector is dominated by large estates. Analysis of panel data on rural communities in Ethiopia also reveals that households with favourable access to infrastructure and arable land escaped poverty, while those that did not remained poor or fell into poverty (Dercon 2002).

The PRSPs tackle the surface of employment only

The experiences of African countries in the 1990s show that nations with low initial levels of inequality are more likely to experience declines in poverty (Christiansen, Demery and Paternostro 2002) than those with relatively high initial conditions of inequality. Analysis of a sample of Sub-Saharan Africa countries also shows that the rate at which income growth is transformed into a reduction in poverty decreases with the level of inequality. Depending on the level of inequality in a given country, the reduction in headcount poverty after a 10 per cent increase in real growth varies from as high as 7 per cent to as low as 0.2 per cent (Fosu 2005).

Strengthening the employment content of Poverty Reduction Strategy Papers

Because decent employment is a major route out of poverty, it should be at the heart of the poverty battle in Africa. Consequently, decent employment must be mainstreamed in the development strategies of African countries to be successfully translated into action.

This section presents the main findings of an analysis undertaken by the United Nations Economic Commission for Africa on the employment content of one subset of the development strategies: Poverty Reduction Strategy Papers (PRSPs). A very influential poverty reduction instrument at the moment, PRSPs are linked to aid and debt relief and are used by many African countries. As of October 2004, 21 African countries had full PRSPs and

nine had interim PRSPs. The analysis here focuses on the full PRSPs and their respective annual progress reports. The analysis assesses only the degree to which decent employment is reflected in the PRSPs documents, not whether the employment goals are translated into action.

The overall employment content of the full PRSPs is weak

Of the 21 countries with a full PRSP, 17 have an identifiable core section on employment. The absence of an employment section in the other four countries' PRSPs, however, is not necessarily indicative of weak employment content. The assessment of the employment content is based on the extent to which employment issues are reflected in all the sections of the PRSP.

Table 3.4 lists the countries in Africa with a full PRSP by the employment content of their poverty reduction strategies, which is expressed as a share of the positive answers to a set of 116 questions covering diagnosis of the employment situation; policies for creating employment opportunities; policies for improving decent employment; group, regional and sectoral targeting for employment purposes; and quantification of the impacts of policies on the different dimensions of employment. The questions analyze only the explicit employment content of the PRSPs and do not assess the intensity of the effect of the employment policies. The questions do not assess implementation issues, either.

Table 3.4
Breakdown of the 21 full PRSPs in Africa by employment content (share of positive answers to employment-related questions)

Low (0%–33%)	Medium-low (34%–50%)	Medium-high (51%–66%)	High (67%–100%)
Chad	Benin	Tanzania	
The Gambia	Burkina Faso		
Guinea	Cameroon		
Mauritania	Djibouti		
Mozambique	Ethiopia		
Niger	Ghana		
Senegal	Kenya		
	Madagascar		
	Malawi		
	Mali		
	Rwanda		
	Uganda		
	Zambia		

Source: *ECA, based on Benin 2002; Burkina Faso 2000, 2001, 2002, 2003; Cameroon 2003; Chad 2003; Djibouti 2004; Ethiopia 2002, 2003; Gambia 2002; Ghana 2003, 2004; Guinea 2002; Kenya 2004; Madagascar 2003, 2004; Malawi 2002, 2003; Mali 2002, 2004; Mauritania 2000, 2002, 2003; Mozambique 2001, 2003; Niger 2002, 2003; Rwanda 2002, 2003; Senegal 2002; Tanzania 2000, 2001, 2003, 2004, Uganda 2000, 2001, 2002, 2003; Zambia 2002.*

None of the 21 countries had a high employment content, and only Tanzania, at the top of the ranking, had a rating above 50 per cent. Most of the full PRSPs have either medium-low or low employment content, leading to the conclusion that the overall employment content of the full PRSPs is weak. The rest of this section discusses the specific areas that are stronger and weaker in terms of employment content.

Certain policies are used by most PRSPs to encourage the creation of employment opportunities

To encourage the creation of employment opportunities—including generation of new jobs and enhancement of employability— at least two-thirds of the 21 full PRSPs adopted the following policy measures: improved access to education and training, increased access to credit and loans, infrastructure investment, private sector development, agriculture and rural development, and institutional capacity building. However, the degree to which each of these policies address the creation of employment opportunities differs considerably across countries.

Access to training and education as well as credit and loans constitute an important means of increasing people's employability (see below). Training policy is explicitly linked to employment opportunities by all 21 countries. Examples of specific actions to enhance employability through training policy include developing new technical education and vocational training programmes consistent with labour market demand (Benin), creating an employment and vocational training observatory to improve knowledge about the labour market (Burkina Faso), strengthening training centres to encourage self-employment and to create a pool of qualified workers (Burkina Faso), building vocational guidance and counselling systems to facilitate access to available job opportunities (Gambia) and creating demand-driven skills programmes for employment promotion (Tanzania). Fifteen of the 21 countries explicitly link education policy to the generation of employment opportunities, while a similar proportion addresses the generation of employment opportunities through provision of credit and loans (microfinance and microcredit instruments).

Infrastructure investment is one of the most powerful instruments for creating employment and reducing poverty (Calderón and Servén 2004). All 21 countries address the creation of employment opportunities through infrastructure investment either directly (by recruiting workers for infrastructure investment projects) or indirectly (by generating economic activity and hence increasing labour demand). In most cases the infrastructure investment linked to employment is road construction and rehabilitation. Labour-intensive infrastructure investments are often used to generate employment. For instance, in Rwanda labour-intensive public works are one of the main policies for creating jobs (box 3.3).

Twenty of the 21 countries refer to private sector development as an instrument for job creation. And 17 countries explicitly address job creation through the development of small and medium-size enterprises—said to be the subsector of the private sector with the most potential to create jobs (see chapter 7). However, one crucial aspect of private sector–led job creation is rarely mentioned in the PRSPs: reducing and simplifying business regulations

Box 3.3
The importance of labour-intensive public works for creating jobs in Rwanda

Labour-intensive public works are one of the main policies for promoting employment in Rwanda's PRSP. Its goal captures the importance of this policy: "Every sector of government needs to seek opportunities for labour-intensive methods of carrying out their objectives." Promoting labour-intensive public works in Rwanda requires a multisectoral approach in several areas:

- Roads infrastructure.
- Roads and bridges maintenance.
- Agricultural infrastructure.
- Environmental infrastructure (agroforestry, reforestation, soil and water management).
- Water supply.
- Schools and health infrastructure.
- Labour-intensive programmes in urban areas.
- Labour-intensive rural public works programme.

Source: *Rwanda 2002.*

and administrative procedures (see chapter 7). Only the PRSPs of Cameroon, Djibouti and Mozambique consider this an important instrument for generating employment.

Agricultural and rural development's direct and indirect links make it very important for employment creation (see chapter 4). All 21 PRSPs rely on agricultural and rural development to create employment opportunities. For Burkina Faso, for example, agricultural and rural development is the main channel for expanding employment. The actions are very diverse: developing activities in the informal economy primarily related to agriculture, livestock and crafts (Cameroon), developing forestry management (Chad), enhancing the role of regional markets for exporting livestock (Djibouti), electrifying rural areas and developing rural off-farm activities (Ethiopia), using labour-intensive agricultural technologies (Ghana), developing small and medium-size enterprises and promoting microprojects in rural areas (Mali) and supporting labour-intensive agroprocessing in the rural sector (Tanzania), to name a few.

Generating employment opportunities depends not only on the existence of adequate policies, but also to a large extent on the existence of strong institutions capable of managing change with regard to employment issues and playing an intermediary role between supply and demand for labour (ILO with others 2004). Eighteen of the 21 countries with

a full PRSP address employment creation through measures related to institutional capacity building. Tanzania is a best-practice case (box 3.4). However, one important aspect of institutional development for employment creation that is addressed in only about half of the PRSPs is the development and improvement of the labour market information system (ILO with others 2004).

Box 3.4
Tanzania's institutional capacity building actions for creating employment opportunities

- Tanzania's poverty reduction strategy contains a wide range of actions to create employment opportunities through institutional capacity building:
- Establishing a Labour Exchange Centre in the capital and Labour Exchange Offices in each region to facilitate the matching of skills of job seekers with job qualifications.
- Upgrading the employment section of the Department of Labour to a full-fledged division on employment with qualified staff and working facilities.
- Revising employment laws, labour relations and dispute prevention and settlement sections of the regulatory framework to create an enabling environment for creating jobs.
- Finalizing the National Employment Policy and creating a Country Action Programme for Employment Promotion under the PRSP process.
- Launching employment study reports and translating, disseminating and mainstreaming them into priority sectors for employment creation.

Sources: *Tanzania 2000, 2001, 2003, 2004.*

Some policies with important potential effects on employment are disregarded in most PRSPs

Some policies that can have important effects on employment—even though they may not be explicitly linked to employment—are disregarded by more than half of the PRSPs: delivery and management of community services; environment protection and management; health, global and regional integration; land access and security; liberalization and privatization; macroeconomic policy; and polices related to population growth.

Macroeconomic policy has enormous potential for creating employment opportunities. Employment-friendly macroeconomic policies facilitate growth of employment-intensive manufactures; develop employment-friendly and long-run growth-oriented public investments framework; manage public sector wages to develop human capacity in public services delivery and to ensure an employment-friendly industrial relations environment; provide

tax incentives for investment projects with low investment cost per domestic employee; avoid raising taxes on workers' incomes; and concentrate on expanding tax coverage to property (ILO and UNECA 2004). Nevertheless, only seven of the 21 countries with a full PRSP have a macroeconomic policy that is directly and explicitly linked to employment generation.

Policies related to global and regional integration have many and sometimes severe implications for employment (see chapter 6). Nevertheless, these implications are not examined in most PRSPs. Only 8 of the 21 countries link these policies to employment opportunities, and some countries do not even include global and regional integration policies in their PRSPs. The most serious concern regarding global and regional integration policies is that they are hardly linked to their potential short-term adverse effects on employment. Tanzania and Zambia are the only countries that make a brief reference to these effects. Moreover, none of the PRSPs contain specific measures to mitigate these short-term adverse effects. Even though many PRSPs contain some policies, such as training and social security, that can mitigate the adverse consequences of global and regional integration, these policies are not connected explicitly to this particular goal. Although limited, the scope of national policymaking to mitigate the adverse effects of trade liberalization on employment is considerable (Fosu 2004). National policymakers can reduce labour mobility costs from the importable sector to the exportable sector and can increase the elasticity of labour demand in the exportable sector (see chapter 6).

The potential short-term adverse employment effects of liberalization[3] and privatization policies, as well as the actions to mitigate these adverse effects, are also poorly reflected in the PRSPs. The record, though, is slightly better than in the case of global and regional integration. Eight of the 21 countries mention either the positive or negative effects of liberalization and privatization on employment opportunities. Of these eight countries, six acknowledge the adverse effects on employment of liberalization and privatization policies, and four contain actions specifically meant to mitigate the adverse effects of these two policies. These mitigating actions are microprojects targeting the socioprofessional reintegration of laid-off workers (Burkina Faso), development of the informal sector because of its provision of alternative employment opportunities (Ghana), training and job search programmes (Zambia), retrenchment costs paid by the government to miners (Zambia) and social protection strategy by the Ministry of Gender, Labor and Social Development (Uganda).

Policies related to population growth are another example of policies with important employment effects that are disregarded in the PRSPs. Africa is expected to experience a rapid increase in the supply of labour, which will increase unemployment (see chapter 4). In this context, policies that control the fertility rate and promote the increase of job opportunities become necessary. However, only five PRSPs contain these types of policies, and some do not even include a section on population growth. A few mention the relationship between population growth and unemployment—but only from an analytical point of view, without any explicit reference to their intentions to address the problem.

There is scope for improving decent employment aspects in the PRSPs

So far the analysis has centred on the quantitative dimension of employment. But employment has a qualitative dimension called decent employment, which involves productivity, equity, security, dignity and freedom. The qualitative dimension, especially the productivity aspect, cannot be disregarded in African PRSPs. Generally speaking, decent employment can be better reflected in the PRSPs.

The productivity dimension of decent employment refers to increased output per worker and earnings above the poverty threshold. All 21 PRSPs contain goals or actions to improve the productivity dimension of decent employment. However, the degree to which work productivity is addressed differs significantly across countries. Ghana emphasizes this dimension the most (see box 3.5).

Box 3.5

Ghana's PRSP emphasizes the productivity dimension of decent employment

Unlike the PRSPs of most of African countries, Ghana's PRSP strongly emphasizes the productivity aspect of decent employment: "The national employment policy framework is aimed at creating an enabling environment for accelerated growth and employment. A second objective is to create adequate wage and self-employment opportunities for entrants into the labor market." Furthermore, Ghana's PRSP has a comprehensive set of policies explicitly aimed at enhancing productivity, including:

- Providing training to the self-employed and other informal sector workers.
- Improving the infrastructure, marketing and provision of extension services in the agricultural sector.
- Promoting the use of information and communication technology in the agricultural sector.
- Supporting the development of electronic commerce.
- Providing microfinance for small and medium-size enterprises and rural activities.
- Strengthening the Management Development and Productivity Institute.

Source: *Ghana 2003.*

Equity, security and dignity are the three dimensions of decent employment addressed by most of the PRSPs. However, as in the case of productivity, the degree to which these dimensions are addressed varies across countries and is minimal in some PRSPs. The PRSP of Mali, however, adequately covers these three dimensions (box 3.6). The freedom dimension of decent employment refers to the absence of forced labour and the freedom to join organizations. Unlike the other dimensions of decent employment, the freedom dimension is covered by only a few countries' PRSPs. And even these countries focus only on reducing the prevalence of child labour.

Box 3.6
Work equity, security and dignity in Mali's PRSP

Mali's PRSP clearly emphasizes the need to promote decent employment. In addition, it covers all the dimensions of decent employment, except the freedom dimension.

Equity

With respect to equity the PRSP states that: "Equal opportunity of access to employment, in particular between men and women, will be sought through all employment initiatives."

Security

The PRSP has the following general objectives: "Implementation of specific action programmes aimed at encouraging enterprises to provide better job opportunities and at increasing the incomes of the poorest people, or their protection from social risks." Moreover, the PRSP promotes the development of social security systems (including protection against contingencies such as work-based accidents and industrial illnesses, unemployment, illness and maternity).

Dignity

Work dignity is a strategic objective in the PRSP employment strategy. The particular aspects of work dignity that are emphasized include the creation of jobs of acceptable quality, the promotion of worker's rights and the promotion of participatory social dialogue of workers.

Source: *Mali 2002.*

Gender and youth employment issues are not mainstreamed in all the PRSPs

Apart from creating more and better employment, there is a need to target, for employment purposes, certain groups that deserve particular attention in Africa: women and young people (see chapters 2 and 5).

Sixteen of the 21 PRSPs target women, in various degrees, for the generation of employment opportunities. Several have measures to improve decent employment among the female workforce. But in most cases equity is the only dimension of decent employment that is addressed; only a few countries address the other dimensions of decency.

Employment generation for young people is addressed in various degrees by 17 countries. However, only five countries have the objective of improving any of the decent employment aspects specifically for young people. Most propose to generate employment opportunities for young people through technical education and vocational training. Examples of other actions include creating jobs for young people through the development of the small and medium-size enterprises, fishing, agrobusiness and tourism sectors (Djibouti), a microfinance programme for young people (Ghana); provision of mechanisms to manage transition from school to work, career guidance, industrial attachment, mentoring and coaching (Kenya); setting up different agricultural activities for young people (Madagascar); and creating a multiservice terminal with access to database on unemployed graduates (Mauritania).

Regional and sectoral targeting in the PRSPs for decent employment creation: some gaps

Apart from targeting employment towards certain groups, there is also a need to target employment in specific regions and sectors of the economy because specific regions or sectors might have a special employment need and because by targeting some specific regions or sectors the impact on employment can be larger.

A key consideration for regional targeting of employment is the regional allocation of infrastructure investment. The impact of infrastructure investment on employment creation and poverty reduction is likely to be larger, at least in the short-term, if investment targets regions with high poverty incidence and population density (UNECA 2005). However, in only eight PRSPs do infrastructure investments target regions with a high incidence of poverty. Furthermore, only two PRSPs target regions with high population density and poverty incidence for infrastructure investment.

With respect to sectoral targeting, the informal sector constitutes a very important target because decent employment levels in the sector are especially low (see chapter 2). However, only a limited number of the PRSPs contain goals or actions to address the generation of employment opportunities and the improvement of decent employment in this sector. About two-thirds of them target, in various degrees, the informal sector for the generation of employment opportunities, and about one-third for the improvement of at least one aspect of decent employment. Ghana has perhaps the most comprehensive set of measures to address informal sector employment issues (box 3.7).

Urban areas should also be important targets of employment policies in Africa, because youth unemployment rates in urban areas are higher than in rural areas in nearly all African countries (see chapter 5). However, not all the PRSPs address—notably those of Burkina Faso, Chad, Guinea, Rwanda, Uganda and Zambia—the generation of employment opportunities specifically in these areas.

Other important sectors that should be targeted are the agricultural sector and the rural off-farm sector.[4] In Africa the creation of off-farm employment opportunities together with policies that promote agricultural productivity will raise labour earnings and reduce the

Box 3.7

Ghana's PRSP measures to increase employment opportunities and improve decent employment in the informal sector

Ghana's PRSP focuses on developing the informal sector mainly because of its importance in providing alternative employment opportunities to the formal sector. Improving decent employment is one feature of the development of this sector. The specific measures that help improve decent employment in the informal sector include:

- Promoting the technological proficiency and advancement of the labour force.
- Equipping the workforce with financial and managerial skills.
- Reforming and strengthening the traditional apprenticeship system.
- Making contract enforcement effective.
- Increasing access to credit.
- Creating producer organizations.
- Increasing the production, productivity and employment of the small and medium-size enterprises.

Source: *Ghana 2003.*

incidence of poverty among farmers and rural informal sector workers (see chapter 4). In addition, the rural off-farm sector can help stabilize rural household incomes during the off season (Haggblade, Hazell and Reardon 2002) and in periods of drought. Although, most of the PRSPs articulate measures to increase agricultural productivity and to create rural off-farm employment in general, only a few explicitly promote the generation of rural off-farm employment to stabilize rural incomes. Ethiopia is a notable exception; its PRSP envisages the creation of off-farm income-generation activities to create supplementary employment during food shortages. This goal is implemented through public employment generation schemes that are linked to the development priorities of rural areas (that is, soil conservation, road construction, small-scale irrigation, water supply and sanitation).

The poor quantification of employment impacts in the PRSPs

Quantifying the expected or targeted impacts[5] of policies on the different dimensions of employment is useful for two reasons: it helps assess the magnitude of the impact of policies on employment, and it helps monitor implementation of employment goals. However, the PRSPs rarely quantify the expected or targeted impact of policies on employment op-

Table 3.5

Examples of employment dimensions and policies that are quantified in the PRSPs in terms of their expected or targeted impact on employment

Employment dimension or policy	Country	Quantification
Employment opportunities	Madagascar	Creating 10,000 jobs in 2004, 15,000 jobs in 2005 and 20,000 jobs in 2006.
Work productivity	Malawi	Targeting 340,000 beneficiaries over three years with the Targeted Input Programme, which aims to enhance agricultural productivity.
Work security	Ghana	Expanding the social security schemes by 100,000 workers and introducing a mutual health insurance scheme that covers at least 500,000 workers between 2000 and 2005.
Work dignity	Madagascar	Supporting 1,100 farmer organizations and revitalizing 110 chambers of agriculture from July 2003 to June 2004.
Work freedom	Tanzania	Removing 1,000 more children a year from child labour—half of them girls.
Education and training policy	Madagascar	Adding 13,000 qualified workers a year to the labour force.
Infrastructure investment policy	Malawi	Generating employment for as many as 250,000 participants (time frame not specified).
Private sector development policy	Cameroon	Creating about 300,000 jobs through 15,000–20,000 micro, small and medium-size enterprises within five years.

Source: *Cameroon 2003; Ghana 2003; Madagascar 2003, 2004; Malawi 2002; Tanzania 2004.*

portunities or on decent employment. For most of the policies or employment dimensions considered in the analysis, fewer than three countries provide quantifications.

Table 3.5 shows some examples of employment dimensions and policies that are successfully quantified by particular countries. Note how the PRSP of Madagascar sets an overall target for the employment opportunities that it intends to create. Madagascar's PRSP is also an interesting and unique example of the quantification of training and education in terms of employability.

Conclusion and policy recommendations

Despite rising growth since the late 1990s, Africa has had little success in stemming the tide of poverty. By contrast, the incidence of poverty has risen, unlike in other regions. Poverty in Africa is widespread, chronic, gender-biased and pervasive among the labour force. Indeed, the high incidence of poverty among workers suggests that an employment-intensive growth process underpinned by rising productivity is key to reducing poverty. Employment-intensive growth will benefit poor people if it creates strong demand for their services and is accompanied by measures that facilitate their integration into the labour force. Hence, measures that create strong and sustainable employment opportunities for

poor people and empower them to benefit from newly created jobs will be instrumental in reducing the incidence of poverty.

These measures are more likely to be successful if poor people are disproportionately represented in sectors characterized by strong domestic and external demand, if the technologies adopted by these sectors are largely labour-intensive, if poor people have access to productive resources and if poor people have the human capital endowments to access newly created jobs.

Furthermore, the centrality of decent employment to poverty reduction suggests the need to address the employment challenge in the development programmes of all African countries. Currently, PRSPs are one of the most influential development programmes in Africa that explicitly address the issue of poverty. However, an analysis of all 21 full PRSPs in Africa reveals that employment creation is not adequately addressed in most PRSPs.

Given the jobless growth trends in Africa, the significance of decent employment to poverty reduction and the apparent failure of policymakers to adequately reflect employment policies and programmes in their development plans, this report proposes the following broad recommendations.

Stimulating employment growth

- Promote the adoption of labour-intensive techniques, particularly in sectors that employ poor people.
- Encourage export diversification to minimize terms of trade shocks through the production of nontraditional exports.
- Reduce taxes on producer prices to ensure that labour benefits from improved terms of trade.
- Strengthen intersectoral linkages to maximize the spillover effects of growth by designing and promoting integrated development projects.
- Maximize private sector job creation by minimizing constraints to investments and growth (for example, complementary public investments in roads, utilities and the like and minimization of red tape).

Promoting productive employment

Sustainable job growth can occur only in a context of rising productivity. The need to increase productivity is even more urgent in Africa, where most poor people are unskilled and employed in low productivity jobs. Improving productivity, particularly of the working poor, will require measures that not only improve skills but also facilitate access to productive assets. These measures must:

- Facilitate investment in the design and implementation of a human capital development programme (through formal education or skills training) that is relevant to the workplace.

- Improve public sector efficiency through credible reforms that maximize the productivity of public sector employees.

- Maximize physical and financial access to health systems for poor people, through cost-effective investments in social services, including the design of financially sustainable social safety nets.

- Address the adverse effects of major diseases such as malaria, halt the spread of HIV/AIDS and meeting the needs of people living with HIV/AIDS through preventative measures and targeted access to medical care for poor people.

- Improve marketing and distribution channels through improved infrastructure and institutional reforms to address physical barriers to markets (for example, lack of roads, bridges and the like) as well as institutional barriers.

- Improve access to formal wage employment by ensuring that labour regulations are not unduly restrictive.

- Review existing laws and cultural practices to ensure that they do not limit women's access to productive assets and employment opportunities.

Devising social protection schemes

Not even the most employment-intensive growth process can totally eliminate poverty. Robust job growth can occur along with poverty due to frictional unemployment, ill health, old age, physical and mental handicaps and a host of other factors that place workers outside the labour force. Thus, social protection schemes are needed to provide safety nets for those who invariably fall through the cracks.

Strengthening the employment focus of Africa's development programmes

To be completely implemented, these recommendations will need to be reflected in the development programmes of African countries in general—and in PRSPs in particular, because they are the most influential development programmes on the continent. Based on the analysis of 21 PRSPs in Africa, the following recommendations are suggested for strengthening the employment content of development programmes in Africa and facilitating their implementation:

- Ensure that employment strategies are informed by best-practice cases.

- Encourage greater participation of trade unions, labour ministries and labour-friendly organizations (for example, the International Labour Organization) in the PRSP process.

- Set identifiable employment targets to facilitate more effective monitoring of progress towards the realization of employment goals.

- Ensure that PRSPs are integrated into national budgets and receive priority funding from domestic and external (ODA flows) sources.

Endnotes

1 The incidence of poverty has been on the rise in transition economies since 1980; however, these countries have one of the lowest poverty rates in the world (5 per cent).

2 The concept of poverty is often based on income or consumption measures of welfare. However, well-being is broader than income or consumption; it encompasses the environment that people need to lead a fulfilling life (UNDP 2004). This environment includes education, health, freedom and social participation as well as income and consumption. This section describes various features of poverty in Africa.

3 In the analysis of the PRSPs trade liberalization measures are excluded from the "liberalization" concept.

4 The rural off-farm sector includes all rural sectors except agriculture, livestock and fishing. These include industrialization, rural services, rural tourism, rural infrastructure construction and forestry industry. The mining sector is not considered a rural sector.

5 Quantification of actual impacts after implementation is not considered here.

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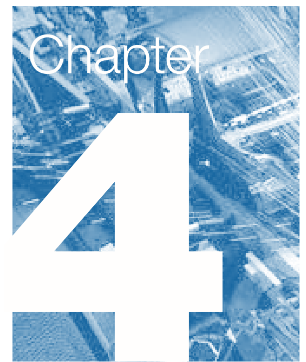


Structural transformation to break away from rural poverty

With 70 per cent of poor Africans living in rural areas, poverty in Africa is largely a rural phenomenon. Increasing rural employment and income is therefore crucial to reducing poverty. An increase in rural incomes will likely improve the living standards of the rural poor, but it could also drive a structural transformation of the whole economy.

Structural transformation is a process by which the relative contribution of nonagricultural sectors to the overall economy rises as agriculture's share declines in relative terms. In absolute terms, however, agriculture continues to grow and contribute to overall economic growth. Agricultural productivity growth and increased farm incomes are prerequisites for structural transformation. Increased farm incomes lead to derived demand for nonfarm products, which in turn leads to the growth of small and medium-size enterprises in rural villages, small towns and larger urban areas. To increase the productivity of the agricultural and other sectors of the economy, improved financial and human capital development is crucial in order to ensure overall factor productivity, including labour productivity. Human capital development in turn depends on Africa's capacity to achieve a much needed demographic transition, characterized by low mortality and fertility rates.

> *"Africa has yet to complete a demographic transition"*

With the highest population growth rates in the world, Africa is the only continent that has yet to complete a demographic transition, mostly due to persistently high fertility rates despite earlier gains in reducing mortality rates. HIV/AIDS and the resurgence of malaria and tuberculosis are eroding increases in life expectancy and affecting the demographic structure of African households as well as the quantity and quality of the labour force. Low levels of human capital make it difficult for Africa to increase labour productivity—a much needed input for structural transformation.

Agriculture is the main source of income for 90 per cent of the rural population in Africa. It is also vital to ensuring food security for the urban population. Yet, in Africa agriculture has failed to feed the growing population. Some 200 million Africans are undernourished despite commercial food imports of $15–$20 billion a year and about $2 billion in food aid per year (UNECA 2005). Many Africans in the agricultural sector who are either self-employed or wage earners are the poorest people in the world, due mainly to the low performance of African agriculture. African agriculture is also severely undercapitalized, resulting in low total and factor productivity compared with Asia and Latin America. Growth and increased competitiveness are needed in agriculture, particularly in the domestic food and agricultural chains (production, storage, processing, marketing), which have the most potential to enhance links between agriculture and the rest of the economy.

Sectoral linkages is key to structural transformation

A strategy to transform the agricultural and rural sectors would require agroindustrial and agribusiness and service sector development to accompany an agricultural productivity-increasing green revolution. Transforming the rural nonfarm sector should therefore complement agricultural transformation to complete the rural strategy for increasing labour productivity, wages, income and rural employment. The rural nonfarm sector not only has the potential to increase agricultural wages by adding value to agricultural products, but it also has the capacity to increase rural wages through direct employment, due to high labour productivity relative to the farm sector. Indeed, rural Africans derive about 42 per cent of their income from rural nonfarm activities—a high share considering that only about 10 per cent of the rural labour force are employed in the rural nonfarm sector (Haggblade, Hazell and Reardon 2002).

For Africa to achieve a structural transformation that stimulates growth, creates employment and reduces poverty, it must:

- Complete its demographic transition by influencing attitudes and providing funds for programmes to meet the unmet demand for contraceptives, reduce the age at which women have their first child, increase education opportunities for girls and employment opportunities for women and, scale up prevention, treatment and care of infectious of diseases, particularly HIV/AIDS.

- Increase agricultural productivity and enhance agricultural links to the industrial and service sectors by expanding appropriate research, knowledge and technology, addressing market development and access issues, improving the management of production assets (water, land) and mitigating the adverse impacts of HIV/AIDS on agriculture.

- Facilitate the growth of job-creating small and medium-size enterprises through rigorous private-public partnerships to improve the provision of infrastructure, credit, inputs, markets, training and other services.

This chapter explores the potential for Africa to achieve a demographic transition, realize an agricultural transformation and develop a vibrant rural nonfarm economy. It discusses the sectoral links that are vital for a structural transformation of Africa's economies. It highlights the relationship of Africa's demographic transition to structural transformation. It then discusses agriculture's role in an overall structural transformation, noting the challenges and opportunities for achieving an agricultural transformation in Africa. The role of the rural nonfarm economy in a structural transformation of Africa is then presented, followed by recommendations for catalyzing a structural transformation in Africa.

Structural transformation through sectoral links

Structural transformation is a process by which sectors other than agriculture account for increasing shares of employment and output of the economy. Though the economy becomes less agriculturally oriented in a relative sense, it continues to grow in absolute terms and generate important growth links to the rest of the economy. Structural transformation thus

involves a net resource transfer from agriculture to other sectors of the economy over the long term (Staatz 1998).

Structural and demographic factors have a significant effect on the structural transformation of an economy, particularly on reaching the turning point where the size of the agricultural labour force begins to decline (Gabre-Madhin and Johnston 1999). The time required to reach this point depends on the initial share of agriculture within the total labour force, the rate of growth of the total labour force and the rate of growth of nonfarm employment. If the growth rate of nonfarm employment exceeds that of total labour, the share and growth of the agricultural labour force begin to decline over time. When the growth rate of agricultural labour becomes negative, a structural transformation turning point is reached, implying that countries with a large initial share of total labour force in agriculture and countries with high growth rates of total labour will take a long time to reach the turning point, while countries whose rate of nonfarm employment growth is much higher than that of the total labour force will reach the turning point faster than countries with low growth in nonfarm employment relative to the growth rate of the total labour force.

Increased agricultural productivity can mean growth and reduced poverty

Table 4.1 illustrates the relative stages of 20 African countries, based on selected indicators of structural transformation. The countries are grouped by their ability to achieve a demographic change conducive to an economic structural transformation. Compared with other groups in Table 4.1, countries in group A are at the declining fertility stage of their demographic transition. For these countries, the total fertility rate has been reduced from an average of 5.1 births per woman in 1990–95 to 4.5 in 1995–2000 and 4.0 in 2000–05. African countries in group B have average fertility rates of 5.3 births per woman, down from 6.3 in 1990–95. And countries in Group C have fertility rates of 6.9 births per woman, down from 7.2 in 1990–95. Countries that are more advanced in their demographic transition (with low fertility rates) are excelling in transforming their economies. For instance, these countries have lower shares of total labour in agriculture, higher agricultural labour productivity and higher infrastructure development. Countries in group A had an average of 56 per cent of their labour force in agriculture in 2000, compared with 66 per cent for group B and 86 per cent for group C. Similarly, agricultural labour productivity for group A was $662 per worker in 1994–96—higher than group B's $523 and group C's $206. On average, nonfarm employment growth (at 1.6 per cent in 1990–97), measured using industrial growth as a proxy, has not been able to keep up with the total labour force growth in Africa (2.6 per cent).

Like other developing regions where most people are initially employed in agriculture, Africa is likely to achieve growth and reduce poverty by emphasizing agricultural productivity growth and industrialization led by agriculture. There is a strong link between African agriculture and the rest of the economy, with growth multipliers of 1.5–2.7 per cent in Africa, compared with 1.5–2.4 per cent for Asian countries (Spencer 1995). This means that a $1 increase in rural income would translate to $1.50–$1.70 increase in income for other sectors, mainly through expenditure and consumption links among agriculture and other sectors, leading to growth and job creation in the nonfarm sectors. For every job created through increased agricultural production, two to three jobs are created in the nonfarm sector.

Table 4.1

Structural transformation indicators for selected African countries, various years

	Total fertility rate (births per woman)			Share of labour force in agriculture (%)			Labour force growth (%)		Agricultural value added per worker (1987 PPP US$)		Industrial growth (%)	
	1990 95	1995-2000	2000-05	1990	2000	2010[a]	1980-90	1990-97	1979-81	1994-96	1980-90	1990-97
All countries	6.3	5.8	5.5	74	69	64	2.8	2.6	468	463	2.9	1.6
Group A	5.1	4.5	4.0	61	56	51	3.2	2.5	667	662	2.9	2.1
Botswana	4.1	3.6	3.2	46	45	42	—	—	—	—	—	—
Ghana	5.5	4.8	4.4	59	57	54	3.1	2.7	813	684	3.3	4.3
Kenya	5.4	5.0	5.0	80	75	71	3.6	2.7	268	240	3.9	2.0
Namibia	5.8	4.8	4.0	49	41	34	2.4	2.5	1,295	1,458	1.1	2.9
Zimbabwe	4.8	4.1	3.6	68	63	56	3.6	2.3	294	266	3.2	–0.8
Group B	6.3	5.8	5.3	71	66	59	2.9	2.7	526	523	2.3	1.0
Cameroon	5.7	5.1	4.7	70	59	47	2.4	3	861	827	5.9	–3.8
Côte d'Ivoire	6.3	5.6	5.1	60	49	38	3.1	2.3	1,527	1,354	4.4	4.2
Madagascar	6.1	5.9	5.4	78	74	70	2.5	2.8	190	178	0.9	1.1
Nigeria	6.6	6.3	5.9	43	33	25	2.6	2.8	479	684	–1.1	0.5
Rwanda	6.9	6.2	5.7	92	91	89	3.2	2.3	306	206	2.5	—
Senegal	5.9	5.5	5.0	77	74	70	2.5	2.6	328	375	4.1	3.7
Tanzania	6.2	5.6	5.1	84	80	76	3.2	2.8	—	—	—	—
Togo	6.2	5.8	5.4	66	60	54	2.6	2.7	404	461	1.1	2.0
Zambia	6.4	6.0	5.7	74	69	63	3.1	2.8	116	100	1.0	–2.6
Group C	7.2	7.1	6.9	88	86	82	2.5	2.5	216	206	3.6	2.3
Burkina Faso	7.2	6.9	6.7	92	92	92	2	2.1	155	182	3.7	1.9
Burundi	6.8	6.8	6.8	92	90	89	2.6	2.6	218	177	4.5	–8.0
Malawi	6.8	6.4	6.1	87	83	79	3	2.4	162	156	1.9	3.5
Mali	7.4	7.2	6.9	86	81	75	2.3	2.6	251	259	7.0	2.1
Niger	8.2	8.2	7.9	90	88	85	3	2.9	292	256	–1.7	1.3
Uganda	7.1	7.1	7.1	85	80	75	2.2	2.7	—	—	6.0	1.3

— not available

Note: *See text for explanation of groupings.*

a. *Projected.*

Source: *World Bank 1997, 1998; UNDESA 2004, 2005; FAO 2005; Kirk and Pillet 1998.*

Agriculture provides the surest foundation for sustainable growth, through links with the industrial and service sectors. Feedback from productivity gains in agriculture has spurred growth in Asia's manufacturing sector. The so-called "growth tragedy" in Africa has been attributed largely to the failure to establish a productive domestic agricultural supply base as a counterpart to programmes for rapid industrialization and strengthening agriculture as part of the development chain. But focusing on the agricultural sector alone will not

produce the required productivity gains to stimulate rural employment. Lessons from the early stages of structural transformation in Taiwan Province of China and other parts of Asia show that the rural nonfarm sector is a catalyst to agricultural productivity growth and job creation in addition to being a key source of nonfarm employment (Gabre-Madhin and Johnston 1999).

The majority of rural nonfarm activities are related to agriculture, forming part of the off-farm activities of the household. Many are located within the household, but also in rural village centres and small urban towns. A vibrant rural nonfarm sector could absorb surplus rural labour, reducing underemployment in agriculture and slowing out-migration. The rural nonfarm sector is crucial for providing off-farm employment and income, adding value to agricultural products for local and external markets and hence increasing agricultural productivity and providing goods and services to meet increasing demand for farm equipment and nonfarm products for local consumption as rural incomes increase (Majid 2004). The sector is thus a source of multipliers for rural employment and welfare improvement. The rural nonfarm and agricultural sectors have to be viewed as complements with respect to facilitating overall economic growth and employment creation—that is, a productive and diversified agricultural sector will support rural industrial and service sectoral growth and vice versa.

“A vibrant nonfarm sector could absorb surplus labour”

Many researchers (Hayami and Ruttan 1985; Ndulu and van de Walle 1996; Platteau and Hayami 1998) point to the failure of Africa and its development partners to recognize and adopt strategies that take note of the complementarity between agricultural and industrial development. While economic theory and experience from other parts of the world point to the importance of an agriculture-led industrialization and structural transformation of the overall economy (Johnston and Mellor 1961), many strategies have emphasized industrialization and neglected agriculture. Other strategies have advocated sectoral approaches to development, with conflicting policies and outcomes. And many of Africa's development strategies have failed to integrate methods to curb the impact of Africa's rapid and prolonged growth in its labour force and the impact of HIV/AIDS on the structural transformation process.

The impact of HIV/AIDS on sectoral links

As evidence mounts on the adverse impact of HIV/AIDS on African households, communities and economies, it is becoming apparent that some of the underlying assumptions of structural transformation models may not apply in the face of HIV/AIDS. For instance, structural transformation assumes that over time, abundant agricultural labour will migrate from the agricultural sector as growth in the rural nonfarm sector is fuelled by rising demand for nonagricultural goods and services induced by rising farm incomes. The expected decline in the growth of labour as a result of HIV/AIDS will, however, affect the size of the labour force, migration patterns, the cost of labour and the competitiveness of labour-intensive sectors such as agriculture. In addition to its effect on the quantity of labour, HIV/AIDS affects the human capital stock, the availability of financial and social capital, as well as the ability to use land and other natural resources efficiently for a structural transformation of African economies.

The high prevalence of HIV/AIDS in rural Africa shocks the rural economy by rendering a large share of the labour force unable to work due to illness, death and the need to care for others. The sectoral response to labour shortages in the agricultural sector, for example, depends on the number of people who are underemployed in the informal sector in both rural and urban areas. If enough people are underemployed in the informal sector, a decline in the agricultural labour force will result in reverse migration of nonagricultural labour from the informal sector to the agricultural sector as agricultural wages increase due to labour shortages in the agricultural sector (Bryceson and Potts 2005). Evidence from Zambia supports the view that shortages in agricultural labour would induce labour migration from the urban informal sector into agriculture. But it is difficult to generalize this result to other parts of Africa. In addition, it is unclear whether as the disease progresses the demand for agricultural labour will exceed the supply of underemployed labour in the informal sector. To the extent that more educated people were the hardest hit in the early years of HIV/AIDS, several researchers (Ainsworth and Semali 1998; Kirunga and Ntozi 1997) suggests that the loss of labour may be acute in the formal sector and in the more skilled jobs within agriculture and the rural nonfarm sector. This is because replacing skilled workers lost to AIDS with workers from the informal sector or agriculture is not always possible.

These lessons on the significance of strengthening intersectoral links for a structural transformation that creates employment and reduces poverty suggests that Africa must put in place strategies to complete a demographic transition, transform agriculture by increasing agricultural productivity and expanding agricultural markets and increase growth and employment in nonfarm sectors. Furthermore, Africa must seriously address the HIV/AIDS pandemic because it has a bearing on whether Africa can achieve a demographic transition, transform its agriculture and achieve an overall structural transformation.

Demographic transition: a prerequisite to Africa's structural transformation

Demographic transition is the shift towards low mortality and fertility rates thanks to overall modernization of the economy from industrialization, urbanization, education and empowerment of women (UNECA 2001). These developments in turn lead to progress in hygiene, medicine and overall healthcare, resulting in lower mortality rates, particularly infant mortality rates. As infant mortality rates decline, parents reduce their fertility, leading to an overall decline in fertility rates. Many researchers have defined the various stages in the demographic transition (Blacker 1947; Thompson 1948; Zamoun and Tabutin 1994). According to Zamoun and Tabutin (1994), these stages include:

- A pretransition stage with fluctuating birth and death rates and slight population growth.
- The beginning of steady decline in mortality while birth rates remain high, resulting in high natural population growth.
- A period of rapid reduction in birth rates, but still lagging behind mortality decline with the population growth beginning to decline.

- The post-transitional stage with death and birth rates stabilized at levels as low as 10 per 1,000, with birth rates staying higher than death rates, leading to a slow population growth.

Despite some criticism of the demographic transition theory there is a consensus that mortality decline is a prerequisite for fertility decline. Africa is the only continent that has yet to complete a demographic transition. It has failed to reduce mortality and fertility rates to levels conducive to a structural transformation of the economy—that is, similar to levels in Europe and North America before they achieved their structural transformation or, more recently, in Asia and Latin America and the Caribbean (Birdsall and Londono 1998; Gabre-Madhin and Johnston 1999). In Latin America and the Caribbean and Asia total fertility rates have declined about 25 per cent, from 3.4 births per woman during 1985–90 to 2.5–2.6 in 2000–05 (table 4.2). During the same period Africa's total fertility declined at a slower rate of 19 per cent, from 6.1 births per woman to 4.9. The total fertility rate in Africa is projected to remain relatively high, with repercussions for total population and labour force growth rates. Subregional differences in fertility rates point to persistently high rates in East, Central and West Africa, with rates closer to those in Latin America and Asia for North and Southern Africa.

High fertility rates have translated to high levels of labour supply in Africa. Indeed, the working age population in Africa increased from about 281 million in 1985 to 375 million in 1995, reflecting a growth rate of 3 per cent, higher than the annual population growth rate for the same period. In 2005 the working age population in Africa doubled in size from levels in 1985 to 489 million people. By 2015 the working age population is projected to reach 616 million people (UN 2004), a sharp increase in the supply of labour, which will need to be met by an equivalent increase in job opportunities.

"Mortality decline leads to fertility decline"

In addition to affecting the quantity of labour supplied, demographic transitions influence the quality of the labour force as well as its age distribution and dependency burden. Combined impacts of a high share of young people and low quality of healthcare in Africa

Table 4.2

Total fertility rate, 1985–2015 (births per woman)

Region	1985–90	1990–95	1995–2000	2000–05	2005–10[a]	2010–15[a]
Latin America and the Caribbean	3.39	3.01	2.72	2.53	2.36	2.23
Asia	3.40	2.98	2.72	2.55	2.42	2.30
Africa	6.08	5.63	5.22	4.91	4.57	4.19
East Africa	6.69	6.32	5.98	5.61	5.20	4.76
Central Africa	6.58	6.51	6.38	6.28	5.98	5.55
North Africa	4.95	4.12	3.52	3.21	2.95	2.67
Southern Africa	4.05	3.59	3.10	2.79	2.54	2.35
West Africa	6.75	6.38	5.97	5.56	5.09	4.58

***a.** Projected.*

***Source:** UN 2004.*

affect the workforce and human capital on the continent. The dependency ratio, which measures the ratio of young and old dependants to the working age population, is very high in Africa, which limits employment opportunities.

Characterized by high fertility rates, high population growth rates and low levels of human capital, these demographic trends make it difficult for Africa to attain a much needed structural transformation. Several socioeconomic and cultural factors have contributed to persistently high fertility rates in Africa, including low levels of education for girls and lack of job opportunities for women, inadequate access to contraceptives, poor access to healthcare and education (which hampers human capital and skills development), and, the adverse impacts of HIV/AIDS and the resurgence of malaria and tuberculosis, which have an adverse impact on life expectancy and the quantity and quality of the labour force.

"Demographic trends hamper Africa's structural transformation"

Impact of HIV/AIDS on demographic transition

The depressing impact of HIV/AIDS on the quantity and quality of the labour force must be clearly understood and incorporated in the structural transformation process in Africa. This is particularly important for most countries in Southern Africa, which have the highest HIV prevalence rates on the continent and in the world (table 4.3).

Table 4.3
HIV/AIDS prevalence for adults ages 15–49, 2003 (%)

Rank	Country	Prevalence rate
1	Swaziland	38.8
2	Botswana	37.3
3	Lesotho	28.9
4	Zimbabwe	24.6
5	South Africa	21.5
6	Namibia	21.3
7	Zambia	16.5
8	Malawi	14.2
9	Central African Republic	13.5
10	Mozambique	12.2
11	Tanzania	8.8
12	Gabon	8.1
	Sub-Saharan Africa	7.5
	World total	1.1

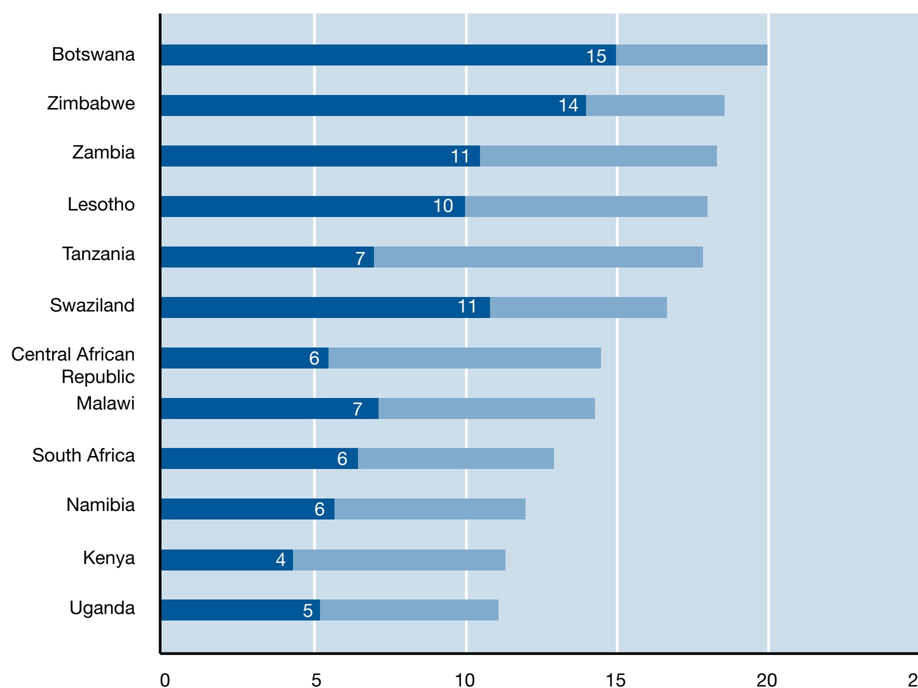
Source: *UNAIDS 2004.*

Recent estimates by the Joint United Nations Programme on HIV/AIDS (UNAIDS 2004) show that all the countries with an adult (ages 15–49) prevalence rate of 20 per cent or higher are in Southern Africa. These high prevalence rates are affecting the quantity and quality of the labour force. The United Nations (UN 2004) found that the working age

population in Southern Africa increased from about 21 million people in 1985 to 28 million in 1995 and 33 million in 2005, a relatively slow increase due mainly to AIDS deaths. Indeed, for five countries in Southern Africa (Botswana, Lesotho, Mozambique, South Africa and Swaziland) population growth rates are expected to be negative. And for six countries with HIV prevalence rates above 20 per cent the projected age structure as a result of HIV/AIDS will have serious implications for many aspects of development in the region. Adult deaths due to AIDS are also increasing the number of orphans in Africa (figure 4.1). Southern Africa has the highest share of orphaned children, led by Botswana (20 per cent), Zimbabwe (19 per cent), Zambia (18 per cent) and Lesotho (18 per cent). AIDS orphans make up as high as 75 per cent of the total number of orphans in the subregion. The additional financial burden of taking care of orphans and the loss of intergenerational transfer of skills and knowledge due to adult deaths have a detrimental effect on the ability of households, communities and governments to engage in productive employment in order to increase incomes, achieve structural transformation and reduce poverty.

Figure 4.1

Effect of HIV/AIDS on the number of orphans in Africa, 2003 (% of orphaned children)



Source: *UNAIDS 2004.*

Agricultural transformation, rural employment and poverty reduction

Despite decreasing trends in the share of people living in rural Africa, most Africans continue to reside in rural areas where the agricultural sector is the main employer. Indeed, in 2005 some 270 million Africans were employed in the agricultural sector, but they remained some of the poorest working people in the world, due mainly to Africa's failure to transform from a low productivity agrarian system to a modern production system with strong links to other sectors of the economy capable of providing meaningful employment opportunities.

Challenges in African agriculture

Africa's agriculture is characterized by weak knowledge-based subsistence agricultural production systems, incomplete input and product markets that are poorly integrated at the national, subregional and regional levels and low private investment in farming systems and marketing chains. The combined effects of these features include stagnating or declining agricultural productivity, weak backward and forward links between agriculture and other sectors, loss of competitiveness in world markets, increased food insecurity and natural resource and environmental degradation. Revitalizing and transforming Africa's agriculture in order to provide decent employment and reduce rural poverty will require Africa to reverse several unfavourable trends and challenges:

"In 2005, 270 million Africans worked in agriculture"

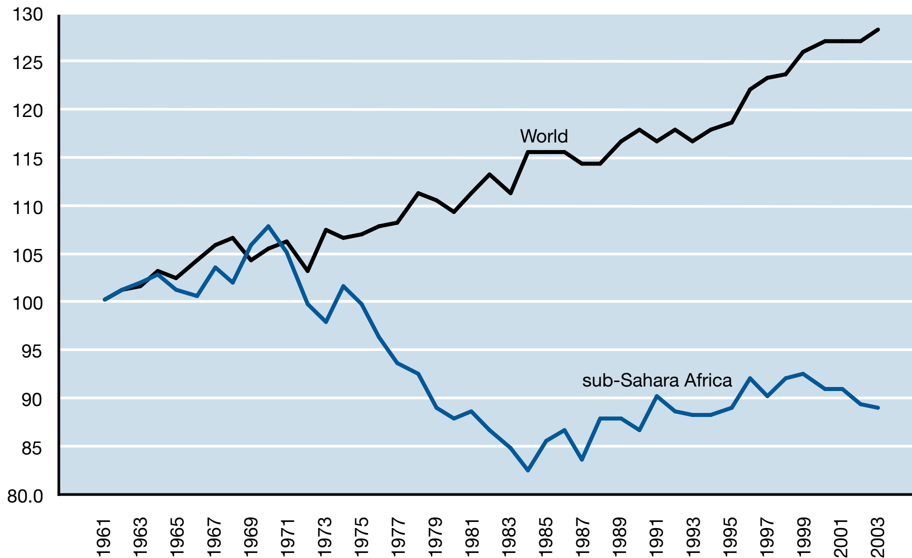
- Low agricultural productivity and poor support for agricultural research and extension.
- Poor water resources management and low irrigation infrastructure.
- Land degradation.
- Poor market infrastructure.

Low agricultural productivity and poor support for research and extension. Agricultural productivity in Africa is only 42 per cent of that in Asia and 50 per cent of that in Latin America (Wolgin 2001). Similarly, factor productivity in agriculture is lowest in Africa, compared with other regions, with labour productivity at only about 57 per cent that of Asia and Latin America. Real agricultural output per worker has stagnated at $375 over the past 10 years, a 12 per cent decline from the 1980 level of $424. Furthermore, the share of arable land under cultivation and the share of arable land under irrigation are lowest in Africa. While other parts of the world have increasing agricultural production per capita, Sub-Saharan Africa's is declining (figure 4.2).

Africa's low productivity indicates the magnitude of the potential loss arising from inefficient use of agricultural resources. It also indicates the agricultural sector's potential to exploit productivity-enhancing technological innovations that can boost national output and purchasing power to reverse the current low productivity in agriculture and lead to substantial growth of overall GDP and employment.

Figure 4.2

Agricultural production per capita, 1961–2003 (Index, 1961 =100)



Source: *FAO 2005.*

But unlike other parts of the world, African agriculture has yet to embark on a sustainable path to a green revolution. One of the most important requirements for increasing the productivity and competitiveness of African agriculture is to significantly reduce the unit costs of production and distribution by increasing agricultural productivity. The problem, however, is that there is only a limited cumulative stock of useable improved technology in African countries. Many African farmers are still using low yielding agricultural technology, which contributes not only to low production but also to reduced labour productivity and often to environmental degradation.

Public investment in research and technology generation and diffusion is needed to encourage broad-based adoption of available technology. In addition, there is a need to strengthen indigenous capacities to develop, adapt and diffuse the kinds of technology needed by low-income producers to effectively compete in domestic, regional and global markets. Unfortunately, government and donor funding for agricultural research has dwindled in recent years, diminishing the capacity of public research institutions. Gaps left by reduced funding have not attracted private sector involvement due to the long lead times for technology development. Experience indicates that 8–10 years are needed to develop and improve a crop variety for release and 15–20 years for technology to move from first inception to widespread impact on farmers' fields. Since the private sector is unlikely to play a significant role in this area, African governments must continue to provide financial support and maintain human capital in national research systems.

> *"An African Green Revolution would improve yields and agricultural practices"*

Poor water resources management and low irrigation infrastructure. One major lesson from Asia's successful green revolution is that irrigation infrastructure was a key complemen-

tary input to hybrid seed varieties and fertilizer in achieving sustainable improvements in agricultural productivity. Similar successes in Africa, therefore, depend on Africa's capacity to harness its water resources for agricultural production in a sustainable manner.

Africa's reliance on rain-fed agriculture makes farmers vulnerable to poverty and food insecurity because the availability of water for food and agricultural production varies. Recurrent droughts frequently wipe out food harvests, livestock and cash crops. Hence, not much progress towards sustainable development can be achieved until Africa reaches a minimum level of developing and managing water resources for secure food and agricultural production. Although abundant on a regional scale, only about 3.8 per cent of surface and ground water resources available in Africa are harnessed or withdrawn to meet the main uses of water: agriculture, community water supply and industry (FAO 1995). Agriculture uses 88 per cent of the total water withdrawn, but barely 6 per cent of total cultivated land is under irrigation in Africa, compared with 33 per cent in Asia. Challenges that hamper irrigation development include financial constraints and inadequate institutional arrangements at the national and regional level, which are critical to improving performance in the water sector. There is therefore an urgent need for reforms underpinned by cooperation and partnership among countries and subregions in the continent, with the water basin serving as the basic unit for resource management.

Poor land management and land degradation. Improving land management for agricultural production and overall rural development requires improved security of tenure and better land distribution in Africa. The United Nations Economic Commission for Africa (UNECA 2004) found that the contribution of land to economic growth depends on the security of property rights, which provides incentives for investment in agriculture and natural resources, thereby contributing to increased and sustained agricultural productivity and natural resource stewardship. In many parts of Africa forms of tenure do not provide enough security to promote and support private investment and to facilitate resource mobility for efficient agricultural production. In addition to issues of tenure security, acute unequal distribution of land must be addressed, along with the increasing social conflicts associated with such entitlement failures. Access to land and security of land rights are therefore central to policy efforts and strategies aimed at agricultural transformation.

"*Food insecure, most of SSA relies on rain-fed agriculture*"

Land degradation, one of the most serious threats to the sustainability of farming systems in Africa, is a result of both fragile physical conditions and poor land management. Africa accounts for an estimated 27.4 per cent of the world's land degradation, and some 500 million hectares of land in Africa have moderate to severe degradation (UNEP 2000; WRI, IUCN and UNEP 1992). Indeed, about 65 per cent of total cropland and 30 per cent of the continent's pastureland are affected by degradation, with consequent declining agricultural yields.

Poor market infrastructure and low market access. Access to markets complements technological innovation in catalyzing agricultural and rural growth. Unfortunately, the African food and agricultural market is characterized by extreme fragmentation along subregional, national and even subnational borders, resulting in segmented markets of suboptimal size. African markets are also unable to ensure optimal profitability for private investment in the different stages of modern commodity chains. Paradoxically, while these fragmented

national and subregional markets are close to each other, they have become increasingly open to trade with the world outside of the region (see chapter 6). As a result, the gap between national and subregional domestic production and increasing regional demand tends to be filled by non-African imports. Conversely, the fragmented national food and agricultural systems of African countries strive to produce for exports aimed primarily at international markets outside the region. To make things worse, agricultural subsidies and support measures of key trading partners of Africa typically encourage the continent's imports and hinder its exports. Thus, with an annual agricultural import bill of $15–$20 billion, one of the biggest challenges that Africa faces in market access is granting full access for the domestic food and agricultural systems to the regional (intra-African) market.

Adverse effects of HIV/AIDS on capital, land and agricultural production. HIV/AIDS exacerbates cash constraints due to expenses on illness and funerals and reductions in wage income by family members who take up care-giving roles. Evidence suggests that affected families sell productive assets (small animals, farm equipment, cattle, land) to meet these expenses (Yamano and Jayne 2004). This reduction in capital for agricultural production may limit the capacity of small-scale farmers to produce marketable surplus from farming activities. In addition, the sale of assets by poor households to wealthier ones may concentrate wealth and increase inequalities in rural areas over time. Women are particularly disadvantaged as a result of HIV/AIDS because they are the primary caregivers whose time is drawn away from income-earning activities as family members fall sick (Opiyo 2001).

As afflicted households lose family members who possess the rights to own and use land, disputes relating to use and inheritance may increase over time (Barnett and Blaikie 1992). Poor households and those headed by women may be especially disadvantaged by the loss of land rights. Although households that are no longer able to use their land would often prefer to rent it out, many, especially widows, are reluctant to do so for fear of eventually losing it. Current agricultural land policies do not provide adequate security of tenure for vulnerable households, particularly those headed by women—nor do they protect landowners who wish to rent land. Cumulative loss of land rights may lead to land concentration among the wealthy and hence increase income inequality in many countries (Lehutso-Phooko and Naidoo 2002). The loss of households' capacity to maintain productive assets may decrease agricultural productivity and production, hampering Africa's efforts to achieve a structural transformation.

> *HIV/AIDS deepens cash constraints for afflicted households*

The impact of HIV/AIDS deaths on agricultural production depends on the age, sex and position of the victim. The death of the head of the household in a poor household has detrimental impacts on production due to loss of off-farm income, reduced area cultivated, reduced labour for weeding and reduced use of other inputs due to lack of finance. Evidence from Kenya shows losses of up to 68 per cent of production when the male head of the household dies (Yamano and Jayne 2004). Other studies find negative impacts on the commercial sector due to rising costs and falling profits as a result of HIV/AIDS (Rugalema 1999; Fox and others 2003). To the extent that, as some evidence suggests, HIV/AIDS might induce farmers to move away from the production of high input crops (such as maize) to low input crops (such as cassava or sweet potato), the pandemic can have a profound impact on agricultural transformation, which requires a move to more high value marketable agricultural output.

Opportunities to modernize African agriculture

Africa must harness existing and emerging opportunities to foster agricultural development for a successful structural transformation of the continent. Positive trends towards democratization, decentralization and improved governance in Africa bring hope for greater participation of formerly excluded stakeholders in policy and public sector programme decisionmaking and implementation. Macroeconomic and sector policies in Africa are on a path of positive evolution as well, creating better incentives for the development of private sector initiatives (see chapter 7).

Recent land reforms in Africa demonstrate that many African governments realize the importance of providing access to land and security of tenure. The general consensus surrounding these initiatives is that both individual and collective land rights can foster sustainable land management practices and higher agricultural productivity. Therefore, the newer regimes of land reforms in Africa recognize land ownership both under customary and statutory tenure systems. To accompany land policy changes, some African countries are engaged in land regulation and administration reforms, mainly in the context of broader reforms emanating from recent democratization and decentralization (table 4.4).

At the regional level, the New Partnership for African Development (NEPAD) has provided several opportunities for African economies, including in the agricultural sector. NEPAD's Comprehensive African Agricultural Development Program highlights the importance of the agricultural sector to the continent's development by outlining areas in agriculture that should receive immediate attention, both in terms of international funding and local funding efforts through government budgets and private sector financing (box 4.1).

"Individual and collective rights foster sustainable land management practices"

Box 4.1
The Comprehensive African Agricultural Development Program

The Comprehensive African Agricultural Development Program (CAADP) is a NEPAD initiative that provides a framework to revitalize agriculture and rural development and achieve food security in Africa. The targets for the programme are that by the year 2015 Africa should have attained an average annual growth rate of 6 per cent in agriculture, developed dynamic domestic and regional agricultural markets, become a net exporter of agricultural products by improving market access and integrating farmers in the market economy, achieved a more equitable distribution of income, become more involved in agricultural science and technology development and used better natural resource management techniques.

The programme's initiatives address NEPAD's four thrusts in the area of agriculture and food security, mainly to extend the area under sustainable land management and reliable water control systems; improve rural infrastructure and trade-related capacities for market access; increase food supply, reduce hunger and improve responses to food emergency crises; and improve agriculture research, technology dissemination and adoption.

The four Comprehensive African Agricultural Development Program pillars and their corresponding programmes and initiatives include:

Box 4.1 *(continued)*

- Extending the area under sustainable land management and reliable water control systems (the land management programme and the water management and irrigation initiative).
- Improving rural infrastructure and trade-related capacities for market access (agribusiness, supply chain and quality control initiative and the regional trade facilitation initiative).
- Increasing food supply and reducing hunger (the regional strategic food reserves and risk management systems, homegrown school-feeding programme African nutrition initiative).
- Disseminating and adopting agricultural research technology (the multicountry agricultural productivity programme, the Pan-Africa cassava initiative, the Pan African NERICA [New Rice for Africa] initiative and the fish sector development programme).

In addition, the Comprehensive African Agricultural Development Program also includes two cross-cutting parts:

- Academic and professional training to strengthen capacity for agriculture and agribusiness.
- Information and knowledge systems to support strategy formulation, governance and implementation support for the Poverty Reduction Strategy Paper.

Source: *NEPAD 2004.*

"Nepad aims to revitalize agriculture too"

At the international level globalization offers hope for African agriculture through new market opportunities for new high value products, as well as foreign direct investment: access to biotechnology and improved information and communication technology. The biotechnological revolution holds great promise for increasing the productivity of food and agriculture systems, even more dramatically than the green revolution (Juma 1999). And revolutionary developments in information and communication technology have drastically reduced the cost of processing and transmitting information and, therefore facilitated access to information about agricultural technology, improved early warning systems, market opportunities, price and demand. If necessary capacities are built, increased access to information technology will offer new opportunities for agricultural education, agricultural research and agricultural extension, in addition to conveying information on markets, transport options, road conditions, weather and employment opportunities.

The rural nonfarm sector for employment and poverty reduction

The share of nonfarm income in rural households is 20–50 per cent in developing countries (Islam 1997). Reardon (1997) found that the main source of income for at least one member of every rural African household is a nonfarm enterprise. And, although only 10 per cent of

Table 4.4

Addressing land-related challenges through policy and institutional reforms

Land-related challenge	Example of policy response
Security of tenure	• Côte d'Ivoire's rural land plan seeks to identify and map all existing rights in order to give them legal status (Delville 1999). • Cameroon's 1974 land ordinance rescinded legal recognition of customary and communal tenure rights and imposed land titling as the only means of acquiring private ownership (Hobbs 1996). • Uganda's 1995 constitution transfers title from the state straight to landholders.
Conflict management	• Niger's 1986 rural code seeks to resolve land tenure conflicts (Lund 1993).
Decentralization of land administration	• Land boards were established in Botswana (now also in Namibia and Uganda), rural councils in Senegal, land commissions in Niger, community trusts and communal property associations in South Africa and land committees in rural Lesotho. • Public participation in decisionmaking through local institutions was improved. • Lesotho's 1998 land regulations require land committees to revoke an allocation in the event that the recipient refuses to adopt soil conservation measures.
Sustainable management of natural resources	• Mozambique's National Policy on Land of 1995 seeks to enforce ecologically sustainable use of natural resources. • The White Paper on Land Reform in South Africa shows that sustainability of production and the environment are key elements of the land reform process. • Land consolidation in Kenya helps in curbing land fragmentation and restoring production efficiency. • Maximum farm size regulations were introduced in Zimbabwe.
Land use development and agricultural productivity	• There are proposals for land taxation in Namibia's land policy • The Swynnerton Plan of Kenya supported African agriculture through agricultural research programmes, credit schemes, transfer of new technology and introduction of high value crops and a new set of institutions. • Ethiopia's agricultural development–led industrialization seeks to increase the productivity of smallholder farmers by dispersing fertilizers and improved seeds, establishing credit schemes and providing support services.
Equitable redistribution to reduce landlessness	• Redistributive land reform policies seek to give more land to landless blacks in Malawi, Namibia, South Africa and Zimbabwe. • Mozambique's 1998 land law recognizes the right to land through occupation on the part of rural families, based on oral testimony.
Development of land information system	• Kenya's tenure reforms sought to establish a well maintained registry that could be used to monitor land transfers and distribution and provide the basis for introducing property taxes.

Source: *UNECA 2004.*

"Everywhere Africa is addressing land-related challenges"

rural people are employed in the rural nonfarm sector in Africa, a disproportionately high percentage (42 per cent) of rural incomes is derived from rural nonfarm activities—more than inAsia (32 per cent) and Latin America (40 per cent) (table 4.5).

The rural nonfarm sector's role in rural development and poverty alleviation

The rural nonfarm sector integrates farming into the national and international value chains helping to transfer value addition to rural areas in the early stages of economic development (Start and others 2001; Davis and Bezemer 2003). At this stage activities of the rural nonfarm sector are closely linked to agriculture, the main employer of the rural labour force. Rural nonfarm enterprises are located mainly in the countryside and are related to the provision of agricultural inputs and services, crop processing and distribution. A dynamic agricultural sector is therefore associated with more rural nonfarm activity. In the second stage of rural nonfarm sector development rural-urban links become stronger, with workers commuting from rural areas to small towns for employment, and agroindustries grow rapidly, although farming is still important. The third stage sees greater emphasis on rural-urban links, more employment in nonagricultural activities and a move towards commercial agriculture. Sub-Saharan Africa is early in the first stages of rural nonfarm sector growth, while Latin America in the second stage and East Asia is in the third (Gordon and Craig 2001).

To the extent that rural nonfarm incomes help smooth out fluctuations or offset shortfalls in farm incomes, rural nonfarm activities contribute to poverty reduction. Rural nonfarm incomes allow households to overcome credit and risk constraints on agricultural innovation, permitting crucial farm investments to raise productivity and increase farm incomes (Tiffen and Mortimore 1992; Ellis 1998; Reardon and others 1998). In addition, the rural nonfarm sector provides employment for the landless poor. Indeed, about 60 per cent of the landless poor in Asia and 30–50 per cent in Sub-Saharan Africa depend on rural nonfarm employment for their livelihoods (Ellis 1998).

Table 4.5

Involvement in rural nonfarm employment (%)

Region	Share of income from rural nonfarm activity	Share of rural workers in rural nonfarm activity	Share of women in total rural nonfarm workforce	Share of rural nonfarm workers in manufacturing	Share of rural nonfarm workers in trade and transport	Share of rural nonfarm workers in other activities	Share of rural nonfarm workers in other services
Africa	42	10	26	24	22	24	30
Asia	32	24	20	28	26	32	14
Latin America	40	35	27	20	20	27	33
Eastern Europe	44	47	37	38	20	27	15

Source: *Haggblade, Hazell and Reardon 2002.*

Nonwage employment helps close the gap between the poor and the wealthy

Demeke, Guta and Ferede (2003) explored the links among growth, employment and poverty reduction and found that although the rural nonfarm sector alleviates destitution because it is a refuge for poor people, it cannot eradicate poverty on its own. While households with resources can have access to rural nonfarm activities that yield high returns, for the majority of rural workers the rural nonfarm sector provides only a low-level livelihood and a safety net. Some (Reardon and others 1998) have even argued that the rural nonfarm sector actually works best for those with resources and education: the ones who need it least.

The failure of most rural nonfarm sector interventions to adequately address poverty lies in the fact that they have focused on self-employment as an entry to the sector. However, self-employment in the rural nonfarm sector can reinforce unequal income distribution because self-employment is most accessible to wealthier, more educated people, especially men, who also control most of the household resources. If poverty reduction and equity are intended outcomes of interventions in the rural nonfarm sector, it is also important to focus on increasing opportunities for wage employment by encouraging the development of small and medium-size enterprises. Unlike self-employment, wage employment helps to close the gap between poor and wealthier households. Therefore, integrating poor people into the labour market can be a viable strategy for both income generation and equity.

Lessons from Park and Johnston's (1995) study of Taiwan Province on China's early stages of development suggest that small and medium-size enterprise growth responds to rural demand, especially if they are related to rural consumption (for example, food and beverages, tobacco manufacturing, textiles, wood, nonmetal furniture, transportation equipment), or if they trigger technological links (for example, metal workshops and enterprises for simple agricultural tools and spare parts). At later rural nonfarm sector development stages enterprises and industries that produce more complicated equipment for other markets may be viable. But in the initial stages labour-using, land-saving productivity-led growth enables broad-based farm and nonfarm cash income growth, which fosters rural demand links and poverty reduction.

Factors influencing growth of and participation in rural nonfarm sector employment

For rural nonfarm activities to increase employment and income creation and reduce poverty, they must be accessible to the poor. Understanding the factors that increase accessibility is therefore crucial. Gordon and Craig (2001) show that possessing capital enhances the capacity to access opportunities offered by the rural nonfarm sector. Their analysis cites five types of capital as crucial to participation: human, social, physical, financial and natural capital. As discussed earlier, growth in the agricultural sector is also key to developing a vibrant rural nonfarm sector.

Human and social capital. Skills, knowledge and health are the key elements of human capital needed to pursue different types of livelihood strategies, while social capital includes networks, relationships and trust, which people draw on in search of livelihood

opportunities. Personal factors such as level of education and vocational training, gender, health status and networks determine the level of human and social capital.

There is a positive correlation between education and rural nonfarm employment. Islam (1997) and Reardon (1997) argue that primary education enhances productivity, while secondary school education stimulates entrepreneurial spirit. Education increases one's ability to interact with key people important to rural nonfarm business opportunities. In addition to formal education, vocational training is important in providing specialized skills for business development (Reardon and others 1998; Lanjouw 1999; Bryceson 1999).

> *Nonfarm employment is inaccessible to many women*

Despite the fact that the majority of women live in rural areas, they are clearly disadvantaged in their access to rural nonfarm employment. This implies that gender is an important factor in determining rural employment in Africa (see chapter 2). Only 26 per cent of African women are engaged in rural nonfarm activities (see table 4.5). The lack of women's access to rural nonfarm employment can be explained by the fact that women are disadvantaged with regard to most factors key to job entry (education, financial capital, time and so on). Female heads of households are pushed towards rural nonfarm employment by the need to sustain their families. Because most of these women are in control of their income and other resources, they have an incentive to engage in rural nonfarm activities.

The health status of members of the household significantly affects their ability to engage in income-generating activities. HIV/AIDS, in particular, mainly affects people at the peak of their productivity, significantly hindering their participation in rural nonfarm employment. By constraining household time and resources, the pandemic also affects the participation of other household members, particularly women. Some of the coping strategies adopted as a result of HIV/AIDS, for example withdrawing children from school, can also have long-term impact on participation (White and Robinson 2000). The presence of sound healthcare systems improves participation in employment by reducing morbidity, improving nutrition and increasing labour productivity and rural incomes (Islam 1997).

Social bonds formed at school and elsewhere have often proved crucial to success in rural nonfarm activities. Fafchamps and Minten (1998) show that social capital in the form of social networks can reduce transaction costs and increase access to economic activities through better access to key information on markets, jobs, loans and other resources. One can deduce that social capital can increase employment and access to rural nonfarm activities. Unequal distribution of social capital can also lead to unequal access to rural nonfarm employment. Results from Africa show that group strategies have the potential to increase or concentrate social capital and help address credit and market access constraints, access to services and overcome barriers to entry. These strategies include producer groups and women's self-help groups with common income-generating activities.

Financial capital. Financial resources such as savings, credit, remittances and pensions constitute financial capital, which is important to engaging in activities, whether in farm or nonfarm sectors (Gordon and Craig 2001). Without adequate financial capital, households remain in those activities which have fewer barriers to entry and, unfortunately, low remuneration. Access to credit, especially reasonable size loans with a realistic maturity, is vital.

Without it, ownership of assets (such as cattle) is important to investing in rural nonfarm activities. Microfinance schemes with assistance from nongovernmental organizations and donors has proven useful in increasing access to credit. In a study of four African countries Bagachwa and Stewart (1992) found that in 30–84 per cent of rural industries poor access to credit was a limiting factor to business development. Market failure in credit provision relates to inadequate and expensive information on borrowers, inadequate mechanisms for enforcing payments, high costs related to remoteness of rural areas and small sizes of loans, among other items.

Physical capital. Basic infrastructure (including transport, communication, energy and water) complement individually owned production equipment and buildings in the development of rural nonfarm activities. High transaction costs, incurred due to poor infrastructure, deter rural nonfarm sector development. Availability of rural nonfarm jobs is associated with good infrastructure, high market density and high population density, particularly in the form of rural towns (Reardon and others 1998).

Box 4.2
CAMPFIRE, Zimbabwe: community-based natural resource wildlife management

Zimbabwe's Communal Areas Management Programme for Indigenous Resources (CAMPFIRE) began in the mid-1980s and provides a legal and managerial framework to assist local communities in sustainably managing their entire ecosystem (plants, animals and people). By 1993 the programme covered 26 six districts, and each village had a wildlife committee responsible for counting animals, conducting antipoaching activities and resolving conflicts. Community game scouts are trained to assist as game rangers. Hunting quotas help monitor and maintain wildlife populations with the help of the Department of National Parks. The World Wildlife Fund assists with aerial surveys, while villagers carry out surveys and mapping on the ground. Regular workshops are held to collate and reconcile information from the various sources.

Benefit to the communities

The activities that provide employment and income from CAMPFIRE include trophy hunting concessions to hunters and safari operators (90 per cent of income), selling wild animals with populations beyond their carrying capacity, harvesting and selling natural resources such as crocodile eggs, caterpillars and river sand, as well as skins and ivory from "problem animals", tourism and selling wild meat.

The programme has created jobs for local people and provided training for local communities as environmental educators, guides and game scouts, among others. In addition, about 80% of the income from the programme goes to the local communities, which collectively decide how to spend it, and 20 per cent is used for administering and managing the projects. Incomes from the programme have contributed to local service provision and infrastructure development—for example, building clinics and schools, drilling wells and erecting fences and roads. During famines the funds contribute to food purchases for the local communities. CAMPFIRE is estimated to have increased rural incomes by 25 per cent.

Source: *http://www.globaleye.org.uk/archive/summer2k/focuson/mars_pt1.html.*

In addition to facilitating rural nonfarm sector growth by reducing transaction costs, roads, electricity and telecommunications infrastructure enhance rural town development (Ellis 1998). These towns in turn facilitate local intersectoral links and serve as market outlets for local manufactured goods and services. They are also employment centres for commuters from rural farms, and they provide services for farm workers, such as retail shops, restaurants, petrol stations and the like. Rural towns are where agroprocessing usually takes place, due to the support services, access to transport and other infrastructure available. Rural towns are also important as intermediate marketing centres, linking rural remote areas to more developed markets elsewhere.

Natural capital. Natural resource endowments, including land, water, wildlife and minerals, help to determine the nature of rural nonfarm activities. Activities such as timber processing, fishing, mining, construction and tourism depend on the resource endowments of a certain area. Natural resource endowments need other factors if they are to facilitate rural nonfarm activities. Box 4.2 provides an example of how the presence of wildlife can help stimulate rural employment and growth through community-based management in Zimbabwe.

> *Mechanization, in later stages, leads to surplus labour*

Agricultural development

Experience based on Asia's green revolution and partial success in Africa shows that agricultural development is crucial to the development of rural nonfarm activities and employment (box 4.3). Indeed, agriculture is the single most important factor to growth in the rural nonfarm sector. Agricultural surpluses enable growth of upstream and downstream activities, providing inputs to the rural nonfarm sector. As intensification occurs during the early stages of agricultural transformation, rural labour shortages may be absorbed in agriculture. However, mechanization in later stages leads to surplus labour, which can be absorbed through rural nonfarm activities. While agriculture is important to rural nonfarm sector growth the inverse is also true: growth in the rural nonfarm sector fuels and facilitates agricultural growth.

Box 4.3
Using a green revolution for rural transformation, employment and poverty reduction: lessons from Uganda

The Luwero Triangle is an area in central Uganda that was devastated by war in the 1980s. When the rural population returned after the war, the people faced problems relating to the low productivity of bananas and other crops, limited infrastructure (including roads, markets and electricity), poor market integration and the devastating impact of the HIV/AIDS pandemic. In 1998 researchers at the Uganda National Banana Research Program at the Kawanda Agricultural Research Institute started to work with farmers and other sectors (including health and education) to design an integrated rural development strategy that focuses on banana production.

Using participatory techniques for scientific, technological and communication development, researchers, extension workers, farmers and participants from other sectors set out to introduce

Box 4.3 *(continued)*

modern and improved varieties of high yielding banana seedlings, increase the use of manure, introduce modern scientific management of water, soils, pests and diseases and encourage market-oriented production.

So far, rural nonfarm activities, ranging from processing, marketing, infrastructure development and even public administration, are being stimulated with concomitant employment creation in the Luwero Triangle. For example, groups of young men have gained employment by providing motorcycle transport services ("bodaboda") to move the increased yields in bananas, coffee and passion fruit to markets. Village processors are producing banana chips, banana flour, banana juice and Uganda Waragi (a potent distilled gin popular across the Great Lakes Region). These village processors are connected to Kampala-based transporters with lorries, who convey the produce to national, regional and even overseas markets. This is the beginning of small and medium-size enterprises joining the value chain.

Source: *UNECA 2003.*

"Small and medium enterprises begin to join the value chain in Uganda"

Recommendations for achieving structural transformation in Africa

To improve the lives of millions of poor people, Africa's economies must provide jobs that facilitate decent standards of living by addressing the challenges related to achieving a demographic transition, slowing the spread of HIV/AIDS and mitigating its impacts on the economy, transforming agriculture and developing a rural nonfarm sector.

Achieving a demographic transition

Lessons from Botswana, Mauritius and Tunisia, which have made significant gains in achieving a demographic transition, point to the importance of strong economic performance accompanied by better education and access to health as crucial factors to achieving a demographic transition (UNECA 2001). The experience in these countries also shows that socio-cultural changes are crucial to achieving a demographic transition. Efforts to reduce fertility rates should aim to:

- Increase the age at which women have their first child by, for instance, enacting and enforcing marriage laws.
- Increase education and employment opportunities for women and girls to empower them to be more involved in decisions relating to marriage and child bearing. Education and participation in the labour force also increase the opportunity cost of rearing children, thus reducing fertility rates.

- Reduce unintended births by meeting the unmet need for contraceptives. This would not only reduce fertility, but also reduce maternal mortality by reducing the number of abortions and deaths among high-risk mothers.

Controlling the spread of HIV/AIDS is necessary to facilitate a demographic transition, while human capital development is necessary for a structural transformation of Africa's economies. It is thus recommended that African governments, their development partners, civil society and other stakeholders scale up their support to HIV/AIDS programmes for prevention, treatment and care by:

- Harnessing lessons on how governments, communities and households are coping with the effects of HIV/AIDS to provide useful insights into how Africa can mitigate the impact on structural transformation.

- Working through existing indigenous community mechanisms with a view to strengthening indigenous responses to the AIDS pandemic.

- Mobilizing financial resources to strengthen the campaign on HIV/AIDS awareness and prevention using all available media.

- Strengthening Africa's participation in processes aimed at scaling up treatment, including the procurement of affordable drugs.

- Strengthening human and financial capacity to respond to needs related to prevention, treatment and care.

> *Strengthening indigenous responses to HIV/AIDS help communities tackle the pandemic*

Transforming African agriculture

Addressing challenges related to agriculture in a comprehensive and integrated manner is crucial to triggering a structural transformation for job creation and poverty reduction. This can be achieved through decisive efforts to expand appropriate research, knowledge and technology for increased productivity at all stages of the agricultural commodity chains; improve the management of water resources; catalyze land policy and associated institutional reforms; address crucial market development and market access issues; and mitigate the impacts of HIV/AIDS on agriculture.

Harnessing technology for agricultural transformation.

It is recommended that Africa:

- Harness both conventional green revolution as well as emerging gene revolution technology to make significant headway towards sustainable agricultural development and food security. In so doing, Africa must harness both the public and private sectors in research as well as in technology development and dissemination to seek out and use these opportunities.

- Increase public funding to research but also foster partnerships with the private sector, specifically in areas that are attractive to the private sector (such as crop and livestock breeding), and assimilate and adapt new technological advances in molecular biology, especially for cash crops. By contrast, the public sector should continue to focus on improving farming systems, farming practices and environmental sustainability.

- Diffuse technology by providing innovative extension services through partnerships with farmers and the private sector and by using information and communication technology.

Developing and managing water resources. To face the challenge of managing water resources to transform agriculture and the rest of the economy, African countries and their development partners should seek to:

- Significantly increase the total agricultural area under irrigation over the next decade by providing loans, grants and technical assistance to small-scale systems managed by local associations and by facilitating large-scale irrigation projects where appropriate.

- Develop the irrigation potential of the major river basins by creating an enabling legal and institutional environment and public-private partnerships.

"Improving water resource management can transform agricultural practice"

Box 4.4
Progress on implementing the African Water Vision 2025

The African Water Vision 2025 was launched at the Second World Water Forum held at The Hague, Netherlands, in March 2000. There the chief executives of the Organization of African Unity (now the African Union), the United Nations Economic Commission for Africa and the African Development Bank requested real and concerted follow-up actions. A technical meeting in Addis Ababa divided tasks among the three regional organizations as follows:

- The African Union would mobilize political support and enhance political will for the implementation of the vision.

- The United Nations Economic Commission for Africa would mobilize UN systemwide capabilities for technical analysis for implementation.

- The African Development Bank would mobilize financial resources for the implementation of the vision.

To date a fruitful process of raising awareness on the critical role of water for African development has been successful. Achievements include:

- The formation of the African Minister's Council on Water and its engagement in partnerships with the European Union, the Group of Eight and many other development partners.

Box 4.4 *(continued)*

- Technical analysis led by the UN system organized as UN-Water/Africa has resulted in projects, programmes and initiatives such as Water for African Cities led by the United Nations Human Settlements Programme, the African Water Development Report and Information Clearing House led by the United Nations Economic Commission for Africa and numerous other smaller initiatives, including Water as an Instrument of Regional Integration and Gender and Water Resources Management in Africa.

- Financial resource mobilization led by the African Development Bank has resulted in initiatives such as the African Water Facility and the Rural Water Supply and Sanitation Initiative. Operational since May 2005, the African Water Facility has raised $80 million towards its goal of $600 million.

Source: *UNECA, OAU and AfDB 2000; UN-Water 2004; AU 2004.*

- Harness and build partnerships at the subregional and continental level to mobilize finances and political will, as happened with implementation of the African Water Vision 2025 (box 4.4).

Enhancing land policy formulation and implementation. It is recommended that Africa:

- Continue to undertake land tenure reforms that legally recognize the different types of socially legitimate types of land ownership (both communal and private), drawing on current land policies and reforms in Africa.

- Promote female ownership of land in rural communities and devolve formal power to local communities and individuals in managing natural resources.

- Build capacity in institutions of land administration, including traditional organizations where appropriate, to speed the implementation of land reform.

- Examine complementary laws, such inheritance laws, with a view to making them consistent with the land reform agenda.

The African Water Vision 2025 means political support for water management

Market development and access. Addressing the problem of market development and access calls for major efforts at the national, regional and international levels.

At the national level there is a need to:

- Deepen and complete agricultural policy reforms and market restructuring processes under way by adopting institutional, legal and financial frameworks that promote private investment in agribusiness and agroindustrial enterprises. Emphasis should be placed on small-scale industries capable of diversifying food and agricultural products, supplying agricultural inputs in a timely manner and providing basic transport and marketing services.

- Significantly increase the density of rural and feeder road networks, with greater involvement of decentralized rural communities in direct investment and maintenance to create rural employment.
- Enact appropriate regulations on product standards to improve the quality and increase the competitiveness of food and agricultural products.

- Promote the development of strong and effective market information systems by devising ways to mobilize private participation for building and strengthening national systems of market information collection and analysis and dissemination. The Kenya Agricultural Commodity Exchange provides an example of how harnessing information and communication technology to provide marketing information can help integrate agricultural markets and increase returns to farming for actors along the agricultural commodity chain (box 4.5).

At the regional level efforts to improve regional economic integration and cooperation should be guided primarily by efficiency and comparative advantage rules. Some initiatives are already under way to enhance regional integration by harnessing private-public partnerships to improve market access (box 4.6).

At the international level Africa must continue the dialogue with its development partners, encouraging them to enhance coherence in their support policies and interventions. The promotion of regional integration should be included in their efforts to assist African countries in agricultural sector reforms.

Mitigating the impact of the HIV/AIDS pandemic on agriculture. Mitigating the effects of HIV/AIDS on rural households and communities will go a long way in facilitating a transformation of agriculture and growth in other sectors of the economy. In this regard, it is recommended that African governments, development partners and other stakeholders:

- Develop functioning land rental markets and help afflicted households earn revenue from renting unused land.

- Mainstream gender equality and minimize other forms of discrimination in development policies and strategies, including policies related to land tenure security, access to water and fuel.

- Intensify technology transfer for animal health to increase the stock of healthy livestock and develop draft rental markets.

“Private-public partnerships enhance regional integration”

Box 4.5
Harnessing information and communication technology for market access in Kenya

The Kenya Agricultural Commodity Exchange (KACE) was launched in 1997 to harness information and communication technology in order to link sellers and buyers of agricultural commodities and provide timely marketing information. KACE's market information services use several types of information and communication technology–based media: market information points, market information centres, short messaging services, interactive voice response service, regional commodity trading and information systems and a website. Through these avenues, KACE collects, processes and disseminates information to clients—including farmers, including smallholder farmers in remote rural areas, commodity dealers, exporters and importers—at different stages in the agricultural commodity value chain.

At the 11 market information points located in rural market centres across the country, marketing information on prices is collected and disseminated to buyers and sellers using bulletin and writing boards. The market information points also serve as a trading floor to link buyers and sellers of commodities in a transparent and competitive manner. Market centres have electricity and telephone access, and market information points are linked by Internet, email and telephone to the KACE headquarters in order to facilitate the flow of marketing information among points and hence link buyers and sellers across the country.

Market information centres are located at district headquarters and are equipped with telephones (landline and mobile), fax and computer (with email and Internet) access. They manage and service the market information points in remote market centres without electrical power supply or fixed-line telephone services by linking market information points and KACE headquarters.

The KACE headquarters processes information received from market information points and centres and sends it directly back to the points or through the centres. This information is downloaded and displayed at the market information points, where users access the information free of charge. Costs are recovered as part of the fees and commissions for trade transactions. Information provided includes prices of various commodities in different markets in Kenya, Tanzania and Uganda. Depending on demand, this information is also available at the international level. KACE hopes to expand the scope of information provided to include input supply and access, storage, credit, transport and agricultural extension.

Through an short messaging service marketing information service called SMS Sokoni, KACE also provides information to mobile telephone users in partnership with one of the mobile service providers in Kenya. Callers can also call a landline to get information using the interactive voice response system. The regional commodity trading and information systems database of buyers, sellers, importers and exporters—as well as the KACE website—are also viable sources of KACE information.

Source: *www.kacekenya.com.*

Intervention in rural nonfarm economy

To increase jobs and income, particularly for poor people in Africa, African governments, the private sector and other actors need to facilitate growth in the rural nonfarm economy and ensure poor people's access to these activities by:

- Adopting a market-oriented approach by focusing on producing goods and services that have high marketing prospects and that can meet marketing requirements.

- Identifying markets that are low-risk, expanding and within the reach of producers. Involvement in regional markets is useful because they allow for learning before engaging in international markets.

- Promoting market links by facilitating information flows and communication between producers and input suppliers and buyers. Links can be fostered by organized visits to markets, participation in trade fairs, organized contacts between producer and other subsector players, providing information to producers and consumers.

- Stimulating demand by providing information to consumers in order to encourage their loyalty. Labelling products can provide information on standards and product characteristics. Information can also be provided in trade fairs and through the media. Providing free samples and discounts have also proved viable ways of stimulating and maintaining demand. Strategies to stimulate demand require training and linking producers to relevant private and public institutions in order to benefit from group advertising and promotion, as happens in national advertising for tourism.

"Industrial cassava substituted imports in 15 industries in four countries"

- Increasing human capital through training.

- Increasing access to credit by providing support to credit cooperatives and microcredit organizations and group savings initiatives. It may also be useful to provide subsidies to facilitate access to loans.

- Improving access to infrastructure such as roads, power, water supply and telecommunications.

- Supporting research and development in improved inputs to ensure the availability and use of the cost-reducing and quality-enhancing technology, inputs and equipment in rural nonfarm activities. Private investment in manufacturing equipment, marketing and repairs is crucial. Box 4.7 shows how providing infrastructure (for example, energy) to poor rural women in Mali has created employment opportunities and empowered women to lift themselves out of poverty.

- Promoting producers organizations to overcome the constraints emanating from the small size of enterprises by benefiting from economies of scale in production, marketing and service provision. Successful producer associations require a participatory method to group development with a genuine grassroots approach.

- Forging institutional coalitions by identifying and appropriately defining the roles of various actors.

Box 4.6

Private-public partnerships to expand markets for strategic crops in the South African Development Corporation

As part of a joint partnership between the United States Agency for International Development and the South African Development Corporation, countries in Southern Africa are increasing rural incomes and food security using a market-based strategy to commercialize dry land agriculture and increase the adoption of improved crop varieties and animal health products. The initiative, which started in 2000, seeks to address market constraints relating to nontariff barriers such as grades and standards, sanitary and phytosanitary regulations, transfer of germplasm and intellectual property rights of selected countries—each with a comparative advantage in certain commodities. The initiative looks to expand markets for technology and outputs for commodities, including sorghum, millet, cassava, sweet potato and heartwater (used to control tick-borne diseases).

So far the programme has supported the adoption of 21 new technologies, including a mechanical grain cleaner for removing stones from sorghum before milling. Similarly, the introduction of a chipping and flour-making machine to farmers in Malawi has resulted in the production of better quality cassava chips, flour and starch. Farmers sell these high value products directly to private industry, thereby increasing their incomes.

The South African Root Crops Research Network has been key in establishing multiplication sites of new varieties, which are then sold to farmers by the private sector. The participation of the private sector in commercializing technology, particularly nurseries established by nongovernmental organizations and farmer organizations, has resulted in the planting of 229,000 hectares of new varieties of cassava and 13,000 hectares of new varieties of sweet potato. The sorghum sector has also benefited, with approximately 296,000 farmers, 15 per cent of total sorghum farmers in the region, now using improved seed. The initiative has also facilitated the sharing of millet and sorghum germplasm, generated genotypes for commercialization and promoted alternative seed delivery systems.

Education and advocacy in market expansion have increased the use of industrial cassava as a substitute for imported products by 15 industries in four countries. Four industrial consumers in Malawi have increased use to 1,160 tons, with the potential to increase it to over 7,000 tons. Many industries report lower input costs as a result of substituting imported inputs with local inputs. For instance, one textile manufacturer in Malawi reported saving $108,000 a year by using local cassava starch. In addition to industrial growth, introducing technology for these drought-resistant strategic commodities has increased food security.

Source: *USAID 2004.*

"African governments need to become more market-oriented"

Box 4.7

Empowering women by improving provision of modern energy services: the multifunctional platform in Mali

Beginning in 1993 the United Nations Industrial Development Organization and the International Fund for Agricultural Development initiated a programme to supply labour-saving energy services and promote the empowerment of women by providing a multifunctional platform to rural villages in the Sikasso region. A typical multifunctional platform consists of a small diesel engine mounted on a chassis to which up to a dozen pieces of end-use equipment can be attached in order to provide a variety of energy services, including motive power for agricultural processing (grinding and husking mills, vegetable and nut oil presses) and electricity for lighting, welding, battery charging or pumping water.

In most of the villages where platforms were installed, the programme has primarily benefited women by providing them with energy services that replace traditionally time-consuming and labour-intensive activities. It has also helped alleviate the drudgery of survival activities and increased income-generating opportunities for women. In addition, the programme has helped develop the skilled workforce necessary to operate and maintain the platforms and provide new business opportunities and a source of income for the women who own, operate and manage the platforms.

The multifunctional platform programme in Mali has proved a cost-effective approach to reducing energy poverty in rural areas and empowering women by creating income-generating opportunities through affordable modern energy services. Experiences and lessons learned have been so encouraging that the United Nations Development Programme has decided to expand the initiative to other West African countries and to launch a regional multifunctional platform programme covering Burkina Faso, Guinea, Côte d'Ivoire and Senegal.

Source: *www.ptfm.net*

Conclusions

This chapter reiterates the call to Africans, African governments and their development partners to increase efforts towards achieving a structural transformation of the continent. Such a transformation would offer millions of unemployed and underemployed Africans the chance to attain meaningful employment and achieve a decent standard of living.

A structural transformation in Africa will need concerted efforts towards completing Africa's demographic transition. This requires that Africa catalyze its efforts to reduce fertility and improve social development by adopting programmes and policies to increase employment opportunities and access to education for women and meeting the need for contraceptives. Achieving a demographic transition and structural transformation also requires that Africa address the HIV/AIDS pandemic by scaling up prevention, treatment and care programmes.

Structural transformation of African economics calls for broadening the analytical and programmatic perspective beyond the narrow confines of sectoral development. With respect to the agricultural sector, it requires taking a broader view of the food and agricultural system, which encompasses an integrated approach to investing in improving productivity and efficiency at all the stages of the commodity chains, from research and development to input markets, farm-level production, processing, storage, handling, transport and distribution (marketing and trade) to the final consumer. The links among these stages are key to achieving optimal contribution of the food and agricultural system to broad-based economic growth and transformation through more value-added and income-generating employment. The food and agricultural system, therefore, should be conceived of as encompassing the farming sector and the agribusiness industrial and services sectors. Consequently, agroindustrial and agribusiness development and a green revolution must go hand in hand.

Facing challenges in African agriculture is necessary to ensure that agriculture indeed serves as an engine of growth in a structural transformation of African economies. To achieve significant improvements in agriculture, Africa should harnesses technology by strengthening agricultural research and extension; developing and managing water resources at both the national and regional levels, with a view to increasing the amount of land under irrigation; catalyzing land reform to provide access and security of land rights and hence facilitate private investment in land; and developing and facilitating access to markets, particularly by completing marketing reforms, increasing infrastructure and information systems, facilitating regional integration and pushing for increased access to international markets. In addition, Africa must mitigate the impacts of HIV/AIDS on agriculture by developing and disseminating labour-saving technology; improving healthcare, water provision and sanitation; and addressing gender disparities that make women and children especially vulnerable to poverty.

“Agribusiness must be part of an African Green Revolution”

Enhancing the links between agriculture and other sectors requires a vibrant rural nonfarm sector—crucial to sustaining growth in the agricultural sector and key for amplifying growth effects in agriculture to other parts of the economy. The rural nonfarm sector is therefore needed to achieve broad-based economic growth that is capable of providing employment and reducing poverty. To facilitate the growth of the rural nonfarm sector, efforts to transform agriculture must be accompanied by incentives for market-oriented production of goods and services as well as growth of rural towns. These incentives include facilitating the growth of rural financial institutions to provide credit, providing education and vocational training, promoting market links, building infrastructure (for example, feeder roads, electricity, water), encouraging participatory management of natural resources and providing a conducive business environment through supportive macroeconomic and fiscal policies.

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Chapter 5

Meeting youth unemployment head on

At 21 per cent, youth unemployment in Africa is much higher than the world average of 14.4 per cent and second only to the Middle East and North Africa's 25.6 per cent. The high share of young people (ages 15–24) in Africa's population contributes to the severity of the problem.

There are notable differences in youth unemployment with regard to gender. The unemployment rate for young women in Sub-Saharan Africa is 18.4 per cent–lower than the unemployment rate for young men (23.1 per cent)–but young women's labour force participation is lower as well. The lower unemployment and labour force participation rates for young women indicate the impact of cultural norms and role models, which restrict women's employment options to unpaid household work. A further disadvantage for girls is their limited access to education, as compared with boys, which also limits their prospects for jobs in the formal labour market.

"Youth unemployment in Africa is ranked second in the world"

Youth unemployment in Africa also has a geographical dimension: it is generally higher in urban areas than in rural ones. However, the lower youth unemployment figures in rural areas are likely to mask a significant amount of underemployment in low productivity smallholding agriculture. In fact, countries with a large formal agricultural wage sector, such as Kenya and São Tomé and Principe, have high youth unemployment in rural areas.

Several factors account for the high youth unemployment rate in Africa, most notably low economic growth, which is manifested in low economic activity and low investment. Low economic activity entails low overall job creation. Given the sustained population growth rates, labour markets are not able to absorb all the newcomers, resulting in scarcity of jobs, which leads to more selection by education and experience; precisely the assets that young people are struggling to acquire.

Lower enrolment rates, coupled with low completion rates, low quality of education and a failure to orient curricula with the needs of the private sector have contributed to the mismatch of skills of youth labour markets in Africa. Limited formal work experience and a lack of general and job-related skills also put young Africans at the end of the hiring list. The situation further deteriorated in the 1990s when downsizing meant that the public sector ceased absorbing qualified labour. Consequently, a rapidly growing informal sector has become the "sponge" that provides job avenues to all categories of youth labour, including skilled workers.

The health status of young people affects their employment situation. Young people who are HIV-positive eventually become ill with HIV-related diseases, which can increase their

absence from work, reduce their productivity and lower their chances of being employed. If left untreated, people are ultimately unable to work.

Unemployment has social as well as economic consequences for young people. Unemployed young people are forced to find alternatives to generate income, including activities in the survival-type informal sector and, in extreme cases, criminal activity. Urban youth unemployment is further exacerbated by rural-urban migration. Rural migrants believe that more jobs and social opportunities are available in urban areas, but once in the cities they find themselves without a job and with limited social networks. Trapped and discouraged by bleak job prospects, some turn to the sex, criminality and drug industries to survive.

Youth joblessness also implies missed opportunities in the use of human resources to produce goods and services. In addition, smaller tax revenues result from a smaller tax base for income tax and indirect taxes such as the value added tax. A further implication is related to security. An increase of one percentage point in the ratio of people ages 15–29 to people ages 30–54 increases the likelihood of conflict such as civil unrest or war by 7 per cent. Higher crime rates also have a direct economic cost in terms of loss of foreign direct investment. For example, foreign investors have cited crime as the most serious deterrent to investing in South Africa. If young people continued in secondary education, one possible consequence could be a reduction in the crime rate.

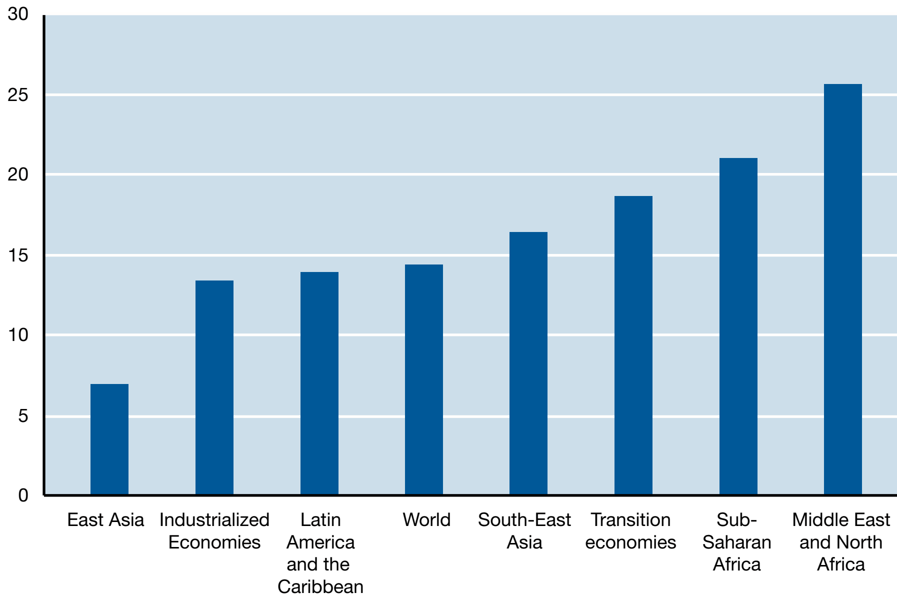
Tapping into the unused potential of unemployed young people could prove a crucial asset for economic development on the continent. Rather than accepting unemployed young people as a burden to society, there is an urgent need to focus on youth employment or occupation policies and to mainstream those policies into a larger development strategy framework. Well targeted youth policies—and specifically national employment policies—public spending directed at young people, projects to tackle rural employment, and the creation of job centres should be an integral part of such a strategy. Public work programmes and internships through public-private initiatives aimed at young people can provide them with an entry to the labour market and improve access to and equity in education. Guided by the needs of the private sector, they can also enhance the quality, curriculum content and resource allocation of the education system. In this regard, it is particularly important to engage young people in monitoring public resource spending.

Africa's youth unemployment: a reason for concern

The youth population in Sub-Saharan Africa was estimated at 138 million people in 2002-2003, with 28.9 million, or 21 per cent, of them unemployed.[1] This is the second highest youth unemployment rate in the world, exceeded only by the Middle East and North Africa, where youth unemployment is 25.6 per cent (figure 5.1). East Asia has the lowest youth unemployment rate with only 7 per cent.

As the fastest growing labour force in the world on current trends, Sub-Saharan Africa's youth labour force will be even more difficult to accommodate in the future. In fact, the

Figure 5.1
Youth unemployment rates, by region, 2003 (%)



Source: *ILO 2004b.*

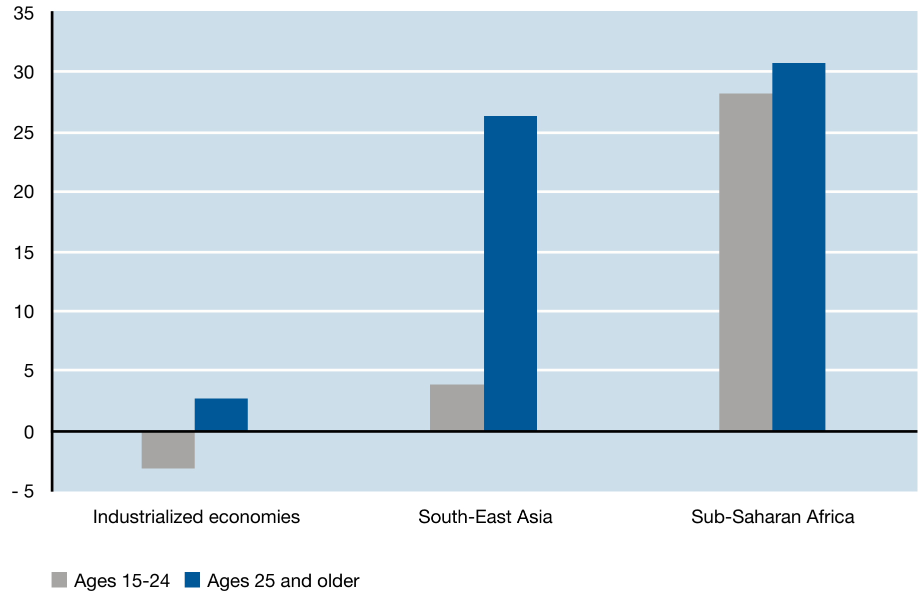
ratio of youth unemployment to adult unemployment was 3.6 in 1993 and remains virtually unchanged at 3.5 in 2003. Over the last decade the rate of youth participation in employment in Sub-Saharan Africa rose from 64.4 per cent to 65.4 per cent, but it dropped in the rest of the world–from 58.8 per cent to 54.9 per cent–as young people entered the workforce later due to more time spent on education (ILO 2004b).

The situation of young people in the labour market is aggravated by the fact that the formal labour market is still small. Young people are often at the end of the job queue for the formal labour market because they lack adequate skills and experience, as well as efficient social networks. Excluded from reasonably paid formal employment, young people are left with atypical or vulnerable forms of formal employment with low pay or the informal sector, where legal protection is limited. As a result, the bulk of young people are engaged in easy-entry informal sector activities with low returns and long hours of work, including street vending, car washing and watching, and making and selling crafts. Numerous young people are compelled to perform jobs with the lowest level of protection, even though they are among those who need the most protection.

A significant number of young people are discouraged by an unsuccessful job search and leave the formal workforce entirely. A survey in South Africa revealed that 39 per cent of unemployed young people have almost given up actively searching for a job and 47.1 per cent gave up because they found no job opportunities in their areas. Some 23.5 per cent said that they could not afford transportation to look for work. And 57 per cent had in-

Figure 5.2

Projected regional labour force growth, by age group, 2003–15 (%)



Source: *ILO 2004b.*

> *Fertility rates are declining at a much slower pace in Africa*

quired at workplaces, farms and factories or called other possible employers, but only 6.9 per cent had registered at employment agencies or trade unions (Kanyenze, Mhone and Sparreboom 2000). The survey illustrates the lack of transparency in the labour market, where employers and potential employees are unable to advertise jobs or qualifications, making it more difficult and costly to actively search for a job.

Demographic factors affect youth unemployment

The fast growth in Africa's youth population is a major factor in youth unemployment, with the demographic situation especially serious in Sub-Saharan Africa. Still high, fertility rates are declining at a much slower pace than in the rest of the world. On current economic growth rates, future increases in the youth labour force do not bode well for the labour market. The youth labour force in Sub-Saharan Africa is projected to grow by 28.2 per cent between 2003 and 2015, compared with a mere 3.8 per cent increase in South-East Asia (figure 5.2) and a 3.1 per cent decline in industrialized economies (including the transition economies). This sharp increase in youth population will boost the supply of young people in the labour market, further constraining job creation. Sub-Saharan Africa is also the only region where adult and youth labour forces will grow at a similar rate, around 30 per cent, with further adverse repercussions for the youth labour market (ILO 2004b).

Lower unemployment rates for young women–but also lower labour market participation rates

At 18.4 per cent the female youth unemployment rate is lower than the 23.1 per cent male youth unemployment rate, though the share of young women participating in the labour market is lower than for young men (ILO 2004b).

> *Cultural norms keep women away from labour markets*

A large number of young women work in the household, where their labour is not accounted for in the system of national accounts. This situation is especially common in urban areas, where the share of women working exclusively in the household is higher than in rural areas. For example, in Zambia 39 per cent of urban young women work at home, compared with half that figure in rural areas (Leibbrandt and Mlatsheni 2004). In several African countries cultural norms and the absence of appropriate role models hamper young women from actively searching for a remunerated job. Many young women are not counted in unemployment statistics because they have simply never actively searched for a job in the formal sector. Informal sector participation among women is so high because women find it easier to combine work in the informal sector with their household duties. If more women started to actively search for formal sector jobs, their recorded unemployment rate would be higher.

Women are also underrepresented in higher education, where the number of young men enrolled is higher. In effect, while many young men are studying, women of the same age support the family and work in the household. Literacy rates for young men ages 15–24 are significantly higher than for young women in the same age group. In Guinea 48 per cent of young men in urban areas are in school, compared with only 22 per cent of young women (Leibbrandt and Mlatsheni 2004).

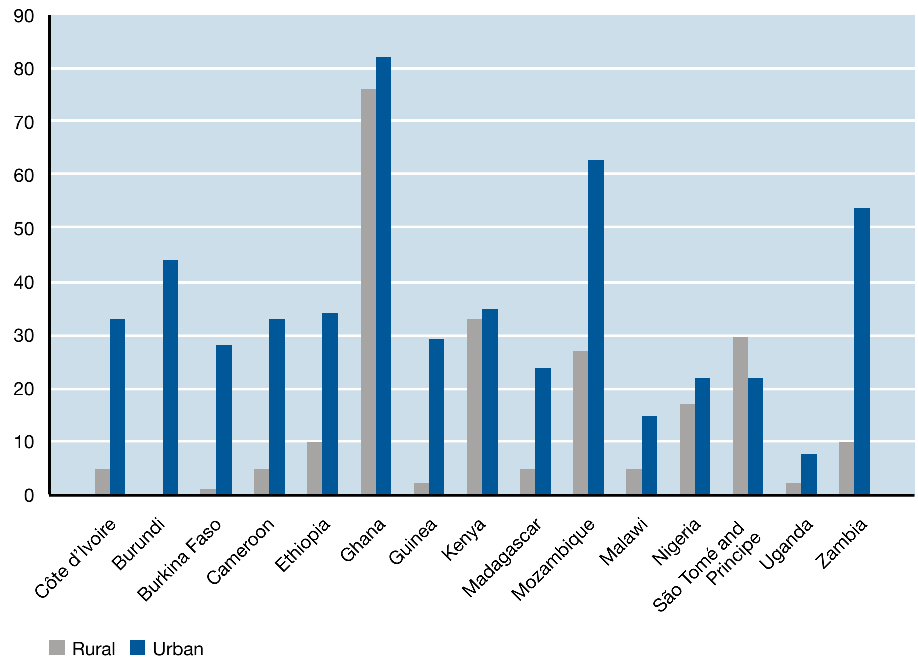
Rural underemployment and urban unemployment

Youth unemployment in urban areas is generally higher than in rural areas. In rural areas most employment is in small-scale agriculture, which is why official unemployment levels are low. With incomes meagre due to low productivity, rural areas have more underemployment. But rural unemployment is high in countries with commercial farms and a formal agricultural wage sector, such as Kenya and São Tomé and Principe (figure 5.3). In Kenya, for example, rural youth unemployment has reached 33 per cent (Leibbrandt and Mlatsheni 2004).

In all cases rural exodus continues to be a problem. Many young people migrate to urban areas to find a job with higher remuneration, but jobs in urban areas are not easy to find. Urban employment generally accounts for only a small share of total employment. Once in the cities, these young people might face unemployment as well as underemployment (UN 2003). Migration to urban areas can also be attributed to other non-job-related reasons, including ethnic tension, which is less prevalent in urban areas, or the desire to live in an urban area with more amenities.

Figure 5.3

Rural and urban youth unemployment rates in selected African countries, (%)



Source: *Leibbrandt and Mlatsheni 2004.*

The roots of youth unemployment are deep

Young people are at a disadvantage on the job market thanks to a combination of poor economic performance and limited availability of assets such as education, experience, health and finance. There is a vicious circle of low growth, which reduces availability of assets, which leads to even lower growth. Insufficient aggregate demand, lack of skills among young people and the relative size of the youth labour force are the most commonly cited causes of youth unemployment (Blanchflower and Freeman 1999).

A central reason for high rates of unemployment is low economic growth, which is manifested in low economic activity and investment rates, which do not generate enough additional employment (see chapter 2). The combination of both low economic activity and high population growth results in a scarcity of jobs, meaning that hiring is based more on experience and education, the very assets young people are struggling to acquire (Box 5.1).

Even in an economic upturn, lack of work experience combined with lack of assets puts young people at a disadvantage for new job opportunities. In economic downturns the last-in, first-out of hiring and firing disproportionately affects young people.

Box 5.1
Hope through youth employment

African young people facing unemployment as well as social exclusion are particularly vulnerable. Living in substandard housing and working in survival-type economic activities reinforce young people's perception of a bleak future. But different kinds of microenterprises in degraded urban areas give rise to legal economic production and a more hopeful future.

For example, the Kibera Youth Project in the heart of one of Africa's poorest slums in Nairobi is engaged in producing an entire line of solar panels. For many young people working on the project, it is the first time anyone in their immediate family has been given or held a job.

Only a few months after the youth group completed its first prototype solar panel, it drew up a business plan to turn the project into a self-sustaining enterprise. If successful in attracting investment, the group would like to expand its sales to the rural parts of Kenya, where electricity supply is irregular.

Group coordinator Fred Ouko stated that the young people involved in the project are gaining confidence and "are making a full product, selling it, and they know they can do this for themselves".

Source: *Hicks 2004.*

Low youth literacy in SSA contributes to high unemployment

Low levels of education and skills mismatch reduce chances in the labour market

Investment in human capital in Africa is critical for supplying adequately skilled workers. The low level of education of young people is a significant factor in the longer unemployment spells they face. Youth education in Africa is below the average: for example, youth literacy in Sub-Saharan Africa is 76.8 per cent, lower than the 94.8 per cent in Latin America and the Caribbean and 98 per cent in East Asia and the Pacific (UNDP 2004).

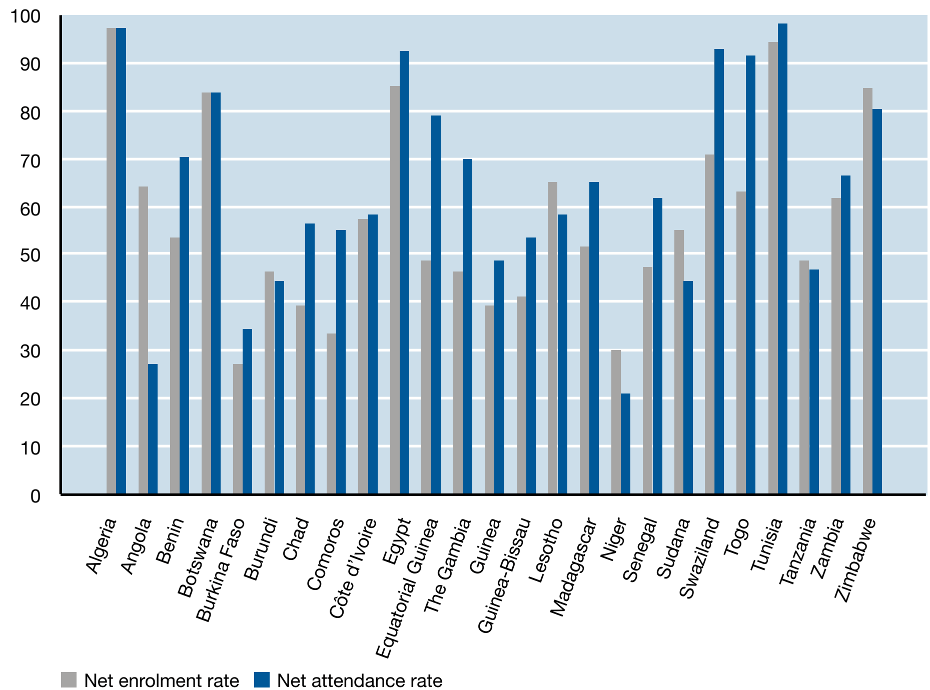
Besides the low enrolment rates in Africa (figure 5.4), primary school completion rates are also low: the world average was 81 per cent in 2001, while the average for Sub-Saharan Africa was just above 50 per cent. North African countries are in a better position with completion rates of 74 per cent (ECA 2004b).

In most of Sub-Saharan Africa the formal primary school age does not correspond to the age range of those enrolled. Part of the gap between enrolment and attendance figures in Africa can be attributed to initial enrolment, which takes place at ages above the official age. The school to work transition phase comes later, when pressure to earn a living rather than continue education becomes more acute.

In recent years returns to secondary education have decreased. A study in Kenya reveals that over 1978–95 the wages paid to workers with secondary education fell, while the direct cost of a secondary education remained stable. This made secondary education less attractive to young people, and the private rate of return to secondary education declined

Figure 5.4

Primary school enrolment and attendance rates for selected African countries, 2001 (%)



Note: *Averages are weighted by population.*

a. *Includes only Northern Sudan.*

Source: *UNESCO 2002.*

from 23 per cent to 7 per cent. The social rate of return also fell from 20 to 6 per cent over the same period (Appleton, Bigsten and Manda 1999).

Some young Africans believe that they are not adequately rewarded for their time at school, seeing it as "unproductive". In rural areas parents may prefer using their children's labour to reinforce the family's prospects in agriculture. But youth unemployment in Africa is higher among the less educated than among the more educated. In South Africa, for example, nearly two-thirds of unemployed young people do not hold a secondary school level certificate. In Ethiopia 45 per cent of unemployed young people are illiterate, and 33 per cent have only a primary level education.

Post-primary education in Africa since independence has been developed largely to supply the public sector. The 1990s reforms towards more market-oriented economies have not been matched by adequate adaptation of the curricula. And skills demanded by the labour market are not matched by the educational product ("skills mismatch"), illustrating the lack of a functioning feedback between educational institutions and the private sector.

The low quality of education, which leads to a general lack of skills, is another cause of youth unemployment. Free education programmes are often limited to primary education and provide only basic skills. High dropout rates worsen the situation further. Out-of-school training would be required for these young people to qualify for jobs, but in most cases the resources for training and skills development are scarce, if available at all (Leibbrandt and Mlatsheni 2004). In some countries training activities were offered in areas such as carpentry, auto mechanics and bricklaying, among others. Because these training activities ignored labour market demand, they led to unemployment and low returns on investment in training. When training activities are offered, they need to be carefully assessed against the kind of skills required on the labour market (Kanyenze, Mhone and Sparreboom 2000).

Kenya, Nigeria and South Africa have introduced apprenticeships–structured programmes that integrate theoretical learning with working experience (box 5.2). They involve partnerships between governments, service providers and the private sector and are a good example of the kind of feedback mechanisms needed to address the skills mismatch in Africa. Expanding similar mechanisms to formal schools is a promising way to enhance the skills match. A similar system of productivity councils–where the skills profile needed by the private sector was fed directly into the curricula of the educational sector–was part of the economic success of the East Asian countries.

The Global Entrepreneurship Monitor research project found that young people (ages 18–34) were the most likely to become active as entrepreneurs. A third of successful entrepreneurs came from that age group (Leibbrandt and Mlatsheni 2004). Promoting self-employment and entrepreneurial skills and granting access to assets such as education, training, health and finance enable young people to take advantage of the opportunities offered by self-employment.

Box 5.2
Apprenticeship in Nigeria

An example of the attempt at linking education and training at the workplace is the Nigeria's National Open Apprenticeship Scheme in Nigeria under the Ministry of Labor and Productivity's National Directorate of Employment. Under the scheme vocational education and training in more than 100 occupations are provided to unemployed young people. The programme uses production facilities such as workshops and technical instructors of private industries, government institutions and, by way of a subcontracting arrangement, wayside craftspeople and tradespeople (informal sector operators).

Unemployed young people and school-leavers can train for six months to three years under reputable master craftspeople. To enhance trainees' theoretical understanding of the trade in which they are involved, theory classes are organized every Saturday to complement the practical training received. Since the scheme's inception in 1987 nearly 600,000 unemployed young people have received training, and 400,000 of them have started their own microenterprises.

Source: *Kanyenze, Mhone and Sparreboom 2000.*

AIDS is a serious health issue for young people

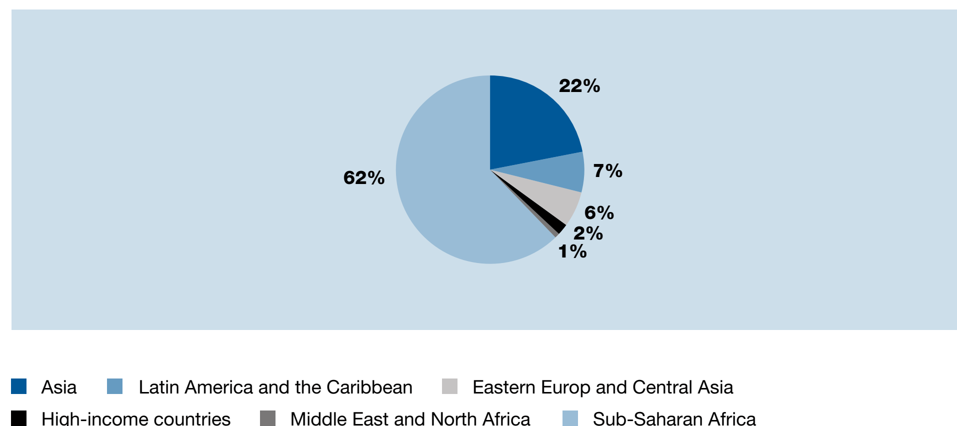
The poor health status in Africa is a severe bottleneck to employment and economic growth. At 45.2 years, life expectancy in Sub-Saharan Africa is among the lowest in the world. Of 100 newborns fewer than 30 reach age 40 in Swaziland, fewer than 56 in Cameroon and more than 90 in Algeria do (UNDP 2004). Among other factors, weak healthcare institutions and the AIDS pandemic contribute to high mortality in Sub-Saharan Africa. AIDS is the single most serious health issue in Africa today because of its negative effect on productive age groups. At the end of 2003 an estimated 35.7 million adults (ages 15–49) across the world were living with HIV/AIDS–10 million of them young people. Even more worrisome, every day more than 6,000 young people contract HIV worldwide (UNAIDS 2004).

"75 per cent of the young people living with Aids in SSA are women"

Sub-Saharan Africa has the highest share of young people living with HIV: nearly two-thirds reside in the region (figure 5.5). It is also disheartening that three-quarters of the young people living with HIV/AIDS in Sub-Saharan Africa were women, making the share of women living with HIV/AIDS 1.7 times higher than in any other part of the world (UNAIDS 2004).

Young people who are HIV-positive eventually become ill with HIV-related diseases, increasing their absence from work, reducing their productivity and lowering their chances of employment. Untreated, young people are ultimately unable to work. According to the International Labour Organization (ILO 2004c), by 2005 more than 2 million workers across the world will be unable to work at any time as a result of HIV/AIDS, and by 2015 that figure will be more than 4 million. Already an estimated 36.5 million people of working age have HIV/AIDS, and by next year the global labour force will have lost as many as 28 million workers due to AIDS since the start of the epidemic.

Figure 5.5
Distribution of young people living with HIV, by region, end 2003



Source: *UNAIDS 2004.*

Because the burden of caring for sick family members falls more heavily on women and girls, they are forced to leave economically productive activities and divert their time to care giving. If 2 million workers are unable to work because of HIV/AIDS, approximately 2 million more people of working age will be unable to work because of care duties; the indirect impact of care can thus double the direct impact of the illness (ILO 2004c).

In 2003 the number of HIV/AIDS orphans, defined as children and young people ages 0–17 who have lost one or both parents to AIDS, reached 15 million, and more than 80 per cent of them were in Sub-Saharan African countries. Having been robbed of parental care and guidance, the orphans often withdraw from school, leaving them ill-equipped to find work.[2]

Consequences of youth unemployment are severe

In Sub-Saharan Africa the lack of job prospects and the likelihood of a desolate future for unemployed young people may contribute to socially deviant behaviour. Furthermore this situation could reinforce marginalization of young people from the labour market and society at large.

Young urban migrants have no jobs and limited social networks

The motivation underlying urban-rural migration is similar to the motivation underlying international migration of young people discussed in chapter 6. Many young people migrate from rural to urban areas expecting better opportunities there (Ogbu and Ikiara 1995; Linden 1996; Sommers 2003). This has created a rapid growth in urban population and intensified competition in the urban labour market (Schoumaker and Beauchemin 2002).

"Social networks are key to find a job in urban areas"

In a context where social relations are as crucial as qualifications, young urban migrants searching for a job face an uphill struggle of "surviving" with limited social networks (Lange and Martin 1993). Increasingly, the informal sector provides employment to young educated people, whose access to modern sector employment is declining. With lower literacy rates, rural young people are at a disadvantage relative to more educated urban young people (box 5.3). The rise in criminal activity, drug addiction and prostitution among young unemployed migrants is due partly to the combined effects of the lack of social networks and insufficient job opportunities.

Youth unemployment contributes to crime and violence

The death rate attributable to violence in Africa is estimated at 60.9 per 100,000 people– more than twice the global rate (WHO 2004a). Crime and violence have been increasing in many parts of Sub-Saharan Africa among unemployed young people. Youth gangs, viewed as second or substitute families, typically satisfy the economic and social needs of unemployed young people through violence.

Some young people enter the criminal world at a very young age and end up becoming victims of crime themselves. The combination of youth unemployment and availability of firearms has been deadly. According to the Nairobi Youth and Crime Survey, the most common major offences for which young offenders were arrested were theft, assault and drug possession (UN-HABITAT 2004b).

Box 5.3
Urban unemployment among young people in Burkina Faso

Like many countries in Sub-Saharan Africa, Burkina Faso's urban unemployment rate increased 10 percentage points, from 30.7 per cent to 40.2 per cent, for young men and 8 percentage points for young women between 1980 and 2000.

The downsizing of the public sector in the 1990s reduced employment opportunities for young educated people. For example, in Ouagadougou the unemployment rate in 1992 was estimated at 43.3 per cent among 15- to 29-year-olds, compared with 6.7 per cent among those age 40 and older.

Burkina Faso also witnessed a rapid increase in its urban population, fuelled by young migrants moving for economic reasons, which also intensified competition in the urban labour market.

The result: a lower quality of jobs supplied and new generations of young Africans increasingly turning to less profitable and less stable economic activities in the informal sector of the economy. The informal urban sector accounted for 80 per cent of jobs in Ouagadougou in the 1990s.

Source: *Calves and Schoumaker 2004.*

"In South Africa, most young men between 15-21 die from gunshots"

The South African government found that homicide, primarily involving firearms, was the leading cause of death among young men ages 15–21 and that gunshots from all causes were the leading cause of non-natural death in South Africa (Fleshman 2001). According to an advocacy group, Gun Free South Africa, 12 per cent of gun death victims in 1998 were young women, and about 7 per cent of gun death victims were under age 17 (Fleshman 2001).

Commercial sex work is more common among young unemployed girls

In Africa unemployment has driven many young women and girls into sex work. Struggling to support families and provide care to sick members of the household, they are often restricted in their opportunities for education and training. The lack of job opportunities and their disadvantageous social role, both in terms of assets (education and health) and cultural norms, make them more likely to end up as sex workers (ILO 2005).

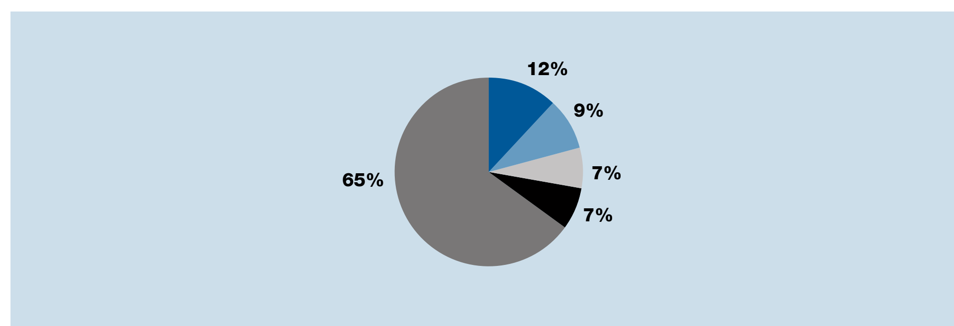
The demand for commercial sex workers from international tourism flows to Africa is on the rise. In Madagascar, for example, sex tourism has challenged the well-being of poor unemployed young women, who often struggle with hunger and destitution. In Kenya the boost in foreign tourism led to an increase in the number of commercial sex workers, as already occurred at Kenya's beach resorts (Meares 1996). Cameroon faces the same type of problem. And in Ethiopia young unemployed women are unwittingly drawn into prostitution, which also appears to be linked to rural-urban migration.

Another repercussion of unemployment closely linked to prostitution is higher HIV prevalence. Surveys of sex workers in some urban areas between 1998 and 2002 indicate extraordinarily high prevalence rates–for example, 74 per cent in Ethiopia and 50 per cent in South Africa (UNAIDS 2004).

Drugs and unemployment

Young people not attending school, living on the street and outside the reach of mainstream services, are more likely to abuse illicit substances than are employed young people (UN 2003). Figure 5.6 show the major problem drugs in Africa as reflected by treatment demand. In SSA, the main drug used by adolescents is Cannabis sativa, or marijuana, which in 2002 accounted for 99 per cent of seizures made by the authorities, with 34.6 million users representing 7.7 per cent of the continent's 15-24 year-old population. In other parts of the world, such as the United States and Europe, Cannabis accounts for over 90 per cent of all youth drug use. Drug abuse decreases young people's possibility of finding employment and results in additional costs to the economy.

Figure 5.6
Main problem drugs in Africa, 1995–2002



"Unemployment can drive women to sex work"

Opiates | Cocaine-type | Amphetamine stimulants | Others | Cannabis

Note: *Data are unweighted average of treatment demand in 24 African countries in 1995–2002.*

Source: *UNODC 2004.*

Jobless young people: an unaffordable price

Youth unemployment and its possible repercussions come at a price to the economy, to society and to the individual. Furthermore, the health burden of HIV/AIDS on GDP in Sub-Saharan Africa is closely linked to unemployed young people. Being young and unemployed in Sub-Saharan Africa contributes to high social costs that further constrain public expenditure (Brenner 1979).

The economic cost of youth unemployment

The most direct impact on the economy of an unproductive youth labour force is lost output in terms of goods and services. With no income tax to collect and the loss of receipts from indirect taxes such as the value added tax, the government takes in less in tax revenue (Bellemare and Poulin-Simon 1994).

The macroeconomic impact of HIV/AIDS in Sub-Saharan Africa is critical. Of the youth population in Sub-Saharan Africa, 6.9 per cent of women and 2.1 per cent of men were living with HIV by the end of 2003 (UNAIDS 2004). This means that 4.76 million women and 1.44 million men were living with HIV in 2003 in the region. Of this total, a significant share is believed to be unemployed young people.

Between 1992 and 2000 the HIV/AIDS epidemic reduced GDP per capita growth for 33 African countries by 0.7 per cent a year. If HIV/AIDS prevalence rates were to remain the same between 2002 and 2020, these countries will have grown 18 per cent less, a loss of $144 billion. The cumulative effects of HIV/AIDS on costs such as replacing workers, depleted organizations and institutions represent even more substantial economic losses (ILO 2004c). Low economic growth has an adverse impact on the ability of governments to raise tax revenues—because they depend on the size of the economy—while increasing the demand on government expenditure, including poverty alleviation. This directly distorts government budgets, especially health budgets.

A study of seven Caribbean countries estimated the economic cost of healthcare expenditures, government transfers, the financial costs of crime, child support, the failure to address adolescent health and teen pregnancy. Annual direct financial expenditures averaged $28–$262 per birth, depending on the country. The sum of direct financial expenditures, foregone tax revenues, cost to society of criminal activity and foregone benefits from spending government transfers and healthcare on other areas ranged from $33 per year and per birth in Guyana to $363 in Saint Kitts and Nevis (World Bank 2003a).

A cost-benefit analysis of 41 programmes that focus on young people in developing countries showed the value of the opportunity cost of investing in formal schooling for young people, basic education and literacy for adolescents. High returns were also registered for some types of school health services (micronutrient supplements) and some types of reproductive health investments. Increased education for young people has several positive outcomes: a lower probability of youth unemployment, lower incidence of HIV infection and reduced likelihood of violence and civil conflict (Knowles and Behrman 2003).

A comparison of the benefit-cost ratio of investing in young people versus productive sectors such as livestock and agricultural development projects shows that it can be more profitable to invest in young people than in these sectors. Investment in education especially pays off in open and integrated economies that are linked to the rapid advances of technology. The benefit-cost ratio of a cotton processing and marketing project in Kenya in 1979 was only 1.8, while that of a youth basic education and literacy programme in Colombia was as high as 19.9. These are valid economic reasons to channel public resources towards young people (Knowles and Behrman 2003).

At the individual level, being unemployed at an early age combined with intermittent unemployment has a direct negative impact on future income streams. This is termed "wage scar". In the United Kingdom the wage for a 42 year-old who has been repeatedly unemployed since youth is 12-15 per cent lower than the wage of a worker who has never been unemployed. This magnitude, however, decreases to 8-10 per cent if individuals avoid repeated incidences of unemployment once they are past youth (Gregg and Tominey 2004). Long and repeated unemployment of young people in Africa is likely to decrease wage levels as much as in the United Kingdom.

Youth unemployment results in higher HIV medical costs

Unemployed young people are at a much higher risk of contracting HIV/AIDS than are employed young people. This is due to persistent behavioural risks, and lack of information, education and services (UNAIDS 2004).[3] Young unemployed women in Sub-Saharan Africa are more vulnerable to HIV infection than are young men. At least three-quarters of young people infected by HIV in Sub-Saharan African countries by the end of 2003 were women. The ratio of infected young women compared to infected young men in Sub-Saharan Africa

> *Investment in youth programmes shows a high rate of return*

Box 5.4

Private sector response to HIV/AIDS

Some private companies have reacted to the HIV/AIDS epidemic–for example, the Debswana Diamond Company in Botswana. Vital to the country's economy, the company accounts for 33 per cent of GDP, 65 per cent of government revenue and over 70 per cent of foreign exchange earnings. In 1999, 75 per cent of retirements from the company and 59 per cent of deaths of company workers were due to AIDS (Whiteside and Barnett 2002).

In the mining sector, in particular, the nature of the industry and the composition of the workforce lead to a unique risk situation with respect to HIV transmission and additional costs to the industry (Whiteside 2000). It is more costly for the company to train new employees than to provide antiretroviral drugs to its employees and dependents. The Debswana Diamond Company also distributes antiretroviral drugs to its affected employees. In general, however, the private sector has been slow in responding to the epidemic.

Source: *UNECA 2004c.*

ranged from 20 women for every 10 men in South Africa to 45 women for every 10 men in Mali and Kenya. This is caused partly by the lack of employment opportunities that many young women face, leading to commercial sex with older men to support themselves and their families. Exacerbated by the higher biological vulnerability of girls and women to HIV infection, gender imbalance,[4] patterns of sexual networking and age-mixing, girls and women are the main victims of this deadly disease (UNAIDS 2004).

In Sub-Saharan Africa the annual medical cost of AIDS (excluding antiretroviral therapy) is estimated at about $30 per patient, compared with overall public health spending of less than $10 per capita for most African countries (Fredriksson and Kanabus 2004). This means that Sub-Saharan Africa would have to spend $186 million a year on young people infected by HIV. For an example of the private sector responding to HIV/AIDS see box 5.4.

Spending on HIV/AIDS reduces resources for other communicable diseases such as malaria and tuberculosis. The World Health Organization's Commission on Macroeconomics and Health has also confirmed the huge cost of economic loss from the disease. It estimates that the total benefits from one averted HIV/AIDS infection in a poor country are as high as $34,600 when annual average earnings are $1,000 a year (Curtain 2003).

Social costs of youth unemployment

Youth unemployment has a significant social cost. In addition to the indirect health cost, youth unemployment partly contributes to illicit activity, which increases insecurity.

Even in developed regions the increase in criminal activity by unemployed young people has had a social cost. In New South Wales, Australia, over 1989–99 long-term unemployment substantially increased young men's likelihood of committing a property crime. Providing more job opportunities for young men could reduce property crime in New South Wales by nearly 6 per cent a year. The crime rate could be reduced by nearly 15 per cent a year if these individuals completed high school (Champman and others 2002). A similar study conducted in England and Wales on the link between unemployment and crime suggests that youth unemployment and the different types of crimes such as burglary, theft, fraud and forgery and total crime are significantly and positively correlated (Carmichael and Ward 2001).

The increase in criminality in a country as a consequence of youth unemployment causes losses in foreign direct investment. For example, foreign investors have cited crime as the biggest deterrent to investing in South Africa (UNODC 2003). Mass unemployment among young people also disrupts long-term development of labour skills and experience. Sustained unemployment could also cause young people to be hostile to the world of work and more receptive to drugs and crime (Nattrass 2002).

Civil disorder, sometimes developing into civil strife and conflict, is one of the most serious constraints to Africa's development (Fosu 2005). Young unemployed men are prime candidates for recruitment as soldiers in any civil disorder. The chances of a poor country experiencing civil conflict have also been linked to the size of its youth population. In addition, lower education status of young men is associated with a higher propensity for

internal conflict. Other things being equal, increasing the young male population in secondary education by 10 percentage points reduces the risk of civil conflict by 4 percentage points (Collier 2000). More pertinent with regard to youth unemployment: without an alternative, conflict could be seen as an income-generating activity (Collier 2000).

Large youth bulges,[5] a characteristic of Sub-Saharan Africa's demographic structures, make countries more unstable in general and more susceptible to armed conflict. A one percen tage point increase in youth bulge is associated with an increased likelihood of conflict of about 7 per cent. And countries that experience youth bulges of 35 per cent or more run three times the risk of conflict of countries with youth bulges of 17 per cent, the median for developed countries (Urdal 2001).

Addressing youth unemployment

"Better educated youth reduces the risk of civil conflict"

The loss in GDP attributed to youth unemployment combined with the cost of mitigating the impact of drug use and criminality associated with unemployment reinforce the need to address the issue. The identification of key youth policy interventions and adequate resource allocation are crucial. Domestic resources in Sub-Saharan Africa are limited by low tax revenues and fiscal sustainability criteria that set upper limits on government expenditure, as well as competing priorities of government expenditure in general. These binding domestic resource constraints should not deter from refocusing public expenditure towards young people. Increased expenditure to raise the educational and health status of young people does not divert funds to the social sector but is a way of prioritizing allocation within the social sector. More efficient public expenditure in general based on decentralization and a public expenditure tracking system contributes to additional resources for youth targeting.

The need to create an enabling environment for the private sector is important (see chapter 7). One of the key areas is to mainstream youth employment within development frameworks in order to mitigate the marginalization of young people in Africa.

Youth employment policies must be mainstreamed

Job creation is essential to Africa's current and future generations. Investments in human capital can have low rates of return if output growth and aggregate labour demand do not adequately expand. Youth unemployment is a component of aggregate unemployment and cannot be tackled unless economic growth is sufficient. Besides accelerating growth, mainstreaming youth aspects within overall development paths is necessary. The Poverty Reduction Strategy Papers' focus on employment creation as an exit strategy from poverty is a crucial policy instrument for targeting young people.

An analysis of 21 African countries' Poverty Reduction Strategy Papers[6] reveals that only 11 have at least one core section analyzing youth employment. Seventeen countries have specifically targeted employment creation for young people, mainly through training, education and the development of the private sector (table 5.1).

Table 5.1
Employment issues in Poverty Reduction Strategy Papers in 21 African countries

Issue	Number of countries dealing with the issue
Analysis of youth employment	11
Goals or actions targeting employment creation for young people	17
Macroeconomic goals linked to employment creation	7
Training goals linked to employment creation	21
Education goals linked to employment creation	15
Private sector development linked to employment creation	20

Source: *UNECA, from official sources.*

The Poverty Reduction Strategy Papers identify three major areas of action for youth employment: training and education, macroeconomic policies and private sector development. These are crucial areas for tackling youth unemployment, but they need to be deepened and backed by adequate resources. For example, on-the-job training is listed as a way to tackle youth unemployment. However, the educational skills required for on-the-job training are not identified, undermining the cost-effectiveness of such actions. The identification of actions necessary for tackling youth unemployment must be well targeted and must be of a more structural nature.

Develop a national employment strategy targeting youth employment. The youth unemployment problem in developing countries has been internationally recognized. The Youth Employment Network is a UN-sponsored forum with young people involved as partners in devising solutions to the unemployment issues affecting them. Of the 10 lead countries adopting a National Action Plan on youth employment, 5 are from Africa. Though the action plans are country specific, their main thrust is based on the four E's: employability, equal opportunity, entrepreneurship and employment creation (Youth Employment Network 2004). Those action plans can serve as an example for other African countries.

"Only 50 per cent of African Poverty Reduction Strategies address youth"

South Africa developed a comprehensive strategy after the 1998 Presidential Job Summit and has undertaken several initiatives to increase employment opportunity for young people. These initiatives include learnership programmes, where young people receive theoretical training then follow up with on-the-job practice—a process that involves government, training service providers and the private sector. Youth Advisory Centres based in communities with a large youth population also provide information on careers and job opportunities and organize training workshops on job- related skills such as writing resumés and interview techniques (Youth Development Network 2004). Namibia, Nigeria, Uganda and Zimbabwe have also initiated or advanced this process.

Create job centres with a specific youth department. Job centres coordinate demand and supply on the labour market: private sector enterprises can advertise vacancies, saving job-seekers time and money from going to the enterprises to ask for a job. To successfully establish job centres it is important to go beyond mere administration of vacancies.

Close contact must be maintained with the private sector to continuously assess skills demands. The job centre also needs to advise young people on marketable skills. And it needs to stay in close contact with training institutions. For young people, job centres can provide information on different professions, facilitate decisionmaking on what to study and promote internships. In its turn, the private sector needs to publicize vacancies and provide data. This will pay off by saving enterprises the transaction cost of searching for adequately skilled staff.

"An essential tool, job centres encourage youth to seek employment"

Resource use: a refocus

In developing countries youth unemployment has been highlighted as a crucial area requiring pertinent policy interventions. At the international level the urgency of the youth problem was recognized and clearly identified in the Millennium Development Goals. Millennium Development Goal Target 16 is to "develop and implement strategies for decent and productive work for youth." In this context the Youth Employment Network was created. The International Labour Organization sees decent and productive work for young people as both an integral part of the Millennium Declaration and a key contributor to meeting other Millennium Development Goals, including those relating to reducing poverty. On a regional level the United Nations Economic Commission for Africa has decided to focus its fifth African Development Forum on the issue of youth and leadership in order to place young people within development agendas and optimize synergies of young people and related policies for accelerating Africa's development (ILO 2004b).

Official development assistance flows to health ($1.2 billion in 2003) and education ($1.3 billion) were the largest share of aid to Africa (OECD 2003). In Africa public expenditure on education averages 3.8 per cent of GDP and public expenditure on health averages 2.8 per cent of GDP (World Bank 2000). The need to mobilize more resources for young people more efficiently cannot be overstated. There is also a need for education and health service providers to be closer to end-users and for young people to be more involved in the process.

Decentralization. Decentralization covers the issues regarding the appropriate balance of financial and administrative responsibility among central governments, subnational governments, institutions engaged in the provision of services and target communities. There are two key considerations in determining this balance: efficiency and feasibility.

Government budgetary allocations are public, but information on actual spending is generally unavailable (Kanungo 2003). A public expenditure analytical tool is crucial for ensuring that resources for youth unemployment are used efficiently.

Public expenditure tracking surveys have been conducted in Ghana, Tanzania, Uganda and Zambia, and they should be replicated in other countries in Sub-Saharan Africa. The main findings show how necessary public expenditure tracking surveys are:

- In Uganda only 22 per cent of funding for books and other instructional material, key to improving educational quality, reached end users in 1996—and in Ghana only 49 per cent did (Reinikka and Smith 2004).

- Estimations for Uganda show that 40 per cent–94 per cent of total drugs provided by the government did not reach their targeted end-users (Ablo and Reinikka 2000).

- Accountability is key: if young people in rural areas are supplied with information on funds designated to them, they can hold local authorities responsible for efficient targeting and spending. After the introduction of public expenditure tracking surveys in Uganda funds for education provided by the central government that actually reached their target shot up from 13 per cent to 80 per cent–90 per cent in 1999–2000 (Reinikka and Smith 2004).

Public-private partnerships

Public-private partnerships are essential for overcoming supply constraints in education and provide feedback from the private sector to the education system, which mitigates the skills mismatch. The private sector can participate in education by providing inputs such as textbooks, operating public schools and delivering education through private schools. By contrast, the government is concerned with access, equity, quality and whether public resources are used to support the realization of a well educated society (UNITAR and DMAN 2001).

Provider or regulator. Governments must move from providing education and health services to regulating them:

- The government of Uganda gave Makerere University more responsibility to make it financially viable. This has enabled the university, in consultation with the business sector, to design new courses that target professionals and companies in order to increase their skills. Integrated internship programmes also offer the possibility of smooth transition from school to work (Dang 2002).

- Public-private partnerships improve the quality of education by using private sector core competencies to robustly link education with job skills and gainful employment, as practiced by the United States Agency for International Development's Office of Global Development Alliance. The Global Learning Portal, one of the alliance's activities, provides pre-service and in-service training for teachers at all levels in developing countries to improve their capacity and hence the quality of education. Ethiopia, South Africa and Uganda are among the pilot countries (USAID 2005).

Overcoming supply constraints. With funds limited by macroeconomic stability programmes, government face serious financing gaps for investment. New ways of financing investment have to be found. These might include involvement of the private sector and NGOs, only to mention a few.

- Public-private partnerships have been considered as a strategy for building schools in South Africa, particularly in the provinces of Free State and Mpumalanga.

- The emergence of private financial institutions (microfinance institutions, cooperatives and private banks) in many parts of Africa means that public-private partnerships in financing education (administration of government loan) could be used to decrease transaction costs and increase efficiency. They could prevent a low student loan repayment rate, such as Ghana's low 8 per cent rate for tertiary education.

Improving management. Different education services—such as in-service training of teachers, developing curriculum and learning materials and training school managers and governors—can be outsourced to private contractors (Pampallis 2003). The Aga Khan Development Network partnership with the government of Pakistan is an example of improved quality of education service delivery and promotion of professional development for teachers (AKDN and DFID 2003).

Provision of information communication technology courses by the private sector in public universities is another area of partnership. In South Africa Educor, a local company, was contracted to provide the entire computer training programme of a public university (Dang 2002).

"Integration is necessary between universities and business"

Public works programmes as an entry gate to the labour market

In addition to low demand for labour, a barrier to finding work for many young people is lack of work experience. They must become accustomed to regulated working hours. Public work programmes can be useful for drawing young people away from the street and helping them to pursue other goals, such as environmental cleanup programmes (Box 5.5). In Ghana young people were employed in reforestation and urban sanitation programmes, and in Nigeria young people have been employed on government agricultural plantations (Nwuke 2002).

The use of public works programmes for young people can be further enhanced by combining the entry gates to the work environment and training. Public works programmes should be seen within the wider context of continued education, acting as a catalyst for combining wage-earning apprenticeships and market-driven skills acquisition.

New directions for the education system

Improving access to education is imperative, especially because less-educated people have access to fewer jobs. In Sub-Saharan Africa youth literacy increased from 66.8 per cent in 1990 to 76.8 per cent in 2002—insufficient for active participation in the job market because basic education is a prerequisite for training young people (UNDP 2004).

Youth unemployment is partly the result of a mismatch between inadequate educational outcomes and skills demand. The education system must provide the skills profiles required by the labour market to enhance the employability of young people. At the formal school level this requires achieving full enrolment in primary schools. Complementary policy

Box 5.5

A countercyclical safety-net role

A large public works programme that covers infrastructure, health and education is operated by the Social Fund for Development in Egypt. Nongovernmental organizations manage it, and the private sector is in charge of implementation and maintenance. At least 25 per cent of programme funds have to be spent on labour whose salaries must not exceed local wage rates. Between 1991 and 1997 more than 42,000 jobs were created, 90 per cent of them temporary, and most of the participants were young. The Social Fund's Small Enterprise Development Organization targets university graduates with its loan programmes, which provide start-up loans with heavily subsidized interest rates. Credit officers are actively encouraged to approach university graduates.

To create permanent jobs and to involve the private sector in training young people, the government decided to introduce a dual system in technical education and vocational training in 1991, known as the Mubarak-Kohl initiative. The private sector contributes by defining the training needs, and the Ministry of Education supervises the design of a pedagogical, organizational, legal and financial framework that fits the local situation. For the pilot phase, cities with a high number of medium-size and large enterprises were chosen. Eventually, all types of training will be organized along the lines of the dual system. After completing preparatory school, all Egyptian children will have the opportunity to enrol in technical secondary education and graduate three years later. Ideally, they will find employment in the business where they acquired their skills, and if not they have improved their chances of finding a job elsewhere.

The initiative was considered very successful: over 1995–2003 some 8,000 young people were trained, with 1,480 companies and 40 schools participating. The initiative is scheduled to be extended.

Source: *Kanyenze, Mhone and Sparreboom 2000.*

“Public works are one doorway to the job market”

interventions are required to enhance quality, gender parity, curriculum development and secondary education.

Increased enrolment. Primary school enrolment must be increased by:

- Involving local stakeholders—parents and communities—to increase enrolment in primary schools. Tanzania and Uganda increased enrolment substantially through parent and community involvement.

- Backing political commitment to universal primary education with adequate domestic and external resources, not only of a financial nature. Lower school fees have led to huge increases in enrolment in Kenya and Uganda. Ghana is expanding its school feeding programme to cover 2.5 million students. A United Nations Children's Fund and World Food Programme initiative in Malawi showed a 36 per cent increase in attendance among schools with nutrition schemes (South African Institute of International Affairs 2004).

- Ensuring timely enrolment. Late starters at primary school receive greater peer pressure to start working, are less likely to develop basic reading and writing skills and have a lower training capacity.

Quality of primary education. The drive for higher enrolment can lead to a decrease in education quality due to declining spending per pupil. Quality is ensured by high completion rates and by the increased supply of quality teachers and adequate equipment, including books and laboratory facilities.

The number of additional primary school teachers in Africa needed to achieve full enrolment by 2015 is three million (South African Institute of International Affairs 2004). Due to the HIV/AIDS epidemic, many African countries do not have an adequate supply of graduate teachers, which has led to a declining teacher-student ratio, a proxy for quality that has reached 1 to 100 in some places. Many African countries have used teachers that are not graduates, further decreasing quality. For example, 75 per cent of teachers in Benin are unqualified, 30 per cent of teachers in Mozambique have not received any training, and 30 per cent of teachers in Angola have fewer than five years of schooling (South African Institute of International Affairs 2004). The policy interventions required are:

- Increasing the supply of teacher training institutions and qualified teachers. The cost can be mitigated through distance learning. For example, in Zimbabwe five training centres are connected by the Internet for online teacher training.

- Providing on-the-job training for teachers. African governments must update the technical competence of teachers, based on modern teaching methodologies and a changing curriculum content.

- Ensuring that teachers have beneficial conditions of work conducive to retention within the profession. This can be achieved through government policy.

- Offering short-term courses that combine pedagogic techniques and classroom experience for school leavers who temporarily replace graduate teachers. This is crucial for upgrading quality.

- Ensuring that books and teaching equipment are available. An extremely important element for quality education, they generally have a high cost but are necessary. Regional cooperation in areas such as book supplies can mitigate some of these costs.

- Pursuing private-public partnerships, which have high potential for improving school quality. For example, Sasol (a South African oil company) supports a number of schools to meet its own labour demand. It ensures trained teachers and adequate facilities for students.

- Increasing the use of information technology, which has enormous potential to provide teaching material and at the same time decrease cost (box 5.6).

“Africa needs an additional five million primary teachers”

Gender parity. Boosting female enrolment in formal schooling is important because it has spillover effects on the economy. Education for girls reduces child and maternal mortality, decreases vulnerability to HIV/AIDS and increases enrolment of the children of educated mothers (South African Institute of International Affairs 2004). A single year of primary education for a girl corresponds to a 10 per cent–20 per cent increase in women's wages. An extra year of education for girls has been shown to reduce infant mortality by 5 per cent–10 per cent (South African Institute of International Affairs 2004). To improve gender parity, African governments must:

- Accelerate girls' enrolment through incentive schemes. For example, homegrown feeding programmes generally support both genders, but affirmative action for girls could be implemented. Bangladesh successfully eliminated fees for girls in primary education and introduced food for education. In return for food parcels, parents must ensure that their daughters attend school for at least 75 per cent of the school year.

- Reduce or waive miscellaneous costs. Eliminating hidden costs, such as those for uniforms, stationery and textbooks, greatly increases girls' enrolment.
- Emphasize gender in the public resource transfer to education to make it more cost effective.

"Curricula need to include more technical subjects"

Curriculum development. There is an urgent need to move from incremental or cumulative concepts and mnemonic notions to instrumental or problem-solving tools curricula. This requires a curriculum that focuses on technical and scientific subjects. South Africa has introduced an outcome-based education curriculum reform that is student-centred and that introduces a problem-solving approach to education (South African Institute of International Affairs 2004).

This requires an adequate supply of trained teachers, a serious constraint in Sub-Saharan Africa. For example, in six of nine provinces surveyed in South Africa 60 per cent of educators had not been trained in math and science. The number of university science graduates

Box 5.6
E-slates to the rescue

At the Mbita Point primary school in Kenya students are using handheld computers to get up-to-date information on textbooks.

A pilot project by Eduvision has implemented a wireless connection to a base station at the school that is in turn connected to a satellite receiver. This allows downloading of visual and textual information that can be placed on e-slates of students.

The project intends to download more than 15 million books in the public domain and make them accessible to rural schools at a lower cost than acquiring new textbooks.

Source: Siddle 2005.

who could form a pool of science teachers is very low. For example, only 4 per cent of university graduates study science in Ethiopia, 1 per cent in Namibia and 11 per cent in Eritrea. Other policy actions that should be taken include:

- Giving priority to mathematics and science education at all levels of education and offering incentives to attract students in tertiary institutions. The University of Pretoria, for example, sponsors 140 students a year in math and science.

- Collaborating on science and mathematics institutions across countries. A collaborative initiative on science and mathematics teaching that link teachers in Kenya, Uganda and Zimbabwe through the Internet has been successful (UNESCO 1999). The project reduced the unit cost of training a science teacher through distance learning and could be repeated in other countries in Sub-Saharan Africa.

- Developing public-private partnerships to create a curriculum that responds to skills profiles demanded by the labour market. The Carnegie Corporation provided the University of Makerere and the University of Dar es Salaam with $4 million to boost enrolment of women undergraduates in science and technology (South African Institute of International Affairs 2004).

- Standardizing textbooks and training materials in science and math on a regional level to mitigate costs (South African Institute of International Affairs 2004).

Secondary schooling. The need to invest in secondary education in Sub-Saharan is imperative. Current completion rates for junior and higher secondary education are about 15 per cent–25 per cent. Secondary education is crucial because it provides critical higher skills and knowledge, which have become a determinant of competitiveness in the world economy. Policy on secondary education has only recently been recognized as an area of neglect (Lewin 2004). For example, Uganda's Universal Primary Education Programme has been running for seven years and is successful, but in 2003 fewer than half of the 700,000 students who finished primary school could be accommodated in secondary schools. To expand secondary education in order to tackle the educational mismatch is important, African governments must:

- Increase enrolment at the secondary level while keeping unit costs in check.

- Develop distance learning for secondary school students, while reducing costs and allowing access to rural areas.

- Allocate adequate domestic and external funding for a more balanced education budget between primary and secondary schooling.

Vocational training is critical to promoting social inclusion

Vocational training. The number of young people working in the informal sector in Africa indicates that besides formal schooling policy interventions, skills development and nonformal education are critical. Out-of-school young people must be involved in vocational training if social exclusion is to be avoided and employability enhanced (box 5.7). The policy interventions in this context are:

- Providing adequate financing for vocational training.

- Linking vocational and entrepreneurial training with job centres to ensure that the skills profiles supplied match demand.

Gainful employment requires good health

Box 5.7

Madagascar finds a clearly effective approach

Madagascar's government and the UN System Joint Programme to Promote Basic Education for All Malagasy Children were behind an innovative nonformal education programme. Launched in 2001, it offers learning opportunities for out-of-school children, illiterate and jobless young people and adults. Today, one of three children are not in school in Madagascar, while one of three adults cannot read or write.

Specialized centres have been set up in each province to offer adolescents a chance to catch up with five years of primary schooling. In just 10 months they receive intensive training that permits them to pass the end of primary school exam.

For illiterate young people and adults, the way to literacy is different. They attend the intensive functional literacy for development courses in two phases: the first phase is 48 days and covers reading, writing and numeracy; the second phase is 36 days and provides basic technical and professional training. The aim is to give participants skills to find jobs or improve their earnings. Sixteen areas have been proposed, including farming, fishing, carpentry and sewing.

Source: *http://portal.unesco.org/education/en/ev.php-URL_ID=27727&URL_DO= DO_TOPIC&URL_SECTION=201.html.*

Internship programmes and on-the-job training

Internship programmes and entry wages that are below average wages are another way to give young people a chance to work. Many employers are reluctant to employ young people without experience. Working for a period with lower wages could give young people a chance to demonstrate their competencies and acquire new skills through learning-by-doing. The introduction of apprenticeships in Kenya, Nigeria and South Africa has proven successful and could be replicated in other countries (see box 5.2 for information on apprenticeship programmes in Nigeria).

In Zimbabwe a cluster of Dutch companies is prepared to take part in a project to provide one year of work experience for young people. This follows a successful programme begun in 1982 between Philips and the Dutch trade unions: about 80 per cent of the young people covered by the programme later found paid employment. Philips itself employed a quarter of them, but the majority were absorbed by small and medium-size enterprises (Kanyenze, Mhone and Sparreboom 2000).

In South Africa a global initiative to support young people called Make a Connection offers an innovative training course to unemployed college graduates. The training period lasts three months and is supposed to build participants' self-confidence and motivation, improve their teamwork and presentation skills, teach them basic computer literacy and how to look for and keep a job. Internships and other activities provide additional exposure to the world of work.

Realigning job expectations

Many young people, especially university graduates, expect to find a job in the public sector. Studies from Ethiopia and Tunisia show that university graduates are prepared to wait for a long time for a public sector job instead of actively seeking a job in the private sector or starting a business on their own (Adenikinju and Oyeranti 2004). Entrepreneurial skills and workshops on how to find business ideas should be integrated in school and university curricula to encourage young people to start their own business.

Healthier young people perform better

There is a two-way causality between youth health and unemployment. Unemployed young people's health is vulnerable because of the risks attached to poverty, marginalization and deviant behaviour. Poor health prevents them from actively participating in the labour market due to absenteeism, which in turn causes a lack of trainability and lower productivity. Good health is the basis for performing well in education, training and on the job. In Sub-Saharan Africa young people are heavily affected by HIV/AIDS.

Combating HIV/AIDS. Prevention must be a central pillar in the fight against HIV/AIDS. In order to do so, young people need to be involved as much as possible in the effort. Half of all new HIV infections worldwide are in young people; more than six thousand contract the virus each day (UNAIDS 2004). Policy actions to fight HIV/AIDS among young people include:

- Providing education and information—starting at an early age—on how to maintain good health and prevent HIV infection. The ABC's of prevention (abstinence, being faithful, condom use) should be a part of curricula (Alonso and de Irala 2004). A study in 17 African countries showed that simply receiving primary school education can halve young people's risk of contracting HIV (South African Institute of International Affairs 2004).

- Offering life skills education courses at job centres, especially to out-of-school young people.

- Tailoring programmes specifically to young people because the way that they obtain information and their needs are different from the ways of adults. Young people themselves should be involved in the design and implementation of courses (Box 5.8).

- Specifically targeting young people with voluntary testing and counselling.

- Making antiretroviral drugs available to employed and unemployed young people.

Box 5.8
Prevention in Botswana

Tsa Banana (For the Teenagers) was a tailor-made programme for young adults in Botswana, funded by the United States Agency for International Development. Launched in 1995, it existed for one year, during which youth awareness of HIV/AIDS increased, and the risks of having unsafe sex decreased. HIV/AIDS awareness tools such as T-shirts, stickers and pamphlets were given to young people. The programme evaluation showed that 68 per cent of female teenagers and 71 per cent of male teenagers had heard about Tsa Banana and that more than half had taken part in the programme's activities. As a result, young adults were more convinced of the importance of protection against HIV.

Source: *UNAIDS 2004.*

"30 per cent of youth in 22 countries have never heard of AIDS"

Gender inequalities. Government should pay special attention to the situation of young women and girls. Three-quarters of young people infected with HIV are women and girls. Several social factors are driving this trend. Young African women tend to have male partners much older than themselves, and those partners are more likely than young men to be infected by HIV because they have had multiple sex partners. In this context, it is imperative that countries in Sub-Saharan Africa enforce existing laws against underage female brides.

Gender inequalities in the region make it much more difficult for women to negotiate condom use. Furthermore, sexual violence, which damages tissues and increases the risk of HIV transmission, is widespread, particularly in the context of violent conflict (UNAIDS 2004). Access to education and training for young women must be improved. The more girls are educated, the longer they refrain from sexual activity and the more likely their negotiating power increases for condom use (South African Institute of International Affairs 2004).

While often seen as a burden to society, unemployed young people in Africa can also be considered an opportunity for the future, given the proper education and training. The alarming youth unemployment figures in Africa and the prospects of a bleak future require immediate action interventions and medium-term plans that address the structural causes.

Policy interventions to tackle youth unemployment should combine enhancing the employability of youth and mainstreaming youth policies within national development frameworks. Young people need to be equipped with the right skills, in both education and health, to actively participate in the labour market. With better perspectives on the labour market they will be more encouraged to engage in secondary education and additional training.

Endnotes

1 Youth is defined by the United Nations Department of Economic and Social Affairs as the population ages 15–24 years, although the definition varies among countries and development institutions. In this analysis the UN definition is used unless otherwise indicated. In 2002 Sub-Saharan Africa's population was 688.9 million, with youth assumed to account for a fifth of the total. Youth unemployment in Sub-Saharan Africa was 21 per cent in 2003 (ILO 2004b). Leibbrandt and Mlatsheni (2004) also estimated the share of youth population for 15 Sub-Saharan Africa countries at one fifth and the (urban-rural) population-weighted unemployment rate for youth at 21 per cent. This unemployment rate is applied to youth population to calculate 28.9 million unemployed youth on the continent.

2 Many orphans are now heads of households and are far less likely to attend school, more likely to be undernourished, less likely to receive immunization or healthcare, more likely to be very poor and more likely to become involved in risky situations such as crime, prostitution and others (World Bank 2000).

3 At least 30 per cent of young people in 22 su rveyed countries had never heard of AIDS and how it is transmitted. Up to 87 per cent of 15- to 19-year-olds do not believe that they are at risk (UNICEF 2004).

4 Some studies have shown that girls are in a less of a position to demand condom use during sexual intercourse.

5 Youth bulge is defined as the ratio of the population ages 15–29 to the population ages 30–54 (Urdal 2001). The United Nations Department of Economic and Social Affairs defines youth cohorts as population ages 15–24 years relative to the total adult population (age 15 and older).

6 Benin, Burkina Faso, Cameroon, Chad, Djibouti, Ethiopia, The Gambia, Ghana, Guinea, Kenya, Madagascar, Malawi, Mali, Mauritania, Mozambique, Niger, Rwanda, Senegal, Tanzania, Uganda and Zambia

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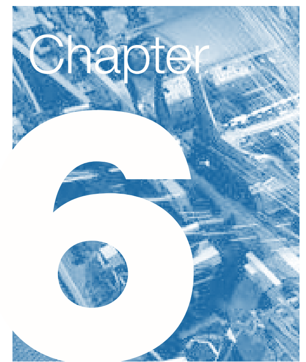


Harnessing globalization to create decent jobs and reduce poverty

Globalization has created hundreds of millions of new jobs—mostly in developing countries, relatively few in Africa. Yet, Africa's markets are integrated in the global economy. Although its shares in both world trade and FDI are 2 per cent of the global total, its shares of trade and FDI in GDP are in the same range as in other regions or even higher. The continent is already affected by the current wave of globalization that is driven by lower transport and communication costs, liberalized markets for goods, services and capital and faster technical change.

"A more competitive Africa can benefit from globalization"

Because world trade in manufacturing goods increased sharply in the past decade, while trade in raw materials more or less stagnated, diversification into manufactured exports is more likely to create growth and jobs in Africa. Despite some shift towards manufactures in both exports and FDI, Africa will benefit from globalization only if its manufacturing sector becomes more competitive.

Globalization, as well as poverty reduction, are positively linked to productivity growth through different channels. Both trade and FDI will increase only if a country is competitive in the international market, with competitiveness depending on the ratio of wages to productivity. And because increases in productivity allow wages to rise, there is a strong link between productivity and poverty.

Empirical evidence shows that globalization has a positive impact mainly in countries where raw materials are not the dominant exports and levels of human capital are fairly high. Because the supply of low-skilled workers in most African countries is very large, wages are more likely to increase for skilled workers, especially in the light of rising demand for skilled workers due to technological advances.

Four lessons on how to harness the opportunities from globalization:

- First, African countries need to focus on productivity growth. Asia gave attention to quality of education, expanded girls' education and improved vocational skills, essential for technological change and growth. Productivity councils or centres identified enterprises' technical problems and developed appropriate remedies and training packages to solve them.

- Second, to increase the competitiveness of exports and attract more FDI, the improvement of infrastructure, especially telecommunications, is essential. Most infrastructure in Africa is concentrated along the coasts and in major urban centres, whereas poverty remains higher in the rural areas. Improved rural infrastructure

would help to integrate with the urban sector and the global economy. Infrastructure projects could also be made more cost-effective through regional cooperation, which needs to be strengthened and streamlined.

- Third, industrial policies have to be designed carefully and adapted to local conditions. For instance, the Asian miracle was driven not by liberalization but by well designed industrial policies, including directed credit, trade protection, export subsidization and tax intervention. The East Asian policy package worked because it combined these incentives with the discipline of government monitoring and the use of export performance as a productivity yardstick. Export processing zones have created employment in Madagascar and Mauritius. To be successful, they need government backing and a strong management team that closely monitors enterprises.

- Fourth, incentives for both foreign and domestic investment should be targeted with care. To be preferred are labour-intensive sectors, as are firms with strong backward and forward links, because they increase the externalities from technological upgrading. Investment promotion agencies should focus on linkage-intensive sectors such as agroprocessing and tourism, bringing domestic suppliers and foreign affiliates together and facilitating learning from foreign companies.

Globalization provides opportunities for women in sectors as different as shea butter and information and communication technology. Shea butter, or karité, is one of the few relevant export commodities under women's control in Sahelian Africa. Global market forces could give them an opportunity to improve their income and reshape rural women's livelihoods. In the data processing enterprises mushrooming in several African countries, a large share of owners and employees are women. To improve women's ability to benefit from globalization, their education has to be improved, especially in modern technology.

Although globalization has generally brought benefits, it has also been associated with inequality, vulnerability to external shocks and a brain drain. African governments need to cushion the most vulnerable groups against globalization's adverse effects. They include low-skilled workers who would have difficulty moving to a different sector—and poor people, who generally lack the assets to invest in productive activities. Mitigating the adverse effects of globalization includes providing basic social security, retraining workers for growing sectors and improving access to education and credit.

To increase the benefits from high value agriculture, it is essential to link smallholders to international markets. Because the horticultural sector, for example, is too diverse and fast-changing for the state's direct involvement, governments should allow a variety of private institutions and marketing arrangements to develop. To help smallholder farmers participate in value chains for export production, governments should increase their support for producer groups. They could also facilitate the adoption of innovations by providing market information and extension services.

Harnessing the potential of migrants for sustainable development includes tapping remittances, investment, skills transfer and diaspora networks. Because contract enforcement

across borders is especially difficult for small and medium enterprises, networks can foster cross-border trade and investment links. Migrants can facilitate flows of information and knowledge and thus facilitate technological progress. And returning migrants, with their new skills and attitudes, could help to expand employment through private sector engagement.

Africa's markets are integrated in the world economy

Globalization in Africa: facts and figures

The current period of globalization is distinct from previous ones. At the beginning of the 21st century trade and financial services are far more developed and deeply integrated. More than ever, economic decisions are influenced by global conditions (Jenkins 2004), and production processes spread over several continents. Although Africa's share in worldwide flows of trade, investment and remittances is low, globalization affects its economies substantially, because the shares in production and consumption are fairly high.

In the past 20 years, dramatic changes in international markets have helped shape the current era of globalization. A complex process affecting many aspects of people's lives, globalization is defined here as the growing international integration of economies with regard to markets for goods and factors of production (Bigsten and Durevall 2003). This chapter analyses the integration of economies through trade, foreign direct investment (FDI) and to less extent the mobility of labour.[1]

Unlike the globalization witnessed in the 19th century, today, labour markets remain more closed than ever. Most industrial countries have restricted immigration, particularly that of low-skilled workers. Moreover, after the terrorist attacks of September 11, 2001, the movement of people, not only into the United States but also into other countries of the world, has been restricted and controlled more and more.

Despite these limitations, about 2 per cent of the world's people live outside their countries of origin. This reality poses considerable challenges to the domestic labour markets of the African continent, a net labour exporter. Changes in remittance flows might also affect poor people's consumption possibilities.

Contrary to general perception, Africa's markets are integrated considerably in the global economy (figures 6.1 and 6.2). But, this integration is asymmetric. Africa depends on the rest of the world, whereas the rest of the world does not depend on Africa. Its shares in both world trade and FDI are only 2 per cent of the global total, a reflection of the continent's low share in world GDP. When few goods are produced, there are fewer exports. When markets are small, the incentives for FDI are limited. Compared with countries that have similar characteristics, African countries' trade and FDI flows are not exceptional–but are determined by their small size, low incomes and geography. That is why policies to increase exports and FDI have to focus on improving productivity (Bigsten and Durevall 2003).

The closer integration of markets is driven mainly by lower transport and communication costs. It also depends on the liberalization of markets for goods, services and capital. Yet, borders still inflict significant transaction costs, particularly due to different legal systems

and currencies. That is why prices of tradable commodities differ markedly across different countries, even after taking indirect taxes and retail costs into account (Rodrik 2005). In general, natural protection has been sharply reduced in Africa, even without trade liberalization. But in landlocked African countries transport costs remain an obstacle to integration (UNECA 2004b).

Another issue is the increasing speed of technical change, both a cause and an effect of globalization. Technical progress in information processing and communication has enabled the steps of production to be split and performed in different locations. Increased trade and cross-border investment give less developed countries better access to technology and increase their market competitiveness (Lall 2002).

Africa's share in world trade is low but its dependency on trade is high

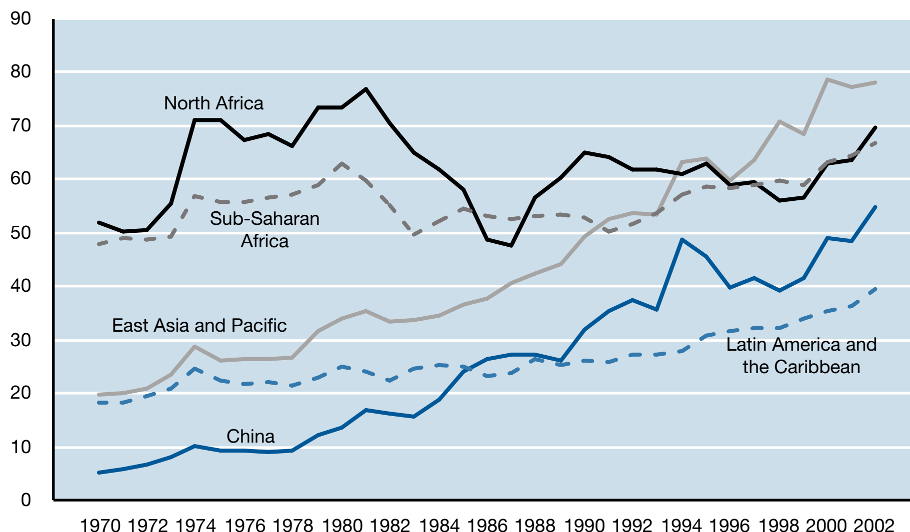
While world GDP rose on average by 3.8 per cent a year between 1985 and 2000, world exports grew by 6.1 per cent. Developing countries as a whole increased their share of world trade from 19.2 per cent in 1970 to 31.7 per cent in 2002. Developing Asia's share of world trade increased from 17.9 per cent in 1980 to 24.2 per cent in 2002, South-East Asia's from 8 per cent to 20 per cent. Latin America's share remained constant at around 5.5 per cent. Africa's share, by contrast sank from about 5.9 per cent to 2.1 per cent in 2002 (UNCTAD 2004a).

On the basis of foreign trade as a share of GDP, Africa is one of the world's most open regions, behind only East Asia. But that share has oscillated historically in line with commodity price fluctuations. In addition, it increased less than in other regions between 1970 and 2002 (see figure 6.1).

With world trade in manufacturing goods growing fast in the past decade, while trade in raw materials more or less stagnated, manufactured exports were more likely to create growth and jobs (Fosu 1990, 1996). Africa's share in global trade in manufactures, already very low at 1 per cent in 1980, fell to 0.81 per cent in 2001. This happened despite the fact that the share of manufactured goods in Africa's exports rose from 8 per cent in 1980 to 31 per cent in 2001.[2] For developing countries on average, manufactured goods account for 65 per cent of their exports (UNCTAD 2004c).

Between 1970 and 2002 exports grew on average slightly faster than imports in Sub-Saharan Africa and slower than imports in North Africa (UNCTAD 2004a). In both regions many countries ran trade deficits, with export earnings covering only 54 per cent of total imports, particularly the least developed African countries, whose major exports are agricultural commodities. This limits the ability to import machinery and equipment, essential for creating new productive employment. These trade deficits are partly financed by aid inflows and increasingly by worker's remittances (UNCTAD 2004b).

Figure 6.1
Trade as a share of GDP in selected regions, 1970–2002 (%)



Source: *World Bank 2003.*

> *FDI has recently risen in manufacturing, agroindustries, and services*

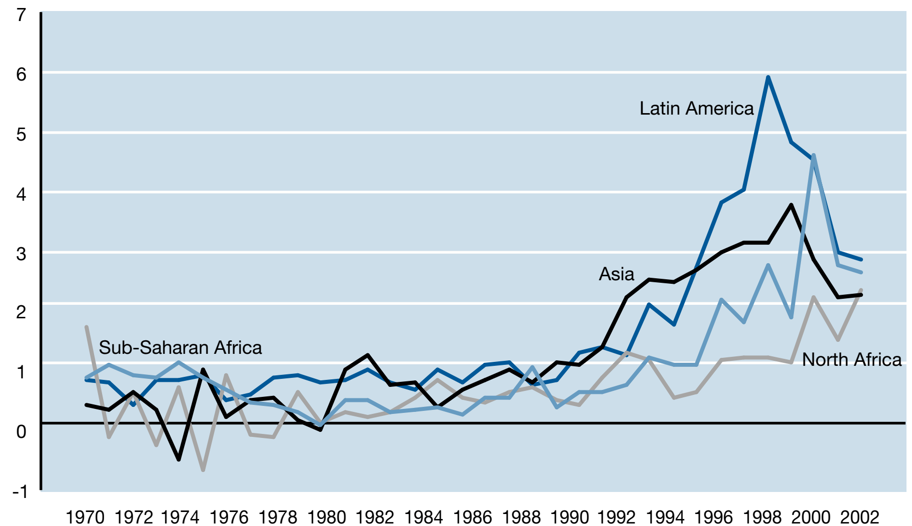
FDI in Africa has also expanded, if from a low base

Growth in world trade was accompanied by growth in FDI. Indeed, global FDI grew at 17.7 per cent a year over 1985–2000, boosting net inflows to developing countries as a whole.[3] The developing countries most successful in attracting FDI were the most successful exporters. Inflows of FDI to South, East and South-East Asian countries (excluding China) moved from $3.5 billion in 1980 to $35.9 billion in 2002, with a peak at $97.9 billion in 2000. Africa's share of FDI inflows for developing countries is half what it was in 1980 (UNCTAD 2004a).

Contrary to general perceptions, however, Africa benefited from the recent rapid expansion of FDI. In Sub-Saharan Africa FDI stabilized at an average of $8.75 billion a year during 1997–2002, twice the average of $4 billion at the beginning of the 1990s (World Bank 2004). In 2003 FDI to Africa increased to $14 billion, despite a declining world trend.[4] And like Latin America the share of FDI in GDP increased to more than 2 per cent (figure 6.2).

Even so, more than half the FDI to Africa is to the primary sector, mainly extractive industries, which exploit resources but use little local labour. Data from foreign affiliates of U.S. firms in Africa show that manufacturing FDI is 17.5 times more labour-intensive than mining FDI. In some African countries, though, FDI has recently risen in manufacturing, agroindustries and services, as for Egypt, Morocco and Mozambique (UNECA 2004b). There has also been an increase in employment in manufacturing FDI in Africa[5]. This investment is driven partly by low labour costs and partly by preferential access to markets of industrial countries.

Figure 6.2
FDI as a share of GDP in selected regions, 1970–2003 (%)



Source: *UNCTAD 2004a.*

Imbalances in migration lead to a brain drain in Africa

The main direction of migration is from developing countries towards industrial countries, so Africa is a net emigrating region. The stock of African migrants is highest in France, where more than 1.6 million of the 4.3 million Africans living in Organisation for Economic Co-operation and Development (OECD) countries reside. The second most common destination is the United States, where more than 880,000 African nationals reside. Most migrants come from North Africa, mainly Morocco (1.3 million) and Algeria (680,000). The reported remittances have increased from $8.6 billion in 1990 to $11.1 billion in 2002, partly reflecting an increase in the number of migrants (World Bank 2004; Doquier and Rappoport 2004).[6]

In principle, migration could reduce unemployment. But the discrimination in favour of educated workers by OECD countries contributes to the brain drain from developing countries, increasing the shortages of highly skilled workers in many African countries (World Bank 2002). Recent evidence shows that Sub-Saharan Africa is most affected by the emigration of skilled workers, with 14 countries having more than 15 per cent of their skilled workers residing in OECD countries in 2000. Among them: Somalia (59 per cent), Ghana (43 per cent), Mozambique (42 percent), Sierra Leone (41 per cent), Nigeria (36 per cent) and Madagascar (36 per cent). Especially for low-income countries the share of skilled workers migrating increased substantially between 1990 and 2000, meaning that public expenditure for their education does not benefit the home country. (Docquier and Rapoport 2004).[7]

The often lamented brain drain is more a symptom of the problems of employment creation than a cause. Theoretically highly skilled labour should gain high rates of return in places where it is scarce. But this effect is partly offset by agglomeration effects in rich countries–as highly skilled people become more productive through exchanges with other highly skilled people and through their complementarity with more highly productive physical capital. In addition, the large business obstacles in many African countries outweigh the costs of migration and thus reinforce the brain drain.

Trade, FDI and migration are complements

Job creation policies need to look at trade and FDI simultaneously. In effect, trade and FDI grow or stagnate at the same time. This leads to the assumption that trade and FDI are complements rather than substitutes. In particular, the types of FDI dominant in Africa are positively associated with trade. Trade barriers and other obstacles posed by African countries will have little effect on resource-seeking FDI, but they will have a negative effect on efficiency-seeking FDI (Faini 2004). Market-seeking FDI is not very relevant for Africa because its markets are very small. In the services sector, however, especially in energy and information and communication technology, market-seeking FDI has increased considerably in Africa.

The export of services is becoming more important in world trade. Indeed, technical progress has turned services previously nontradable into tradables, increasing the possibilities for outsourcing, which enhances FDI. Because the delivery of services is often associated with the movement of persons, a positive relationship can be assumed between growth of trade, FDI and migration (Faini 2004).

> *The 'brain drain' means a further shortage of skilled workers*

The links between globalization, employment and poverty

There will always be winners and losers from globalization, at least in the short run. The effects on poor people depend on the production factors owned by poor people, such as skills and land, and the goods and services consumed. Poor households typically have several sources of income, not only wages (mainly of low-skilled labour) but also profits from production (mainly in agriculture and the informal sector). Another major source of income is transfers, mainly remittances from family members who have migrated. Because poor people, and particularly poor women, have less access to productive factors, they tend to be less able to respond to change (UNECA 2004b; Winters, McCulloch and McKay 2004).

In Uganda, for example, casual workers on tea estates in the northern region, who have no access to land or formal education, are among the poorest people in the country. By contrast, smallholders who produce nontraditional export crops have increased their income (box 6.1).

Box 6.1
Trade reduced poverty in Uganda but only for parts of the population

In Uganda the sharp decline in poverty by 21 percentage points over 1992–2000, unprecedented in Africa, is considered to be linked to the growth of exports, particularly nontraditional exports (including fish) and tourism. Poverty was reduced in urban areas and in rural areas that grow export crops in the central, western and southern regions. The growth of income for export crop producers led to increased demand for food products and services. For that reason dynamic gains from trade were realized, and the poorer food-crop producers and self-employed in these areas also benefited.

The growth of exports has been supported by macroeconomic reforms, more flexible labour markets and liberalized trade, as well as preferential access to the EU market for horticultural products under the Cotonou agreement. Although Uganda significantly reduced its tariffs in the 1990s, there was no major loss of tariff revenue or surge of imports, partly because of high transport costs.

The success in reducing poverty through increased exports is partly due to the end of civil war and favourable coffee prices. So it might not be sustainable. Furthermore the manufacturing sector did not expand. Instead, wages and employment fell because of increased import competition, and urban wage earners were forced to cope with higher food prices.

The northern region, which produces mainly cotton, tobacco and tea, is still very poor. For small-scale tobacco growers there is only one buyer, BAT Uganda Limited—a situation that leads to exploitation of farmers in the grading and pricing of their product because of the absence of effective producer organizations. Likewise casual workers on large tea estates are among the poorest in the country. As a result 10 per cent of the households that were not poor in 1992 moved into poverty by 1999, partly offsetting the 30 per cent of households who moved out of poverty over the same period.

Source: *Bigsten 2000; Tsikata 2001; UNCTAD 2004b; Morrissey, Rudaheranwa and Moller 2003.*

The employment effect of trade liberalization

According to traditional trade theory, greater openness in an economy leads to more specialization, in line with its comparative advantage. For Africa this implies that sectors intensive in low-skilled labour should expand, because this is the abundant resource. And sectors that are intensive in capital are expected to shrink. The greater demand for low-skilled labour would lead to higher wages in the long run and thus reduce poverty. But employment will increase only if the expanding exporting sector is more labour-intensive than the shrinking import substitution sector (for a detailed discussion see UNECA 2004b and Fosu 2002).

Because trade protection in Africa is generally associated with an anti-agricultural bias, and most poor people are engaged in small-scale agriculture, the liberalization of trade should reduce rural poverty (Berg and Krueger 2003). The higher income of farmers will in turn increase the demand for goods and services provided by the rural poor, such as construc-

tion, personal services, locally processed food and household goods (Winters, McCulloch and McKay 2004).

Low-skilled labour-intensive manufacturing exports should also increase, according to the traditional trade theory. Botswana, Madagascar, Mauritius, Namibia and Senegal have seen their shares of manufactured exports increase over the last decade, driven by labour-intensive sectors such as textiles and garments, but also by food processing, which is less labour-intensive. However, the sharp increase in the number of low-skilled or semi-skilled workers producing manufactured goods for the world market (after the opening of China and India) contributes to the saturation of markets for simple manufactures, reducing prices and wages (ADB 2004).

Low capital intensity is observable in the de-industrialization of import-substitution industries in some African countries. Other factors, such as closing of unsustainable state-owned enterprises, may also have contributed to de-industrialization following trade liberalization (UNCTAD 2002; Lall 1995). For Sub-Saharan Africa the share of manufacturing value added in GDP declined from 17.4 per cent to 14.8 per cent between 1990 and 2002. In Zambia that share dropped from 37 per cent to 12 per cent (World Bank 2004). Several small industries there, such as tire manufacturers and medical supply companies, have folded in the face of competition from large South African firms.

Because trade integration increases competition and shifts the sectoral structure of the economy, more firms enter and exit, increasing temporary unemployment (World Bank 2002). Even in successful globalizers such as Mauritius and Sri Lanka, which substantially increased their shares of trade in GDP, a high unemployment rate persisted over a long period due to structural problems and educational deficits. There is no automatic link between greater market integration and lower unemployment.

There is evidence, however, that demand for female employment will increase through trade and FDI, at least for low skill occupations. Export competition on the basis of cheap labour might increase participation rates of women, who are on average less skilled than men and work for lower wages. This will in principle increase female wages and thus reduce the gender wage gap for similar skills. But this pattern might cement the gender gap in education and thus restrict women to low skill jobs (Oostendorp 2004).

"More trade and FDI spur an increase in female employment"

One reason African countries express concerns over the negative effects of trade liberalization on employment is the relatively inelastic supply response of exports, due to poor infrastructure, capital market imperfections and such institutional impediments as lengthy bureaucratic procedures (Fosu 2002; Lall 1995; chapter 7). While employment in the import substitution sector declines almost immediately, the increase of employment in the exporting sector might take a very long time. Moreover, most empirical studies find an initial decline in wages after trade liberalization, and only later (after more than three years) do wages and employment rise in the export sector (Rama 2003).

An often-overlooked effect of lowering trade barriers is that it might increase the balance of payment deficit because imports grow faster than exports. And if the balance of payments is not self-adjusting because of market distortions, the deficit might become unsustainable.

Demand would thus have to contract, and resources would remain underused, leading to unemployment. There is empirical evidence that trade liberalization has worsened the trade balance significantly in all regions, especially in more highly protected countries (Santos-Paulino and Thirlwall 2004).

These findings mean that traditional trade theory oversimplifies reality. One specific shortcoming is that labour markets in most African countries are highly segmented and far from perfect (chapter 2). Unemployment, for example, is not possible in the neoclassical framework. Segmentation, mainly due to mobility costs across regions and sectors and such institutional barriers as high information costs, may result in significant unemployment (Fosu 2002).

In addition, the skill levels are very different in developed and developing countries. In industrial countries most low-skilled workers are literate and numerate. But this is rarely so in African countries, where a person who is literate and numerate and masters an internationally used language such as English or French is considered semi-skilled. So a product that is intensive in low-skilled labour in an industrial country may be intensive in semi-skilled labour in an African country.

In many African countries the availability of mineral resources determines the comparative advantage.[8] So it is not low-skilled labour that will benefit from greater openness but the owners of the mineral resources. The associated growth of the extraction sector, which usually employs mainly high-skilled labour and has few forward and backward links, is unlikely to reduce poverty (Winters, McCulloch and McKay 2004). Poor people would benefit only if the government spends the royalties it obtains from natural resources on pro-poor policies. The relative abundance of land also partly explains the positive correlation of trade openness and inequality in Africa, because resource ownership is unequal (UNECA 2004b).

FDI increases employment directly but might reduce it indirectly

FDI increases employment directly through hiring. It also has an indirect effect through job creation by suppliers and service providers. Demand for goods and services increases, too, thanks to higher incomes and consequent spending. Estimates of the multiplier effects of FDI in developing countries indicate that around two indirect jobs are created for each worker employed by foreign affiliates (Asiedu 2004). Positive employment effects are associated mainly with greenfield FDI in new sectors. But there might also be a crowding-out of domestic firms and a rationalization effect. So FDI could reduce employment, especially if it occurs through mergers and acquisitions (Lee and Vivarelli 2004).

For example, FDI in agricultural processing, such as food production and household chemicals, could drive local artisanal producers out of business, mainly women who process local agricultural goods in informal businesses. So processing could increase female poverty in rural areas. By contrast, multinationals in the agricultural processing sector tend to employ a large share of low-skilled women, for whom they provide relatively good wages and job security, so that female poverty rates may be reduced.

There is empirical evidence based on U.S. affiliates in Africa that the creation of employment through FDI depends on good infrastructure, openness to trade and education, after controlling for GDP per capita. By contrast, an endowment with natural resources does not increase employment in foreign affiliates (Asiedu 2004). This is consistent with studies that find no employment effect of FDI in mainly African low-income countries but a positive employment effect in middle-income countries (Spiezia 2004).

More trade and FDI could increase productivity

Globalization, and poverty reduction are positively linked to productivity growth through different channels. Both exports and FDI will increase significantly only if a country is competitive in the international market, and competitiveness depends on the ratio of wages to productivity. Closer integration into the world market can increase productivity as well.

There is also a strong link between productivity and poverty. Higher productivity allows wages to rise and thus reduces poverty. But if productivity growth in Africa lags behind other regions, wages have to be reduced for it to be competitive. However, lower production costs through increased productivity could be translated into lower prices and higher real incomes, resulting in increased demand for other products and thus more jobs (ILO 2004b).

A reduction in poverty is usually associated with better healthcare and education, which increase productivity (chapter 5). A virtuous circle can thus be established between productivity and poverty reduction. Most countries have experienced growth in both productivity and employment over the past 20 years (ILO 2004b).

> *Low productivity is proportional to high poverty*

In the manufacturing sector low levels of competitiveness of African firms are reflected in slow growth and low export levels. In Ethiopia, Mozambique and Uganda the value added per worker is only a third of that of India or China. For other countries the relatively high value added per worker is driven mainly by high levels of capital per worker. In Nigeria the capital per worker is 10 times higher than that in India. In addition capital is used very inefficiently in many African countries, with capacity use ranging only between 45 and 80 per cent (Eifert and Ramachandran 2004).

Because of low productivity, labour costs per unit of output in Sub-Saharan Africa generally exceed those in East Asia—this, despite the fact that most African workers receive less compensation than their counterparts elsewhere. In Ethiopia and Uganda wages are less than half the rates in India. With overall labour costs accounting for a small share of the total costs of African firms, competitiveness must come from lower nonlabour costs and higher productivity (Eifert and Ramachandran 2004). Otherwise a reduction in wages would only increase the number of working poor.

Globalization is one channel for improving total factor productivity.[9] Openness could increase productivity through greater import competition and the greater export competition facing firms entering global markets. Evidence from manufacturing firms in African countries shows that exporting has a positive impact on productivity, implying a learn-

ing-by-exporting effect (Bigsten and others 2004). In addition, imports of machinery and intermediary inputs from industrial countries give developing countries direct access to better technology.[10] Similarly, FDI can provide access to advanced technology and skilled management, increasing productivity. FDI can also induce technology diffusion through labour turnover to domestic firms and other forms of interaction.

The increase in productivity associated with globalization could reflect an increase in output using the same amount of production factors as well as a decline in inputs producing the same amount of output. In the latter case the short-term effect of increased productivity will be a reduction in employment. If import competition increases suddenly without complementary improvements in the business environment, the least productive firms will just close down and this will drive the increase in overall productivity.[11] But if higher productivity leads to lower prices and increases output, the reduced demand for labour in per unit output is offset by an increase in labour demand due to output expansion (ILO 2004b).

Empirical evidence shows that globalization increases productivity and thus provides scope for wage increases. For example, in Botswana during a period where trade openness declined, labour productivity was reduced, especially in agriculture. In Algeria and Egypt labour productivity increased during periods of increasing openness (Gros 2004). Further evidence from other African countries shows that labour productivity in foreign-owned enterprises is higher than in domestic-owned enterprises, as in the rest of the world, thanks in part to better training opportunities (Asiedu 2004; UNCTAD 2002).

Because of the use of different technology and different economic environments, workers with the exact same skills are less productive in developing countries than in industrial countries, contributing to the lower wages in developing countries. Although global integration of markets reduces these wage gaps, some will persist due to unfavourable conditions in many developing countries. So the incentives to migrate to regions with higher productivity and pay will not vanish (World Bank 2002).

Although migrating can be beneficial for the migrants, high-skilled migration will have negative effects on the home economy. Because skilled and low-skilled labour often complement each other in production, a decrease in skilled labour (when low-skilled labour is abundant) will reduce low-skilled workers' productivity and wages. Further, skilled labour is needed to attract FDI, and disproportionately contributes to tax revenue. But skilled migration might have positive feedback effects, though with a lag, through remittances, return migration with additional skills and the creation of networks that facilitate trade, capital flows and knowledge diffusion (Docquier and Rapoport 2004).

Globalization can reduce poverty if skill levels and economic structure are favourable

If globalization has an effect not only on the level of income but also on its distribution, it could result in pro-poor or anti-poor growth. It is well established empirically that the main effect of trade liberalization on poverty is through its effect on growth (Berg and Krueger 2003).[12]

But the empirical evidence on the relationship between globalization and inequality is mixed. Cross-country studies do not find an effect of increased trade openness and FDI inflows on wage inequality across occupations or inequality in general, so openness induces pro-poor growth (Winters, McCulloch and McKay 2004; Ravallion 2004; Rama 2003; Vivarelli 2004). But if the type of exports is taken into account, there is evidence that inequality increases for primary exporters but decreases for exporters of manufactures (Calderon and Chong 2001).

Studies trying to capture the direct effects of globalization on poverty also come to the conclusion that it depends on the circumstances. For least developed countries the relationship seems to be asymmetric–with declining exports leading to an increase in poverty and increasing exports reducing poverty only under certain conditions, Uganda shows (see Box 6.1). Thus, for least developed countries no correlation can be found between export growth and changes in private consumption per capita, so little effect on poverty can be expected (UNCTAD 2004b).

African economies require greater diversification as well as more skilled workers

Some empirical studies find a negative (though not very strong) relationship between poverty and globalization, measured in terms of economic integration, personal contacts, technology and political engagement (Heshmati 2004).[13] Others find that a higher share of exports is associated with less poverty for all developing countries, which is in line with the pro-poor growth effects of openness mentioned above. But this effect is stronger for countries with high literacy and a high share of raw material exports (Ravallion 2004).[14] This highlights the fact that complementary policies need to ensure that trade liberalization can reduce poverty.

African countries need to reform to benefit from globalization

There is widespread agreement that liberalizing of trade and investment will increase exports and FDI only if certain preconditions are met, among them, macroeconomic stability, functioning institutions, secure property rights and adequate infrastructure (Winters, McCulloch and McKay 2004; Srinivasan and Wallack 2003; Hoeckman and Javoricik 2004; UNCTAD 2004c). In addition, the empirical evidence presented above indicates that globalization has a positive impact mainly in countries where raw materials are not the dominant exports and human capital levels are fairly high. Because the supply of low-skilled workers in most African countries is very large, wages might increase only for skilled workers. Thus a low-wage, low-skilled development strategy is unsustainable in the long run (ILO 2004b).

Because most African economies are not significantly diversified upward, globalization might increase unemployment and poverty. If the supply-side constraints in sectors with higher value added are not addressed, integration into the global economy will not be beneficial for many African economies (UNECA 2004b).

A main conclusion of this section is that the East Asian success story–market integration in the 1970s and 1980s based on initially low-skilled labour–will not work for Africa. Global

conditions have changed dramatically, and African countries have a different structure from the initial conditions in Asia. Agriculture is much more important, and wages are not downwardly flexible. In fact, compared with labour productivity, wages in Africa are higher than in East Asia. In addition, agglomeration effects might have given the Asian countries a first mover advantage, with the growing industrial sectors located there (World Bank 2002).

To benefit from globalization in the long term, African countries need to diversify their exports into processed goods and manufactures in order to reduce the terms of trade risks and to benefit from growing world demand. To increase productivity, human capital needs to be updated and obstacles reduced for exporters and FDI, especially in infrastructure. Only then will poor people in Africa have a chance to participate in global markets.

Harnessing the potential benefits of globalization

In general, competitiveness in Africa is lower than in other regions, reducing the export sector and FDI's prospects of creating employment. The low efficiency of production is due not only to the low skill levels but also to inadequate infrastructure, obstacles to the private sector and unfavourable economic policies. Competitiveness of production and attractiveness for investors are further hampered by the low labour productivity, which cannot be compensated for by low wage costs, and small markets. To increase African countries' ability to harness the benefits of globalization, they should address these problems but also use industrial policy to boost labour-intensive export sectors, encouraging links between foreign and domestic firms (Wangwe and Rweyemamu 2002).

Education and skills are crucial

Sophisticated modern technologies require high levels of numeracy and a broad base of skills. In this context, formal education should not be equated with skills. It needs to be enhanced by experience of handling particular technologies (Lall 1999). To improve the situation in Africa, both the low efficiency of providing education and the mismatch of skills need to be addressed (chapter 5).

One lesson from East Asia's experience is the attention to the quality as well as quantity of education, including an emphasis on vocational skills, essential for technological change and growth (ADB 2004). East Asia's experience shows that sustained export-led growth requires investment in secondary and tertiary education. In 1960 workers in East Asia and the Pacific had less than three years of schooling, less than in Latin America and the Caribbean. By 1990 countries in the region had the highest average number of years of educational attainment in the developing world, with a marked improvement in the educational attainment of girls, and consistently improved teacher-pupil ratios (ILO 1999). An important pillar of the education system in Asia was the productivity council or centre. These councils identified technical problems of enterprises and developed appropriate remedies and training packages to solve them (Gauci and Paddison 2001).

Demand for skilled labour in manufacturing and services increases where the widespread application of information technology calls for higher levels of skills (Lall 1999). New information and communication technology is dramatically changing the tradability of information-related services. Large companies are increasingly outsourcing information and communication technology functions to external service providers. The global market for such outsourcing, estimated at $110 billion in 2002, is expected to grow to about $173 billion in 2007 (Scholl and others 2003).

The use of ICT can expand markets for SMEs

Africa's share in this market, though tiny, is rising. The number of call centres in South Africa, the biggest player, has increased threefold since 1997. In 2003 there were more than 500 call centres in the country, employing about 70,000 people. It is estimated that the number of workstations related to call centres and back-office services will increase by more than 200 per cent until 2007 (De Vynck 2004). Other African countries such as Ghana (Box 6.2), Mauritius and Senegal have also received investments linked to offshore services (UNCTAD 2004c).

These kinds of offshore services require mainly semi-skilled workers, because the technological content of the work is quite thin. But they require proficiency in written and spoken English, familiarity with the culture of the client countries and social skills. Overall the skills for these jobs, though low in developed countries, are above African national averages, and the entry into information processing could be a building block for future upgrading.

Infrastructure is a key to boosting trade and investment

The lack of reliable infrastructure in African countries is one of the major barriers to trade, leaving them relatively unattractive to foreign investors. Most African firms are hampered by basic problems in transport, energy and information and communication technology (UNCTAD 2001). Low density of infrastructure is partly caused by low population density, and the networks in some countries are further degraded by civil wars, still severe in Africa. Aggravating all this are administrative barriers, which cause severe delays and increase transport costs (UNECA 2004b).

With inefficient state-owned power monopolies as the rule, access to reliable and cheap electricity is a major problem. This inefficiency means high direct costs for electricity and generators—and production losses caused by power outages, 5 to 10 per cent in some countries (Eifert and Ramachandran 2004). In Ghana, where some foreign investors in the information and communication technology sector have started operating, frequent power outages disrupt work and add to the wear and tear on computers. In India, by contrast, where the low cost of labour has always been the attraction, the recent technology changes and infrastructure improvements have made offshore outsourcing economically viable (Furniss and Janssen 2003).

Trends in the quality of transport infrastructure and related transport costs are mixed (chapter 7), posing severe obstacles to exporting, especially for landlocked countries. In Western Africa the ratio of transport costs to the value of exports is 0.33 on average for landlocked countries, almost twice the 0.17 for maritime countries. The exports of landlocked western African

countries are only 12 per cent of those of their maritime neighbours in their per capita value (Faye and others 2004). These high transport costs also shield import substitution industries from competition, with all its positive and negative effects. To increase export opportunities for landlocked countries, regional cooperation in infrastructure provision is essential.[15]

The use of information and communication technologies can expand markets for small and medium enterprises in Africa, as an empirical study in East Africa shows (Chowdhury and Wolf 2003). In general there has been some progress in telecommunications in Africa, with a rapid increase of fixed-line and mobile subscribers from 14.7 per 1,000 inhabitants in 1992 to 70.8 in 2002 (Hale 2003). And access to telecommunication is much higher, because many people share phones through various arrangements, leading to about 6 per cent of Africa's population using mobile phones in 2004 (BBC, 09/03/2005). These improvements were achieved through the entry of new providers of cellular phone and Internet services. But they lag far behind China and India in quality and costs.

For information and communication technology to stimulate exports and attract FDI, African countries need to continue with telecommunications reforms. The reforms include private investment; competition and universal access policies to open, affordable and secure information and communication technology; liberalizing and ending national monopolies; opening the door to the equitable use of telecommunication tools; competition among providers to expand the range and scope of services; and effective and independent regulatory agencies to establish business confidence.[16]

Box 6.2
Outsourcing in Ghana

Ghana is best known for producing cocoa and gold, but today Affiliated Computer Services, a Fortune 500 company from Texas and a global leader in IT and business process outsourcing, is one of the country's largest private employers. Some 1,700 employees process American health insurance claims on their computers—working around the clock in three shifts. The number of staff is expected to reach 2,000 employees by the end of 2004, many of them women.

The key technology in this process is a satellite link that enables data to be sent overseas instantaneously. All the workers at the data-entry facility—from the site manager to the computer-networking technician to the typists—are natives of Ghana. The average employee salary is $1,000 a year, compared with $20,000–$25,000 in the United States. In addition employees receive health insurance, meals and subsidized transport. American supervisors visit only occasionally. Indeed, from their U.S. bases they can view any insurance form in Accra at any moment.

Other foreign investors in the data-entry business also opened shop in Accra, and more are expected to follow. Most of these companies operating in the country have recorded an average increase of 50 per cent in revenue and profits. Now, Ghanaians talk of someday hosting 100,000 computer jobs, or more, with keypunching as a base.

Source: *Hale 2003; Zachary 2003, 2004.*

Infrastructure development is particularly urgent in the rural areas. Most infrastructure in Africa is concentrated along the coasts and in major urban centres, but the majority of poor people still live in rural areas. Improved infrastructure in the rural sector would help it integrate with the urban sector and the global economy. It could enhance the attractiveness for investment not only of agricultural products but also of nonagricultural goods and services (Fosu 2004). For example the export potential of soya beans, shrimps, fish, cashew nuts and gum arabic can be realized only if rural infrastructure services are improved, including extension services and trade support (ADB 2004).

Telecommunications can contribute substantially to lower prices and better delivery, increasing competitiveness. FDI can help in developing and enhancing such infrastructure. But prudent regulation is needed to prevent foreign firms from extracting rents. Privatization programmes in telecommunications and electricity mainly drive the current increase in FDI for services. Unfortunately, in some countries foreign investors withdrew after problems with the regulatory authorities (UNCTAD 2004c). An appropriate balance is required.

"Infrastructure development serves in integration of rural and urban sectors"

Promoting nontraditional exports through export processing zones

Evidence supports the view that the Asian miracle was not driven by liberalization but by well designed industrial policies, including directed credit, trade protection, export subsidization and tax intervention. The East Asian policy package worked because it combined these incentives with discipline through government monitoring and the use of export performance as a productivity yardstick (Rodrik 2004).

African countries, by contrast, are faced with a changed international environment, and the strategies in East Asia will require considerable adaptation. More effort is required to correctly identify sectors that have a true comparative advantage in the longer run and to design industrial policies that provide incentives for increasing productivity rather than rent-seeking.[17]

Export processing zones (EPZs) are one mechanism that many African countries have used to try to take advantage of globalization, but with limited success (Rodrik 2004). Exceptions are Mauritius and Madagascar (Box 6.3). The success of Madagascar's EPZ was assured mainly by French investors, attracted by a French-speaking environment where many of their compatriots had already set up businesses. With time the origin of investors became progressively more diversified.

The choice of Madagascar helped in getting around the textile quotas imposed by developed countries in the Multi-Fibre Arrangements (the quotas of many Asian countries were already saturated), a key factor in attracting investments from Mauritius. Early investments in the EPZ were made in anticipation of AGOA, which granted Malagasy exporters quota-free and duty-free access to the U.S. market in 2000 (Gibbon 2003).

Companies also sought to make the most of the low labour costs in Madagascar. The monthly wage for a low-skilled machine operator in the textile industry is less than a third of the equivalent wage in Mauritius, around half of that in China and about 60 per cent of

that in India (Cadot and Nasir 2001). Even though labour productivity is apparently very much lower in Madagascar than in Mauritius or China (and equal to that in India), unit production costs are among the lowest in the world. In response to increasing labour costs in Mauritius, Madagascar received investments from Mauritian textile industries.

Successful EPZs worldwide share some common characteristics (OECD 2001):

- They get support from the highest levels of governments to create a truly international business environment.
- They are located near major cities and have good transportation links.
- They have a strong management team, which selects enterprises according to success criteria and supports EPZ firms.

Box 6.3
Madagascar's dynamic export processing zones

The Malagasy government began promoting its EPZ in the early 1990s. Output in EPZ enterprises (mainly garments, textiles and aquaculture) increased by about 20 per cent a year from 1997 to 2001 as foreign investors took advantage of the country's low labour costs and incentives under such trade initiatives as the U.S. African Growth and Opportunity Act (AGOA). The growth of EPZs has shifted the export structure away from traditional commodities, including vanilla and coffee. By 2001 EPZ firms created more than 100,000 jobs and accounted for about 50 per cent of all secondary industry employment in the country. They also contributed to some infrastructure development in remote areas and addressed major community needs, such as healthcare and education.

The expansion of EPZs has had favourable impacts on economic opportunities, for low-skilled workers and for women, who made up 68 per cent of workers in the sector in 2001. There has been a significant step up in pay for women, whose main alternative is employment in the informal sector.

But with the requirements for skills intensifying, the share of female workers is falling. The share of skilled workers rose from 36 per cent in 1996 to 66 per cent in 2001 and the share of low-skilled labourers fell sharply. The use of more sophisticated technology and a change in the industrial composition of EPZ firms have increased the demand for relatively skilled male workers. And rising wages have attracted more men.

The expansion of Madagascar's EPZ has a broader potential impact, which includes spillover effects to other sectors of the economy. To export duty-free to the United States, Madagascar must now source the cotton and other raw materials that go into its garment production either locally or from AGOA-eligible countries. This will be good for Madagascar's cotton sector, and an integrated cotton mill already in operation could provide the necessary inputs.

Source: *IMF 2003b; Glick and Roubaud 2004.*

EPZs can help increase exports and attract FDI only if they are embedded in an outward-looking strategy of development. The long-term aim should be to reduce distortions that limit competitiveness in the whole economy. Then the export incentives meant to compensate for these distortions in the EPZ will no longer be needed (ADB 2004). This approach will also help to integrate EPZs better into the domestic economy.[18]

Target investment in labour-intensive sectors

Most African countries pursue policies to attract FDI, if with limited success. Although the rate of return on FDI is higher in Sub-Saharan Africa than in other regions in the world, there is evidence of systematic bias against Africa because of a high perception of risk (World Bank 2002). Consistent with this bias, FDI to Africa is systematically lower than would be predicted by the fundamentals (Jaspersen, Aylward and Knox 2000). Useful tools to change this bias can be marketing the locational advantages of African countries and correcting a poor image through independent country ratings.[19]

Some of the East Asian globalizers managed to kick-start their industrialization by targeting specific sectors for learning-by-doing. But given the speedy changes in technology and the global economy, the risks of targeting have increased. And, the fallacy of composition suggests that if many countries see the same sector as lucrative, competition will intensify, limiting the benefits. Rather than target specific sectors, the overall environment for investment, and especially for upgrading technology, should be improved (Fosu 2004).

> *EPZs in Madagascar meant more jobs for women*

Investment promotion agencies attract foreign investment in labour-intensive sectors expected to have a long-run comparative advantage.[20] For example, tax incentives could increase with labour intensity (Fosu 2004). And to overcome information asymmetries, feasibility studies for these sectors can be provided to potential investors. But such support measures are secondary to a conducive investment climate. To work, they need to be precise transparent and predictable–and their administration streamlined (UNCTAD 2000b).

It is not enough to attract FDI. More attention should go to domestic firms, which need support to increase productivity and product quality through the adoption of new technologies (UNECA 2005). Instead of using a pick-the-winner strategy for providing business support, it would be better to select firms with strong backward and forward linkages to the rest of the economy, increasing the externalities from technological upgrading. One example of this approach is to target the packaging sector as a crucial input to agricultural processing industries. In many African countries, most packaging material is still imported.

It is also imperative to strengthen the institutional capacity of governments and administrations to design appropriate macroeconomic and other reform policies, as well as provide essential public goods and services. This includes improving (or starting) the policy dialogue between government, the private sector and civil society, to help build consensus on long-term strategies and avoid frequent policy reversals.

Linkage-intensive industries create spillover effects

To enable a larger share of the population to benefit from globalization, African governments should promote trade and attract nonmineral FDI in linkage-intensive sectors. These linkages could be through demand for local products, through the supply of products and services to local firms and through knowledge spillovers.

Promoting linkages is not easy. The willingness of foreign firms to create and strengthen local linkages can be influenced by government policies addressing relevant market failures. For instance, foreign firms may be unaware of the availability of viable suppliers. African governments should address such market failures without imposing domestic content requirements, which tend to discourage FDI (UNCTAD 2004c). The linkage programmes should focus on the competitive needs of domestic enterprises, including private and public support services as well as skills and technology upgrading (UNCTAD 2001).

Spillovers of knowledge and management skills to local firms are among the most critical benefits of FDI for host countries. Policies facilitating this process have a greater likelihood of success. In Tunisia the government pays up to 50 per cent of the training costs in connection with technological investment (WTO 2002).

Links between foreign and domestic firms tend to change. Initially foreign affiliates mainly import inputs from overseas suppliers with whom they have strong ties. As they get to know their new environment, they tend to diversify supplies in the host country. Success depends on the ability of domestic suppliers to deliver quality products and services. Sometimes foreign firms provide support to local suppliers to help them meet the required standards. Another possibility is for them to induce their traditional suppliers to invest in the host country (Lall 2002).

For forward linkages, agroprocessing is of special interest because it is one of the most linkage-intensive industries in developing countries. It generates demand for perishable agricultural inputs, such as milk and vegetables, which have to be sourced locally. And because it is labour-intensive, agro-processing will improve labour markets (ADB 2004).

In Vietnam, for example, Unilever built partnerships with local suppliers of raw materials and packaging materials, offered financial support and shared knowledge, while getting access to higher quality inputs (Box 6.4).

Another linkage-intensive sector with good potential in Africa is tourism. In 2003 travel receipts increased by 25 per cent, more than twice as fast as global travel receipts. North Africa hosts nearly two-thirds of tourists visiting the continent, Southern Africa nearly a third. The World Tourism Organization forecasts 5 per cent annual growth for Africa until 2020, above the world average of 4.1 per cent. Africa is projected to be the destination for 47 million tourists in 2010 and 77 million in 2020. The highest growth rates are in Central, Southern and East Africa, while West and North Africa have moderate growth rates (World Tourism Organization 2004).

Tourism can generate direct and indirect jobs in hotels, travel agencies, transport firms, restaurants and national parks and monuments. It is labour-intensive, with 3.3 employees per hotel room in Africa, compared with 0.5 in Europe and 1.7 in Asia (World Tourism Organization 2000). Tourism projects can be of particular interest for coastal regions, insular territories and vulnerable rural or mountainous regions that have suffered from the decline of traditional activities and tourism is one of the rare development opportunities.

Because a major part of African tourism depends on natural and cultural resources, which need to be protected, Ethiopia, Morocco, Namibia and Senegal are introducing eco-tourism policies, certifications and labelling systems (UNECA 2003b). Local people must be involved in tourism activity, making them beneficiaries of the sector while protecting their traditions and lifestyles. This could be achieved, for example, through the support of local craft manufacturers and food and service producers.

A more advanced linkage is a science and technology park, established to accommodate high-technology firms with supporting infrastructure. The parks are on or close to a university research campus to promote the cross-fertilization of ideas between entrepreneurs and researchers, enabling academic knowledge to be applied commercially. Several parks have business incubation facilities on site, providing below-market rents, shared services and technical assistance to new technology businesses. A successful example: the Science and Technology Park in Tunis (UNIDO 2003).

Box 6.4

Unilever in Vietnam: building partnerships with suppliers

Unilever started operating in Vietnam in 1995 and by 2000 had total sales of over 170 million, with many of its brands in leading positions. Its relationships with its suppliers are vital, because they account for 40 per cent of the company's production volume, 20 per cent of its raw materials and 87 per cent of its packaging materials.

The company-supplier relationship is symbiotic: both parties need one another to succeed. Unilever supports its suppliers through training and technology transfers. It also offers them financial support to upgrade their equipment. In turn, the suppliers provide the company with sophisticated packaging or with materials that meet exact specifications.

Business growth at Bicico—a supplier of detergent paste—have developed favourably. Bicico's production volume grew from 3,000 tons in 1996 to 23,000 tons in 2000, and the number of employees from 12 to 250. Quang An 1 became a supplier of plastic bottles for Unilever's factory in Hanoi in 1997. It increased its business with Unilever sixfold in three and a half years. And its improved capabilities enabled it to win new business from other foreign and local companies.

Source: *UNCTAD 2001; Unilever 2001.*

Linkage-intensive, agro-processing has a spillover effect

Regional integration can be a stepping stone to global markets

One major obstacle for most African countries is their small markets, preventing firms from exploiting economies of scale, not attracting market-seeking FDI.

Regional integration could help African countries in diversifying exports and pooling scarce resources to overcome development thresholds. For example, the Southern African Development Community (SADC) countries are sharing knowledge on agricultural research and training, which should increase productivity. The Economic Community of West African States (ECOWAS) has introduced the ECOWAS Passport, which facilitates free movement of people and thus increases the scope for cross-border linkages between enterprises (UNECA 2004a).

To make regional integration a stepping stone for global integration, however, the memberships in overlapping regional communities need to be rationalized, protocols ratified faster and secretariats strengthened. Furthermore, the private sector, which has to be the main creator of new jobs, should be involved more in identifying, formulating and implementing integration policies and programmes. Firms that operate across borders will benefit from rationalizing rules of operations across countries (UNECA 2004a).

For landlocked countries regional integration is crucial to secure access to international markets. This is true for physical infrastructure of roads, railways and ports, which have to link the member countries, and for administrative coordination. The SADC and the Common Market for Eastern and Southern Africa (COMESA) now have common licences and third-party insurance guarantees across countries, substantially reducing transport costs. Streamlining bureaucratic procedures and reducing paperwork could reduce border delays, which will reduce transport costs and the need to keep large inventories (Faye and others 2004).

Trade support measures could also be provided on a regional basis. For example, information on international trade policies and market developments is essential for entering new export markets (ADB 2004). Because the comparative advantages for countries in a geographic region tend to be similar, regional cooperation can avoid a duplication of efforts in collecting this information. Current information on international health, safety and environmental standards is also important for exporters in different countries.

Regional networks of trade support institutions should be strengthened to provide: trade policy information, commercial intelligence, export promotion and marketing, product development, financial services and training. Because no single institution can provide all these services for different sectors effectively, a regional division of labour could benefit all participating countries (OECD 2001).

New opportunities for women through globalization

Trade and FDI can create new opportunities for women, the most affected by underemployment and poverty in Africa. Evidence from Indonesia shows that foreign-owned agricultural enterprises employ a higher share of women and pay higher wages than do domestic-owned plantations (Siegmann forthcoming).

Over the last decade high-value agricultural exports have created substantial opportunities for wage employment and self-employment, with women particularly able to capitalize on the new opportunities. In Africa high-value agricultural exports are female-intensive industries, with women dominating most aspects of production and processing (Dolan and Sorby 2003). In Zimbabwe women occupy 79 per cent of the employment in these industries (Box 6.5) (Davies 2000).

Job security for women has two important outcomes: it raises the standard of living for their families, and it gives them more freedom of choice.

Box 6.5
Three examples of how women benefit from globalization

Zimbabwe has diversified its exports by developing a dynamic cut-flower industry. In 2000 the country was the second largest exporter of cut flowers from Africa, after Kenya, and the third largest in the world. Although affected by the current economic decline in Zimbabwe, the sector is still vibrant. The rapid expansion of the industry has not had a significant impact on total employment, but it has influenced the composition of the workforce, both in terms of seasonal versus permanent and in terms of male versus female workers. Growers were encouraged to promote job security by making all workers permanent, increasing the number of permanent female employees. About 27,000 Zimbabweans were employed in floriculture at the end of the 1990s, 79 per cent of them women.

In West Africa, particularly in Burkina Faso, women have taken advantage of the burgeoning international interest in the environment and "natural" products to export shea butter, or karité, the natural ingredient in skin moisturizers, lip balms and eye creams marketed by many exclusive cosmetic lines in the United States and Europe. Karité is one of the few commodities under women's control in Sahelian Africa and ranks third in Burkina Faso's exports.

In Senegal the number of women working in information and communication technology community services has increased in the last two years, with 35 per cent of the cyber cafes and telecentres owned by women. In Côte d'Ivoire, The Gambia, Guinea, Morocco and Nigeria women have started running cyber cafes, telecentres and telephone shops. Moreover, in the data processing enterprises mushrooming in South Africa, Ghana and other countries, a large share of employees are women, giving them more income to improve their living conditions.

Source: *Davies 2000; EIU 2005; Carney and Elias 2004; Diop 2003.*

"High-value agricultural exports create opportunities for wage-employment"

For women to really share the opportunities of globalization's decent jobs and higher wages, African governments should increase their efforts to improve the female literacy rate, only 53 per cent in Sub-Saharan Africa, compared with 69 per cent for African men and 74 per cent for women worldwide. In Sub-Saharan Africa only 23 per cent of girls were enrolled in secondary education between 1997 and 2000, compared with 29 per cent of boys.[21] The rest can neither read nor write the foreign languages used on computers. Even the majority of those who have been to school do not take science, engineering or computer sciences (UNICEF 2004; UNECA 2005), discouraging their employment in technologically skill-intensive sectors.

How to mitigate the negative impact of globalization?

African governments need to cushion the most vulnerable groups against the adverse effects of globalization. These include laid-off workers in import-substituting industries, especially low-skilled workers, and poor people, who often lack assets to invest in productive activities.

Ways to mitigate the adverse effects of globalization requires providing basic social security, retraining workers for growing sectors and improving access to education and credit. In addition, institutions need to be modernized to improve information flows in the labour market and increase contract enforcement. This will enable African countries to participate in global value chains. Moreover, the links that migrants can establish between their country of origin and their country of residence can be useful for integrating into the world economy.

Globalization might increase risks for firms and workers

Households employ different strategies to deal with falling incomes. One important strategy is for household members to migrate to locations with better employment prospects or lower costs. Households also postpone spending on durable goods and dissave by selling gold and other assets, usually owned by women. And they may sell such productive assets as land or livestock or reduce spending on education, especially for girls, cementing gender inequality.

Poor households cannot use many of these strategies, so the adjustment costs are especially high for them (Winters, McCulloch and McKay 2004). They are not covered by social security, which typically includes only state employees, and group insurance works better among people slightly better off.

An increase in world market prices of agricultural products might not benefit the rural poor living in remote areas (Winters, McCulloch and McKay 2004). Why? Because in many African countries, with high transport costs and inefficient distribution systems, the transmission of changes in border prices is limited. Globalization might thus benefit only coastal areas and capitals, increasing regional disparity and inequality within the country.

Most South-East Asian countries, as well as China and India, achieved high growth and a substantial reduction of poverty in parallel with deeper integration in global markets. But urban poverty fell much faster than rural poverty, increasing inequality even before the financial crisis. In Thailand the gap between the highest per capita income region and the lowest increased from about seven times in 1982 to nine times in 1992. In China the massive increase of FDI inflows and exports was associated with a dramatic increase in income inequality, due to segmentations in labour and capital markets (Zhang and Zhang 2003). A crucial question is whether the socioeconomic system would enable the initially disadvantaged regions to catch up, avoiding otherwise serious social and political consequences (Pangestu 2001; UNCTAD 2004b; Srinivasan and Wallack 2003). Improving rural infrastructure clearly is one remedy for these problems (Fosu 2004).

The lack of property rights enforcement also limits the gains from globalization in Africa (chapter 7). And the barriers to formalization tend to limit firm size. So firms in the informal sector cannot benefit from increased export opportunities, and they rarely enter supply arrangements with multinationals (Hoekman and Javorcik 2004; ILO 2004a). Because the urban informal sector mainly produces nontradables, workers in this sector have little opportunity to gain from globalization. The rural informal sector is involved in producing export products, but the participation in global value chains is becoming more competitive (Fosu 2002).

> *Governments play an important role in mitigating risks of globalization*

For many commodities produced by African countries, world market prices have been relatively volatile, with the prices of several of the commodities declining.[22] For example, if a competing country introduces a product of higher quality, prices for the normal quality product can drop suddenly, or it may no longer be marketable. This was the case for pineapples: Costa Rica introduced a new variety with a longer shelf life and African producers lost their market share.

Globalization can weaken the bargaining power of workers through increased competition. In particular, low-skilled workers employed in sectors where competition is based on cheap labour are likely to suffer from downward pressure on wages. Because of the high unemployment in Africa, real wages are downwardly flexible,[23] and it is more likely that increased demand for low-skilled labour would increase employment but with minimal increase in wages. This will reduce poverty only if the wage in the affected sector lies above the poverty line (Winters, McCulloch and McKay 2004; Cornia and Court 2001). Because women on average have lower skills than do men in most African countries, they will be most affected by these developments (Oostendorp 2004). To overcome low wages, better education or broader training is required.

The greater competition with globalization requires more flexibility of both workers and firms, for faster delivery and for producing to different specifications for different markets. This flexibility can be achieved through technological and management changes but also through forms of employment that are temporary, part-time, casual or contract-based. In developing countries larger enterprises keep only a small core labour force of mainly highly skilled men and respond to changes in market conditions by subcontracting labour-intensive tasks to smaller firms,[24] which have less favourable working conditions, especially for women. In the cultivation of horticultural products, women are often concentrated in temporary and seasonal employment (Barrientos, Kabeer and Hossain 2004).

Macroeconomic risks of globalization

Openness to global capital markets can bring greater volatility in domestic financial markets. If capital inflows are large and short-term, the risk of abrupt reversals can reduce financial stability and job security. For example, the massive outflow of private funds from East and South-East Asia coincided with a rise in unemployment from 5.3 million people in 1996 to 18 million in 1998 (Carr and Chen 2004). In Indonesia and Thailand the workforce was affected mainly through falling real wages and underemployment rather than open unemployment. Younger, less educated and informal sector workers were most affected. Real incomes in Thailand dropped most for people who had not completed primary education. To avoid these negative impacts African governments need to liberalize their capital accounts and financial sectors very carefully, use compensatory policies and encourage competition in domestic financial systems (box 6.6).

There is no immediate risk that the kind of financial crisis that hit East Asia towards the end of the 1990s could also affect Africa. Low-income countries have received only 1 per cent of the total portfolio investment in 2002, compared with 6.9 per cent for China and India (Gunter and van der Hoeven 2004). In addition, many of the Asian countries have recovered quickly, suggesting that the negative impacts can be temporary. A complementary regulatory framework and an appropriate sequencing of liberalization should be used to reduce the risks (Fosu 2004).

The ability of governments to raise taxes might decline due to the greater mobility of resources. And because capital and skilled labour are relatively mobile, their taxation has become even trickier. If low-skilled workers are taxed too much, they will stay in the informal sector (Srinivasan and Wallack 2003).

Globalization might reduce governments' ability to finance social services. One option for governments is to harmonize taxation across regions so that investors face similar tax costs in countries with similar conditions. In addition, due to the greater mobility of the more educated, societies face elevated capital losses in tertiary education subsidies. So it might be advisable to direct government spending towards less mobile factors, such as infrastructure and primary education (Fosu 2004).

Social protection for workers and flexibility of labour markets

To address the risks of globalization, workers require social protection that would reduce the adjustment costs. This includes some form of protection against unemployment, which now depends largely on having a job in the formal sector.[25] Of special importance are retraining programmes that facilitate labour mobility across sectors (Fosu 2004).

Safety nets would reduce adjustment costs and possibly have some dynamic effects. Providing poor farm households with protection against income losses, for instance, would allow them to take on riskier but higher return activities and thus raise their income. In the absence of credit markets a redistribution of resources from the rich to the poor could

Box 6.6

Mitigating risks associated with financial globalization

During the past few decades financial markets around the world have become more interconnected. Global gross capital flows in 2000 amounted to $7.5 trillion, a fourfold increase over 1990. The globalization of finance has brought considerable benefits to national economies and investors, but it has also changed the structure of markets, creating new risks and challenges for market participants and policymakers. Because financial globalization is inevitable, African countries should design appropriate policies to harness its benefits and minimize the risk of financial crises.

Precede capital account liberalization with banking sector liberalization

African countries should pay more attention to the development of the domestic financial sector, which can be opened to foreign participation without necessarily opening the economy to capital flows. At the very least, financial liberalization should precede capital account liberalization, and African countries should contend with liberalizing the financial sector for an extended period before opening their capital accounts. China has achieved some good results with this strategy.

Use compensatory policies

A number of Asian and other emerging economies have instituted a range of compensatory policy changes that would help them avoid or respond more effectively to capital flow reversals. The most important issue is exchange rate flexibility and large increases in holdings of foreign reserves.

Introduce interim regulation

Successful capital account and financial sector liberalizations entail multiple stages that usually call for different sets of regulatory approaches before, during and after. Failure to tailor these regulatory approaches may cause a country to endure unnecessary pain in the short term or even retard its move towards the desired state. The imposition of fairly inflexible rules, such as the elimination of all capital controls, is surely misguided.

Encourage competition in domestic financial system

Policymakers should allow some tinkering at the margins and encourage competition in the domestic financial system from foreign banks and other financial institutions. African countries should keep a close eye on the composition of capital flows. If these flows are short term, intermediated through banks and denominated in foreign currencies, they are much more likely to lead to a financial crisis than if they are long term, denominated in domestic currency and in the form of FDI.

In short, the risks associated with financial globalization are very real, and African countries that open their financial markets need to develop strong financial systems and sound economic and financial policies.

Source: *Häusler 2002; IMF 2003a.*

“Retraining is key to cross-sectoral mobility”

increase the average return to investment and thus stimulate growth (Smith and Subbarao 2003; Srinivasan and Wallack 2003).

Adapting to globalization requires flexible labour markets, but the flexibility needs to be carefully designed. High obstacles to hiring and firing reduce employment incentives and might lead to higher capital intensity, but longer term contracts can provide higher incentives for workers to improve productivity. Minimum wages, if set at a reasonable level, can provide stability and foster the commitment of workers, increasing productivity and reducing poverty at the same time (Cornia and Court 2001; Fosu 2004).

Increasing the opportunities for women in higher value jobs requires addressing their double workload. In most developing countries, especially in Africa, women bear the bulk of reproductive and household tasks, and participation in the labour market increases their workload considerably. Opting out of work to care for children reduces the returns to education and training and thus limits the potential gains from globalization for women. Educating girls can help countries mitigate these problems, for instance by expanding the facilities for childcare (Siegmann forthcoming).

Value chains increase competition among workers worldwide

Demand for exotic fruit and fresh vegetables is expected to grow in industrialized countries, providing opportunities to diversify agricultural production in Africa and to link poor people to global market. But in high value consumer goods–such as garments, leather goods, electronics and horticultural products–the markets are dominated by large brand name companies or retailers, which source their products through a network of global suppliers.

The tight management of these global value chains by multinationals requires products of higher quality and more reliable supply, which small firms in African countries might not be able to deliver. Most retailers develop close relationships with a group of preferred suppliers and integrate their supply chains ever more tightly, making the entry of new suppliers difficult (Dolun and Sorby 2003).

Suppliers must also comply with strict technical and environmental standards to remain part of the supply chain. If not, large retailers will shift to other countries. For example, the near complete stoppage of EU fish imports from Tanzania in 1997/98, due to problems with phytosanitary standards, reduced the incomes of fishers by 80 per cent (Henson and others 2000).

To increase the benefits to workers from the production of high value agriculture, therefore, it is essential to link smallholders to international markets (Chapter 4). In Kenya increased air travel for tourism reduced the cost of airfreight to Europe and provided transport opportunities for small quantities of fresh products. Tourism also increased local demand for high quality fruit and vegetables and provided an outlet for produce not meeting export standards. Because the horticultural sector is too diverse and too fast-changing for a direct

involvement of the state, governments should allow a variety of private institutions and marketing arrangements, as in Kenya.

To help small farmers participate in value chains for export, governments should support farmer groups and joint irrigation schemes. And to facilitate the adoption of innovations, they could provide market information and extension services and establish standards. Probably the most important role for government is to develop new institutional arrangements that would facilitate the enforcement of contracts between farmers and exporters. These measures can reduce the risk in the production of high value vegetables for both farmers and exporters and increase the participation of small-scale farmers (Minot and Ngigi 2004).

For sectors where smallholder production is not feasible, piece-rate wages can provide workers with higher incomes to lift them out of poverty, particularly in packing fruits and vegetables (Dolan and Sorby 2003). Because such wages increase incentives for workers, the costs of supervision for the enterprise are reduced, benefiting both firms and workers. But in many African countries, piece-rate payment schemes are prevented by strong unions or labour laws, which need to be reconsidered (Chapter 7).

> *Piece-rate payment schemes are often stopped by unions*

Using the African diaspora to create employment

The migration of skilled workers from Africa to industrial countries increases the scarcity of skills and reduces the returns of government spending on education. Ways need to be found to harness the potential contributions of international migration for sustainable development. The main channels are remittances, investments, skill transfers and diaspora networks (IOM 2004).

Worldwide remittances have become the second largest source of financial flows after FDI. Growing fastest, they are the most stable capital inflows into developing countries, reducing poverty and vulnerability. The amount of reported remittances has increased from $8.6 billion in 1990 to $11.1 billion in 2002. Africa received about 15 per cent of global remittances, with the bulk going to North Africa. For Sub-Saharan Africa as a whole, remittances contributed 1.3 per cent to GDP in 2002, but for some countries the contribution exceeds 10 per cent. With a significant part remitted through informal channels and therefore unreported, it is estimated that actual remittances are at least twice the official figures (World Bank 2004; Docquier and Rapoport 2004).

So far around 80 per cent of these remittances are used for consumption and schooling. But they can also contribute to upgrading infrastructure (Box 6.7). Even if remittances are used for consumption-smoothing, they increase the demand for local products through multiplier effects. They also increase foreign exchange reserves.

Box 6.7

Remittances for infrastructure in a Senegalese village

According to government estimates, the money remitted every year in Senegal exceeds €600 million, 12 per cent of Senegal's GDP and more than its receipts of official development assistance.

The remittances cover basic daily needs and contribute to the development of poor regions, as in Waoundé, a small Senegalese village. Migrants finance most of the village's collective projects, such as the post office, water pumps, a water tower, a community clinic and a school renovation.

Waoundé is isolated six months a year during the rainy season. Rivers overflow and block the only road leading to it. In 2001 the French government promised to build a new road and a bridge but it required a small financial contribution from the locals. They called on migrants, who paid without hesitating.

Source: *L'Express 2004.*

"Worldwide remittances to Africa are second after FDI"

Remittances are now sent more through formal channels, particularly where the exchange rate regime has been liberalized, as in Uganda. But the tightening of regulations in industrial countries that are intended to fight money laundering and financing of terrorist activities makes the banking system less accessible for migrants and increases the cost of transfers (Sander and Maimbo 2003).

Some African countries have schemes to attract remittances into the formal banking sector and provide incentives for investing them. In Morocco more than 60 per cent of remittances are sent through Groupe Banques Populaires, with branches in Europe. Most emigrants transfer their remittances through the basic checking account, and the relative in Morocco can withdraw money in local or foreign currency at no cost. The bank also provides subsidized credit for real estate and business investments.

Migrant networks should be regarded as an asset and ways to better exploit them should be explored. Because contract enforcement across borders is especially difficult for small and medium enterprises, ethnic networks can foster cross-border trade and investment links. Migrants can also facilitate the flow of information and knowledge and contribute to technological progress.

Return migrants, with their new skills and attitudes, can help to expand employment by engaging in the private sector. They have accumulated savings as well as skills, experience with the business culture in industrial countries and links to those countries–a good basis for starting an export-oriented business. A growing number of Tanzanian women have returned from abroad and started various businesses, including Tanzanite Jet Services, which specializes in meeting the technical and bureaucratic needs of visiting private jets.

A strategy to encourage the return of skilled emigrants should be incentive-based, as in Tunisia (Mesnard 2004). Without an improvement in the business climate that allows

adequate returns, few migrants will return.[26] Several countries, such as Mali and Sudan, are providing tariff exemptions for imported goods, favourable exchange rates and financial support for skilled migrants who want to return home. Host countries could also improve incentives by withholding social security contributions until a worker returns home, with savings that could be used to set up a business (Rodrik 2005).

Conclusions

Globalization offers many opportunities for development but fewer guarantees. To benefit from globalization African countries need to improve their competitiveness and efficiency through policies that favour trade and FDI, while minimizing the risks caused by factors that are outside their control.

Employment is sustainable only when productive activities are competitive in the long term. This can be achieved through productivity enhancements, so that competitiveness is based not just on low costs but also on greater flexibility and stronger links within the economy and across borders (ECLAC 2002). Key areas for improving productivity are upgrading skills and infrastructure. Deeper regional integration can also increase efficiency and improve economies of scale. Direct support for nontraditional exports and labour-intensive investments has to be targeted very carefully to set the right incentives.

To facilitate the adjustment process induced by globalization, priority should go to reducing market failures—through long-term finance to small and medium firms, through training (especially technical and managerial) and through the provision of information. These services should be provided by governments in cooperation with business organizations (Hoekman and Javorcik 2004).

"Globalization sets trade priorities for PRSPs"

One way to reap globalization's benefits in employment and poverty reduction and reduce the associated risks would be to set priorities for trade and private sector development in Poverty Reduction Strategy Papers. Although recent Poverty Reduction Strategy Papers are more growth-oriented and include a range of trade objectives, the links between these goals and the priority actions need to be strengthened. Only 8 of 21 countries with Poverty Reduction Strategy Papers explicitly link the creation of employment to global or regional integration (chapter 3). The labour intensity of export production and FDI, the links to the domestic economy and the dynamic comparative advantages need to be taken into account (UNCTAD 2004c).

Endnotes

1 For an analysis on how to reshape the governance of globalization on the international level to work for all the world's people, see ILO (2004a).

2 Ethiopia, Ghana and Zambia witnessed rapid growth in manufactured exports but from a low level, compared with Mauritius, South Africa and Zimbabwe. In 2003 Africa's trade grew faster than the world average in manufactures, agriculture and especially commercial services (WTO 2004).

3 Migration also increased, though at slower rates than FDI. This implies that the growth in trade did not come at the expense of reduced factor mobility (Faini 2004).

4 The distribution of inflows was broader based than in previous years, with 22 countries receiving more than $0.1 billion in FDI, including several small countries and least developed countries. But the bulk of the increase went to the oil sector, especially in Equatorial Guinea. In addition, a few projects accounted for a large share of the increase, such as a merger in the tobacco sector in Morocco worth 1.7 billion (UNCTAD 2004c).

5 U.S. foreign affiliates with data available doubled employment from 35,100 in 1990 to 74,100 in 2002, mainly in food processing and transportation equipment. These figures might appear small, but because U.S. FDI to Africa accounts for only around 20 per cent of total FDI to Africa, this gives some indication for future prospects (Mataloni 2004).

6 Figures about migration and remittances are generally underestimated because only official flows are recorded, whereas a large number of migrants are illegal, and remittances are transferred through informal channels.

7 For a more detailed discussion of the causes and effects of skilled migration, see chapter 2.

8 Natural resources—not unskilled labour—are the relatively abundant factor of production.

9 The static effects of trade and FDI on wages and employment differ, while their dynamic effects go mainly in the same direction.

10 However, if specialization according to static comparative advantage leads to a concentration in sectors with low productivity growth, trade liberalization might restrict productivity gains and growth potential. So the temporary protection of dynamic sectors might be beneficial where a country expects to have a comparative advantage after a learning process. (Rodriguez and Rodrik 1999).

11 Greater competition in import substitution sectors can also reduce output and therefore capacity utilization, pushing up higher costs. For co petition to increase productivity, barriers to entry and exit both have to be reduced (Hoekman and Javorcik 2004).

12 Trade openness could increase long-run growth through more diffusion of technology, increasing economies of scale in larger markets, higher incentives for capital accumulation and reductions of rent-seeking activities, among others. But there are also a lot of disagreements and contradictions in the vast literature on trade and growth. For example, it is very difficult to distinguish between the effects of trade liberalization and other reforms. The measurement of trade liberalization is itself tricky. And least developed countries have been excluded from many analyses, due to a lack of data (Berg and Krueger 2003).

13 Economic integration is composed of trade, FDI, portfolio capital flows and income payments and receipts, all given as share of GDP. Personal contacts consist of international telephone traffic, international travel and tourism, and transfer payments and receipts. Technology transfer comprises Internet users, Internet hosts and secure Internet servers relative to population (Heshmati 2004).

14 It is also likely that trade liberalization will not have a big effect on poverty reduction in African countries with high inequality. Trade liberalization increases growth but does not have a significant impact on inequality. The growth would mainly reach the relatively rich (Fosu 2005).

15 Because transport and energy infrastructure have been covered in detail by Economic Report on Africa 2004 (UNECA 2004b), the recommendations here focus on telecommunications.

16 By 2004, 36 African countries had established a separate regulatory authority, 24 of them autonomous in their decisionmaking (ITU 2005).

17 Although World Trade Organization rules generally restrict the use of export subsidies, almost all African countries are exempt from this rule because their per capita GNP is below $1,000 a year (UNCTAD 2003b).

18 Because domestic suppliers of intermediate inputs have to pay tariffs on their inputs, it is difficult for them to compete with foreign suppliers. This effect adds to the isolation of EPZs from the rest of the economy.

19 The financial sector and labour market regulations are often not conducive, either (chapter 7).

20 For the garment and textiles industry the phasing out of the Agreement on Textiles and Clothing at the beginning of 2005 is increasing the competition from Chinese producers tremendously. Therefore countries such as Morocco and Tunisia, where textiles and garments are the most important export products, are likely to suffer production and export losses, with negative impacts on their labour markets (UNECA 2005).

21 In North Africa, however, the same numbers of girls and boys are enrolled in secondary education.

22 On average prices for food fell by 12 per cent between 1991 and 2002 and those for agricultural raw materials by 28 per cent (UNCTAD 2003a). For nontraded agricultural products, price fluctuations due to weather conditions can also be extreme, aggravated by the lack of storage facilities and credit constraints. In Ethiopia the domestic price of maize dropped by 60 per cent after a bumper harvest in 2001/02, adding to the negative effects of the drought in 2003 (Ethiopian Economic Association 2004).

23 Because inflation has been fairly high in most African countries, real wages can decline even if nominal wages increase. In low- and middle-income countries unskilled workers' wages fall faster than per capita GDP and profits during stabilization efforts. The rise in the wage share during the subsequent recovery tends to be slower than the previous fall (Cornia and Court 2001).

24 The opening of formerly protected sectors can result in a deterioration of working conditions. In Morocco firms shifted from permanent employees, who enjoyed a number of benefits, to lower paid temporary workers. The share of temporary employment in manufacturing increased by nearly 20 percentage points in six years (Rama 2003).

25 Health benefits are often linked to employment, so the loss of a job also reduces the access to healthcare.

26 For a detailed discussion on how to improve the business climate and foster entrepreneurship, see chapter 7.

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Chapter 7

Enabling the private sector to create jobs

Traditionally the largest employer in Africa, the state has to facilitate investment and job creation in the private sector, especially in small and medium-size enterprises (SMEs). SMEs and the informal sector account for about 63 per cent of employment in low-income countries (Ayyagari, Beck and Demirgüç-Kunt 2003). In addition to being labour-intensive, they appear to have the greatest potential for job creation due to the scarcity of capital for large investments (Beck, Demirgüç-Kunt and Levine 2003).

Most African economies have been more stable since the mid-1990s. But the stabilization programmes have done little to increase private investment. Further and deeper second-generation reforms are needed to improve physical infrastructure and the business environment, to prepare the financial market for small-scale lending and to ensure flexible labour markets. This chapter examines the key issues in creating an enabling environment for the private sector, particularly SMEs.

> *Second-generation reform is needed to ensure progress*

- ***Promoting good governance.*** Based on a continent-wide survey by the United Nations Economic Commission for Africa (UNECA), governance is getting better in most African countries, though many governance-related constraints on private activity remain. The obstacles: centralized government structures, inefficient government services, corruption, the low integrity of the tax system and the lack of transparency and accountability of civil services (UNECA 2004b).

- ***Ensuring a conducive macroeconomic environment.*** Government policy should continue to concentrate on ensuring a stable macroeconomic environment conducive to private investment. Tax policy remains a key variable, as most firms consider it one of the major obstacles to business growth. Tax reforms in Africa should thus be deepened to simplify the tax system, improve tax administration and reduce tax holidays to a minimum, confining them to projects that meet specific export or employment targets.

- ***Improving physical infrastructure.*** Infrastructure development in Africa has been constrained by a lack of public resources and by the difficulty in attracting multilateral development assistance or foreign direct investment to this sector. It thus seems desirable to promote private participation in the provision of infrastructure–with new funds, skills, technologies and management techniques, as well as continuing funding for maintenance and expansion. The challenge is not just to regulate the private service provider–it is to create an attractive environment for the private investor.

Single-access points for SMEs encourage registration

- ***Improving the business environment***—rules and regulations, property rights, contract enforcement, networking and entrepreneurship. Governments should simplify registration procedures, encourage informal businesses to register, secure property rights, improve contract enforcement, promote a culture of entrepreneurship and encourage networking among SMEs. It is crucial to streamline registration procedures and abolish unnecessary regulations–creating single access points, reducing paperwork and avoiding involvement of courts in the registration process. Securing property rights can reduce costs for businesses and increase efficiency, especially for female entrepreneurs, whose ownership of land is seriously restricted in some countries. Reforming the contract enforcement system must include the following measures: allow cases of dispute to be brought to court without lawyers, reduce written documents, improve information systems and judicial statistics, as well as introduce summary proceedings and other innovative measures to speed court procedures such as random case management.

- ***Reforming the financial sector***—to secure greater access for microentrepreneurs to obtain formal financial and nonfinancial services. African governments should actively encourage credit-constrained borrowers and enterprises to develop institutional structures conducive to microfinance, persuade informal financial groups to acquire appropriate legal status and promote links between semiformal and formal financial institutions.

- ***Reforming the labour market***—to reduce employment costs, ensure greater flexibility and efficiently coordinate the demand and supply of labour. Worker protection laws–in the form of minimum wages or hire-and-fire regulations–should be carefully designed and regularly revised to minimize any negative impact on labour demand in the formal sector. To hold down search costs, governments should create and support job centres for employers to advertise vacancies and for job seekers to find information on potential employment opportunities. The ability of such centres to foster employment hinges crucially on providing accurate labour market statistics as well as necessary training and advisory services.

Maintaining a conducive macroeconomic environment

Increased private investment requires a stable macroeconomic environment characterized by a low and predictable inflation rate, stable real exchange rate, and current account and fiscal balances consistent with low and declining debt and rising real per capita income. For Africa as a whole the inflation rate declined from 23.3 per cent in 1991–2000 to 10.1 per cent in 2001–04, thanks to better macroeconomic management, especially in curbing fiscal deficits and inflationary finance. On average, fiscal deficits declined from 5.2 per cent of GDP in 1993–2000 to 1.68 per cent in 2001–04. The overall current account deficit also fell, from 3.8 per cent of GDP in 1981–90 to 2.0 per cent in 1991–2000 and 1.0 per cent in 2001–02.

Macroeconomic stabilization and reform programmes often involved several rounds of financial sector reform and liberalization. By the mid-1990s many African countries had gradually abolished interest rate fixing and relaxed controls over bank lending. Since then the real rate of interest has been positive, and generally rising across Africa.

Despite the seeming success of reforms, savings and investment rates are still quite low, showing that macroeconomic stabilization alone is not enough to stimulate private investment in Africa. Second-generation reforms are needed for accelerating investment and job creation in the private sector, notably by improving the physical infrastructure and business environment, increasing firms' access to credit and ensuring labour market flexibility. Particular attention should go to enabling SMEs in Africa to grow and compete in a market-oriented environment in which the state and the private sector play complementary roles. These issues are taken up later in the chapter. The focus here is on tax policy.

Savings and investment rates are still quite low

Five firms in six in Sub-Saharan Africa consider the tax system to be one of the chief obstacles to growth (World Bank 2004a). Many African countries have implemented some tax reforms in the last two decades, and tax rates are now broadly comparable to those in other developing countries, though Egypt and the Democratic Republic of Congo have some of the highest marginal corporate tax rates at 40 per cent, well above the norm of about 30 per cent (World Bank 2004b). Further reforms of tax structure, administration and incentive policies are particularly important (Addison and Levin 2005; Tanzi and Zee 2000).

"Narrow tax bases and weak tax administrations force governments in developing countries to collect a larger share of their revenues from firms and commercial transactions than is the case in developed countries" (World Bank, 2004a, p. 107). This is particularly true in Africa. And tax avoidance, tax evasion and the large informal economy not subject to taxation mean lower tax revenues in Africa.

Typically domestic taxes in Africa include a sales tax, a company tax or profit tax on formal firms, a local tax on informal enterprises and sometimes a proportional duty on buildings and equipment. Inefficient and corrupt tax administrations often harm business operations and reduce revenue collection. Firms indicate that tax incentives and rebates are difficult for them to use in practice because of corruption and lengthy procedures or delays by officials to solicit bribes. A common complaint by firms is inconsistency and nontransparency of methods of assessing sales and profit taxes (World Bank 2004a; Eifert and Ramachandran 2004).

To compensate for revenue shortages due to large informal economies and narrow tax bases, tax systems in Africa often have many taxes with different rates. This makes it difficult for firms to understand the tax system and weakens the tax administration. Furthermore, some countries lack coordination between central and local tax authorities, increasing the resistance of firms and individuals to pay (Eifert and Ramachandran 2004). The many different tax rates obstruct market forces, distort resource allocation and create inefficiencies.

Indeed, complicated tax structures, together with corruption and long and complicated procedures, raise the cost of complying with tax regulations, particularly for small businesses. This high compliance cost is a reason for many small firms to remain in the informal sector. Complex tax systems with numerous exemptions and special rules are also costly for the government to administer–and susceptible to malpractice (box 7.1). It is common for governments in Africa to offer tax holidays and distortionary tax exemptions and other incentives to attract foreign firms. But the tax holidays are not always effective in achieving their objectives and domestic investors who do not receive such benefits find it difficult to compete with foreign firms.

Tax reform in Africa has to be deepened to reduce the tax system's disincentives.

"African economies must deepen fiscal reform"

- Best-practice examples suggest the need for a lower and uniform corporate tax rate—with a maximum marginal rate of no more than 30 per cent and with limited recourse to special incentives (Kheir-El-Din, Fawzy and Refaat 2000). Reforming the tax structure is likely to improve the incentives for firms to comply with the tax system.

Box 7.1
Tax reforms and remaining problems

Ethiopia
The maximum wage and profit tax rates were reduced respectively from 85 per cent and 89 per cent in 1991 to a unified rate of 35 per cent in 2003. But the maximum import tariff rate of 41 per cent in 2002 and 35 per cent in 2003, despite a decline from 230 per cent in 1991, remains high even by developing country standards. The lower import tariff rate was associated with a huge increase in covered items, from 1,621 in 1993 to 5,608 in 2003, and a decrease in exempted items, from 327 in 1993 to 179 in 2003 (Getachew 2004).

Burundi
The tax system lacks certainty, simplicity and transparency. It lacks certainty because the government uses its discretion to determine who imports what, while tariff rates change from one year to the next. It lacks simplicity because of the variety of taxes within each of the two broad border taxes: entry taxes and fiscal taxes. Import duty exemptions amounted to 50 per cent of tariff revenue in 1993, and the undefined category of other exemptions made up 42 per cent of total exemptions in 1996. Prone to abuse and corruption, the tax system lacks transparency (Nkurunziza and Ngaruko 2005).

Egypt
Larger firms in Egypt's free zones are not subject to tax and duty laws and enjoy an unlimited tax holiday. Firms outside the free zones are generally subject to various types of taxes, including property tax, sales tax and custom duties. Small firms, especially those in the informal sector, pay high import duties on capital and intermediate inputs, giving them little incentive to use modern technology or grow. The tax holiday programme is largely ineffective (El Samalouty 1999).

- Simplifying and developing a more efficient tax system is one key to reducing the cost of doing business, increasing product supply responsiveness and enhancing employment (Fosu 2004).
- To enhance competition, especially between domestic and foreign firms, tax holidays should be reduced to a minimum, confined to projects that meet export or employment targets.
- Wide-ranging reform of the tax administration with the involvement of the private sector would build mutual trust and increase tax awareness and efficiency.

Poor physical infrastructure hobbles private sector development

Sub-Saharan Africa has weaker infrastructure than other developing regions (figure 7.1).[1] Physical infrastructure—such as roads, railroads, energy supplies and telecommunication—is crucial for the private sector. Without good roads providing access to the markets of larger towns, enterprises in rural areas have only limited market access, constraining the growth of the private sector.

Figure 7.1
Infrastructure in Sub-Saharan Africa is weaker than in other developing regions

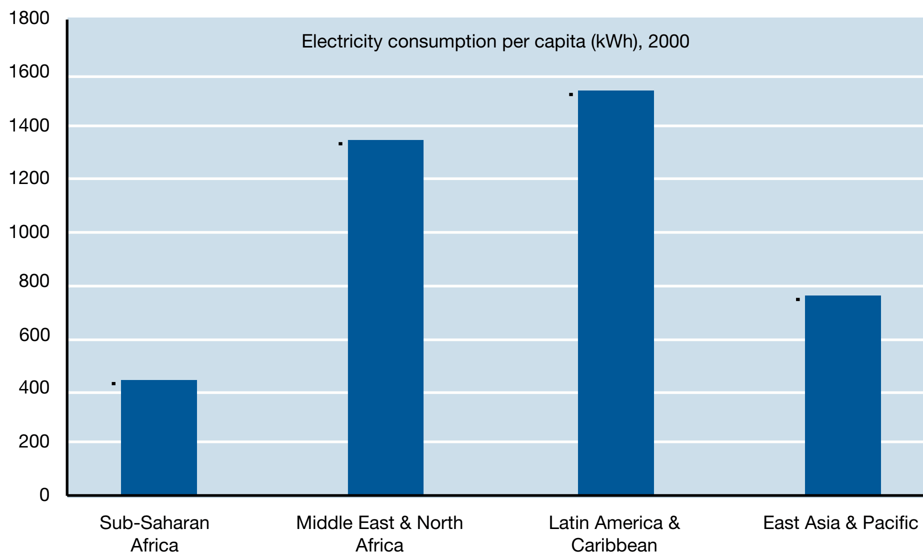
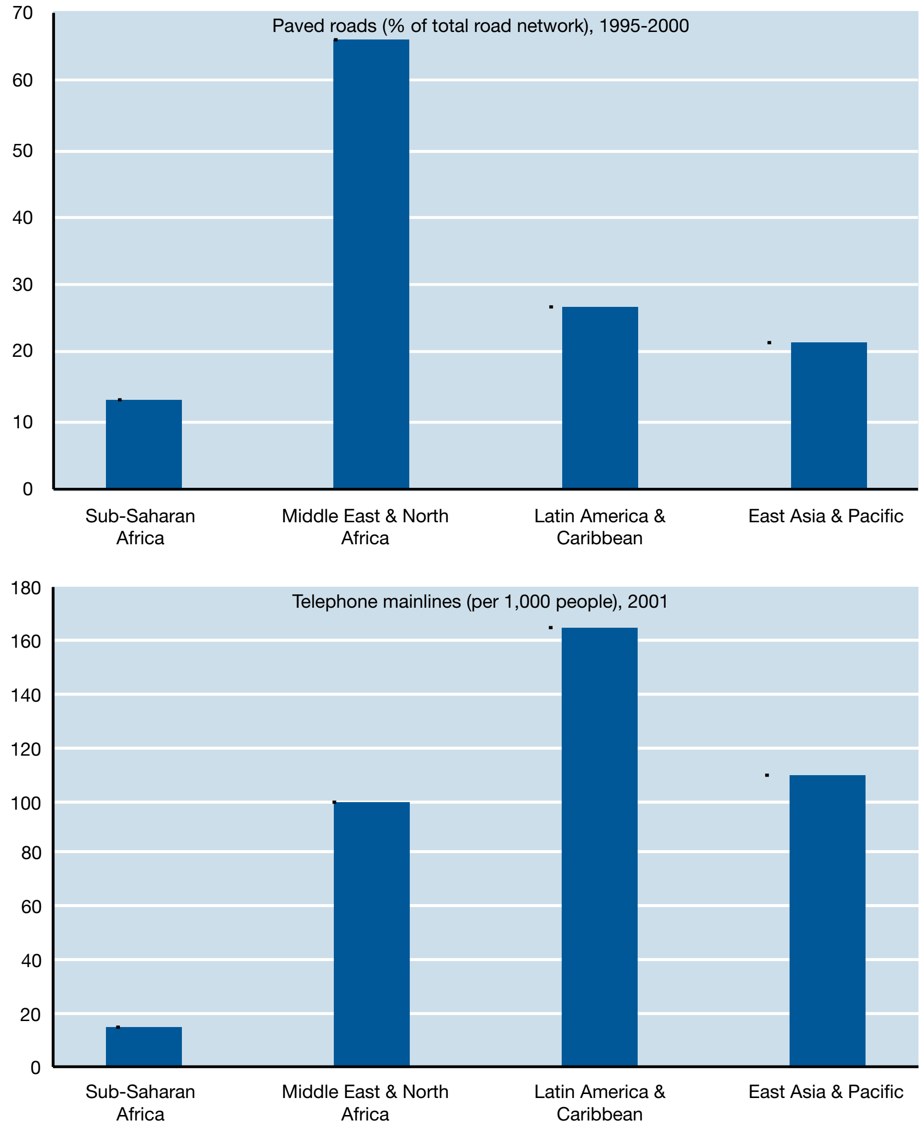


Figure 7.1 *(continued)*



Only 12 per cent of Sub-Saharan Africa's roads are paved

Source: *UNECA 2004a.*

High transport cost discourages the private sector

Poor transport infrastructure accounts for 40 per cent of the cost of transport on average and 60 per cent in landlocked countries (World Bank 2005). Landlocked countries also depend on the infrastructure in transit countries, often vulnerable to political instability countries (Faye and others 2004)

Road density in Africa is estimated at 6.8 kilometres per 100 square kilometres, far below Latin America's 12 and Asia's 18. The road network distribution is very low, at 2.7 kilometres per 10,000 people, resulting in poor accessibility, infrequent service and high transport costs (UNECA 2004a). The freight cost as a percentage of total import value was 13.0 per cent for Africa, 8.8 per cent for developing countries on average and 5.2 per cent for industrial countries (figure 7.2).

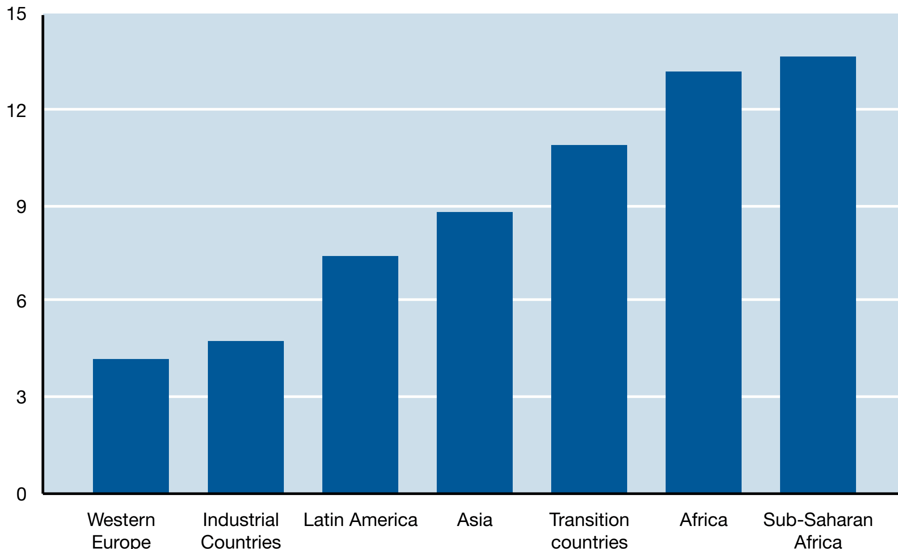
Unreliable energy supply is an obstacle for firms

The poor energy services in most of Sub-Saharan Africa hurt the level and efficiency of private sector investment and lead to much higher production costs than in other parts of the world. For example, a 1999 survey of firms in Senegal cited power failures, transport costs and other infrastructure problems among the top operational problems. Three of the largest companies assessed the costs of power outages (electric generators, operating costs, lost production and deteriorated material) at about 10 per cent of sales. A similar study by the World Bank's regional programme on Enterprise Development in Madagascar in 2002 found poor power supplies to be a major burden on enterprise development (UNECA 2004a).

- In Uganda a survey of 243 firms conducted in 1998 showed that they did not receive electricity from the public grid for 89 operating days a year, on average.

Figure 7.2

Transport costs world regional and country groupings, 2000 (freight cost as a percentage of total import value)



Note: The transport cost rate is the ratio of transport costs as a percentage of the value of imports.

Source: UNECA 2004a.

That led 77 per cent of large firms (in addition to 44 per cent of medium-size and 16 per cent of small firms) to purchase generators, which represented 25 per cent of their total investment in equipment and machinery (Reinikka and Svensson 1999).

- In Malawi and Tanzania firms that bought generators to compensate for the faulty public power supply have been affected by high fuel costs (Privatisation Commission of Malawi 2000; Confederation of Tanzania Industries 2002).

- In Ghana as many as 75 per cent of exporters surveyed said that they had suffered financial losses from power fluctuations (Edjekumhene and Brew-Hammond 2001).

Small firms are the hardest hit by inefficient power services. Public utilities provide most electric power in Sub-Saharan Africa—inefficiently, at high cost and with a low degree of reliability. A study of Nigerian firms found that small firms cannot afford to make costly capital investments to meet their power needs (Lee and Anas 1992). Unreliable power thus slows the growth of small firms and their capacity to generate income.

Public-private partnerships can improve infrastructure

Infrastructure development in Africa has been constrained by a lack of public resources, and by the difficulty in attracting multilateral development assistance or foreign direct investment to this sector. It thus seems desirable to promote private participation in the provision of infrastructure—with new funds, skills, technologies and management techniques, as well as continuing funding for maintenance and expansion. The challenge is not just to regulate the private service provider—it is to create an attractive environment for the private investor.

"Private sharing in infrastructure development is halting"

Infrastructure investors have often been disappointed by low returns in developing countries, and investment in private infrastructure projects in developing countries has declined in the last few years (World Bank 2005). Promoting public-private partnerships in infrastructure has to go hand-in-hand with creating a more favourable business environment. Many governments still perceive infrastructure as strategic and do not allow private participation. Where private participation in infrastructure is prohibited by law, legislation has to be changed accordingly. In other countries it is important to change regulations governing the private sector to make private investment in infrastructure more attractive. Insecure property rights and the high costs of regulation, taxation and corruption are major concerns.

Telecommunication and information and communication technology facilitate private businesses

Poor telephone lines still constrain private sector development in Africa, the region with the lowest density of telephone lines and the fewest Internet users. Only one person of 160 people uses the Internet (African Internet Infrastructure Information 2002). Busi-

nesses in Madagascar often have several telephone lines in the hope that one of them will function (Integrated Framework for Trade-Related Technical Assistance to Least Developed Countries 2003). In Bangladesh, China, Ethiopia and India the World Bank's Investment Climate Surveys found that garment manufacturers are more productive, pay higher wages and grow more quickly when telecommunications services are better (World Bank 2005).

Mobile phones can amplify access to telecommunication. The telephone ladies of Bangladesh show how mobile phones can improve access to telecommunication quickly and form a business opportunity at the same time (box 7.2).

Box 7.2
The telephone ladies of Bangladesh

Grameen Bank, a pioneer in microfinance, initiated the Village Phone project in 1997, giving loans to women in distant villages to buy mobile phones. The women then sold telecommunication services to others. Rural areas proved the perfect setting for such a business, because fixed telephone lines do not exist in many villages, and if they do, they are individually owned and not for community use.

The Village Phone project quickly became popular and successful. Mobile phones became a fast way for village ladies to earn an income. Today 60,000 "telephone ladies" supply telephone service in 80 per cent of the villages in Bangladesh.

Source: *Kumar 2004.*

Internet use and exports are positively correlated in developing countries (Clarke and Wallsten 2004). To improve access to the Internet, the network of fixed telephone lines has to be improved in quality and quantity. The African countries with better infrastructure, such as those in North Africa and some in Southern Africa will have larger populations of Internet users. But Senegal and Cape Verde have much higher levels of connectivity than their GDP per capita would suggest. Internet use may be impeded or enhanced by government policy.

Improving the institutional environment

Despite government efforts to improve the business environment in many African countries, more reforms are still needed in many important areas (box 7.3).

In most African countries doing business is constrained by overregulation that leads to high transaction costs to deal with the bureaucracy. High transaction costs, in turn, reduce the productivity of a business and can generally discourage private sector activity.

Box 7.3

Ethiopia's business climate: initial reform success but more needs to be done

UNECA conducted a survey of 36 SMEs in 2004 in the formal sector in Addis Ababa to probe their perceptions of the business environment. Of the businesses surveyed, 80.5 per cent indicated having problems: 31 per cent with the level of taxes, VAT and custom duties, 24 per cent with the bureaucracy and 17 per cent with the high cost of rent and utilities (especially electricity), inadequate infrastructure or the lack of land ownership. For 28 per cent, rent-seeking threatens their activities.

All the businesses were registered, and for 61 per cent of them the registration process took less than a month. The government simplified the registration process in 2003, and five of the firms interviewed reported to have completed the registration process in one day in 2004. About 20 per cent of the businesses operated informally before registering, for a period ranging in most cases from 15 days to a year.

Most firms perceive contract enforcement through the legal system as inefficient and costly. For this reason, 81 per cent of the businesses that encountered contract enforcement problems prefer to resolve disputes informally. Most of them consider a legal follow-up as unpromising. To avoid contract failures, they generally prefer a careful assessment of the business partner. Nine of the businesses have taken a case to court, but three dropped their cases due to the inefficiency of the courts.

"Business is constrained by overregulation"

Only half the businesses belong to a business association, only three to the Chamber of Commerce. Most consider their membership as beneficial to their business, mentioning networking, sharing information and basic resources, finding business opportunities or voicing common problems to the government.

Of all the businesses, 67 per cent had resorted to loans, of which 54 per cent used solely the formal financial sector, 21 per cent used both informal and formal loans, while 17 per cent relied entirely on the informal credit system. Five businesses cited financial sector constraints, such as the need for collateral, as the primary reason for declining to procure a loan.

The formal labour market was unexpectedly important for firms. Only four of the businesses rely entirely on family labour. When hiring, 42 per cent of the businesses rely on the advertisement system (board or newspaper advertising), 28 per cent use only informal channels, and 25 per cent resort to both formal and informal channels.

Businesses expressed the need for reform in the legal system to facilitate contract enforcement, for a better coordination within the bureaucracy and for combating corruption. They also mentioned reforming land policy and the banking sector, to improve access to small loans.

Source: UNECA staff.

Difficulty of registering a business a severe constraint for small firms

Company registration is the first step to formalize a business and enhances the ability of firms to obtain finance, enforce contracts and receive benefits from the state, such as financial support or low cost land and other services. Company registration should be an administrative act and not a major hurdle.

Table 7.1
Starting a business

Region or economy	Procedures (number)	Duration (days)	Cost (% of GN per capita)
East Asia and Pacific	8	52	48.3
Europe and Central Asia	9	42	15.5
Latin America and Caribbean	11	70	60.4
Middle East and North Africa	10	39	51.2
High-income OECD	6	25	8.0
South Asia	9	46	45.4
Sub-Saharan Africa	11	63	225.2

Source: *World Bank 2004a.*

"Lengthy registration and licensing procedures obstruct business"

In most African countries registration and licensing are serious obstacles to formalizing a business, and 7 of them are among the world's 10 most difficult countries to register a business. The registration cost in Africa far exceeds that in all other regions, and the number of procedures and the registration time are among the highest in the world, with Angola, Chad, the Democratic Republic of Congo, Togo and Guinea the most difficult for formalizing a business (table 7.1 and figure 7.3).

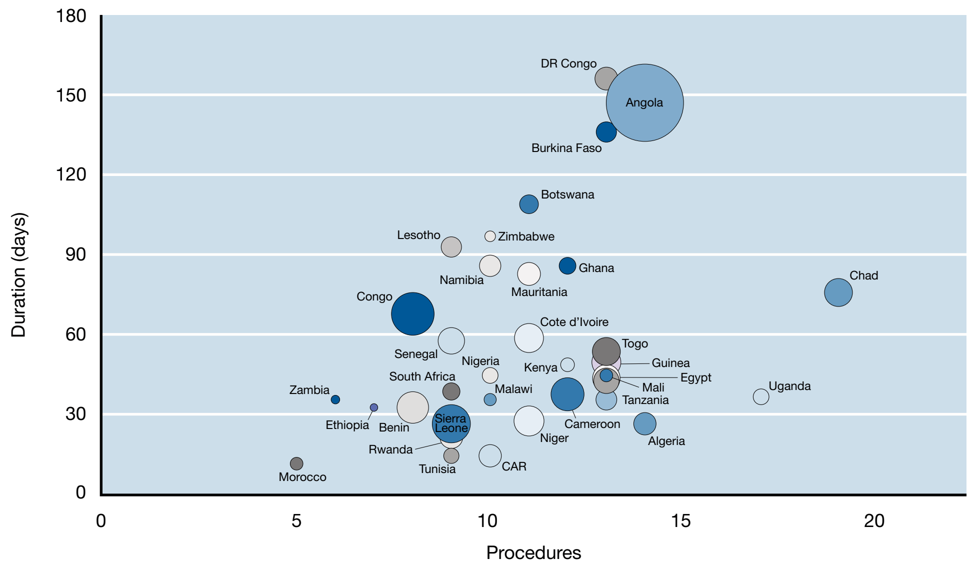
Africa also has positive examples, even world benchmarks, with Morocco, Ethiopia, Zambia and Tunisia performing better than many dynamic Asian or Latin American countries. For example, in India the registration process takes 89 days and costs $265. In Vietnam it takes 56 days, close to the African average of 59 days. Morocco is the best in Africa, with five procedures to register a business, a duration of 11 days and a cost of $195. In Tunisia the process needs 9 procedures and 14 days and costs $277.24.

In absolute terms the registration costs in all African countries are higher than those in countries with GDP per capita many times those of Africa. In Denmark a business can be registered with no fees, and in New Zealand, the world's second most efficient system, the cost is $39. In Africa the average cost of registering a business is $785, with Ethiopia the lowest at $74 and Angola the highest at $6,621 (World Bank 2004a).

The nature of procedures in Chad, the country with the most procedures in Africa, differs greatly from that in Morocco, the country with the lowest number (table 7.2). And the total cost in Chad is more than four times that in Morocco, not even counting the opportunity cost.

Figure 7.3

Registering a business in Africa: number of procedures, duration and cost



Note: The bubble size reflects the absolute cost in dollars.

Source: World Bank 2004a.

It's easiest to register a company in Morocco

Simplifying business registration

Worldwide differences in registration procedures show that the registration process need not entail high costs or long durations. Ethiopia shows what can be done with simple measures. In 2003 the cost of registering a business was reduced by 80 per cent simply by abolishing the requirement to publish notices in two newspapers. The requirement to publish notices in a journal or newspaper takes 90 days in Angola and accounts for 52 per cent of the total cost in Egypt. The countries with the easiest registration procedures—such as Morocco, Ethiopia, Zambia and South Africa—do not require the publication of a notice (World Bank 2004a).

The most efficient way to reduce the number of registration procedures is to create single-access points. In some countries nominating an existing agency to be the single point and bringing together representatives of various other agencies works well, as for Kenya since 2003. Front-line officials should speak the first language of the people they serve, removing a constraint for many informal businesses to deal with bureaucracy. Morocco has a one-stop shop, reducing the number of registration procedures to five. Reform experience in Mozambique that includes the introduction of a one-stop shop is illustrated in box 7.4.

Box 7.4

Improving the institutional set up for Mozambique's SMEs

The public sector environment in Mozambique was characterized by inefficiency, lack of transparency and corruption, particularly in such potentially dynamic economic areas as trade and tourism.

The provincial governments of Zambezia and Inhambane launched two initiatives in 2001, the Balcão Único and the Loja de Negócios, to streamline licensing and setting up commercial enterprises.

Both initiatives are meant to increase transparency and efficiency. A one-stop shop directly under the governors' offices informs clients about necessary forms, licences, fees and regulations. It also forwards completed proposals to the responsible municipalities, provincial directorates or, if required, national ministries.

The civil servants' understanding of the requirements and administrative structures has improved significantly in the course of a year. The average time to register and start a business has significantly been reduced, and allegations of corruption and gross negligence have diminished.

But some administrative barriers and a general lack of an entrepreneurial-friendly attitude and professional commitment have not yet disappeared. Many civil servants and investors still do not have a full understanding of the legislation, especially crucial laws governing land tenure and title rights. A serious constraint is the prevailing perception of many provincial directors that the new institutions would reduce their influence, responsibility and income opportunities. Further improvements need a strong commitment from all stakeholders.

Source: *Johannsen n.d.*

Standardization of paperwork further simplifies the procedure. With standard forms the entrepreneur does not need legal services to fill in the forms. Moreover, it is easier for employees to process documents.

Involvement of courts in the registration process makes the procedure costly and long. In Guinea, for example, the execution of the notary covers 74 per cent of the total cost of registration, and takes at least 12 days. Notaries usually perform a simple verification service that could be done elsewhere. The African countries where business registration is easiest do not involve courts in the registration process.

Table 7.2
Registering a business in Chad and Morocco, 2004

Procedure	Procedures (numbers)	Duration (days)	Cost (dollars)
Chad			
Deposit the legally required initial capital in a bank	1	1	0
Check the uniqueness of the company name	2	1	0
Notarize the company deeds	3	4	559.55
Obtain criminal record for directors	4	2	23.98
Procurement of a medical certificate	5	1	19.98
Register by-laws with the Ministry of Finance	6	2	0
Get an authorization from the Ministry of Industry and Commerce	7	4	28.78
Registration with the Commercial Registry	8	3	88.05
Register with the court	9	2	0
Publication in a legal journal	10	3	71.94
Register for tax	11	1	0
Inscription on the tax rolls	12	3	0
Register for the statistics code	13	3	0
Notification to the Ministry of Labour	14	1	0
Submission of the Internal Regulation Code to the Labour Inspector	15	30	0
Registration with Municipality of Asucion	16	2	90.00
Register for social security	17	2	0
Court authorization of commercial books	18	3	0
Make a company seal	19	7	28.78
Total	19	75	$911.06
Morocco			
Certificat negative	1	1	17.14
Deposit capital at a bank	2	1	0
Legalize statutes at Mayor's office	3	1	24.00
Register at the one-stop shop	4	7	154.29
File a declaration to labour inspector	5	1	0
Total	5	11	$195.43

Source: *World Bank 2004a.*

Corruption hampers small enterprises

Bribes add a substantial cost to doing business, and having to pay bribes to speed up a process is equivalent to imposing a tax. About 70 per cent of the firms interviewed for the World Bank Investment Climate Surveys see corruption as an obstacle to the growth and operation of their business (Hallward-Driemeier and Stewart 2004). According to a study of Ugandan firms, corruption reduces the short-term growth of firms, with an effect much greater than that of taxation (Fisman and Svensson 2002). Firms there pay an estimated average of $8,300 a year in bribes, roughly 8 per cent of their total costs. In Algeria and

Kenya 75 per cent of the firms surveyed reported that they paid a bribe, averaging more than 5 per cent of sales in Kenya (Reinikka and Svensson 1999; Svensson 2003).

Small enterprises are affected more by corruption than are large enterprises, which often have specialized departments to deal with aggressive bureaucrats and have individuals that have acquired special skills on how to cope with the large number of regulations. Large enterprises can also use their political power to influence people in the public administration or pursue rent-seeking activities to obtain benefits not available to others (Tanzi 1998).

Overregulation is commonly cited as one of the major causes of corruption: in an overregulated state procedures take too long, so individuals bribe bureaucrats to speed up the process. Overregulation is positively correlated with a larger unofficial economy and with a larger incidence of corruption (Svensson 2003; Djankov and others 2001). However, 70 per cent of the firms in Zambia and 40 per cent of firms in Uganda report that the problem is not always the regulation, but the interpretation, often perceived as unpredictable (Hallward-Driemeier and Stewart 2004). So regulations lead to corruption when they are not transparent and are open for arbitrary interpretation. The argument that bribes are an efficient way to deal with extreme red tape (Campos, Lien and Pradhan 1999; Khan 2002) is not helpful in fighting corruption.

Corruption is generally connected with the activities of the state and especially with the monopoly and discretionary power of the state. But it is not the size of the public sector that generates corruption. It is the way the state operates and carries out its functions. Tackling corruption thus requires reforming bureaucracy, paying decent salaries, creating credible institutions to prosecute corrupt activities and raising awareness that corruption undermines the system (Collier 2000).

“Raising the stakes can help hinder corruption”

Simplifying the registration process and reducing regulation would reduce the incidence of corruption, especially for SMEs. Regulations with fiscal implications should be replaced, when necessary, with more credible and reliable taxing and spending policies, and tax incentives with nontransparent approval procedures should be minimized (Tanzi 1998).

Increasing the risk of punishment is important in combating corruption. Since the two corrupt parties are unlikely to report the case, the probability of detection is relatively low, so it is necessary to create institutions that make corruption visible (Collier 2000). Establishing citizen watchdog groups has been successful in fighting corruption in Paraguay, once perceived as the most corrupt country in Latin America. The network of watchdog groups quickly expanded to 25. With their help in providing evidence on corrupt activities, bureaucrats were arrested and prosecuted (USAID n.d.).

Since corruption has two sides, blacklisting firms offering bribes can be another robust measure. Blacklisting worked in a large World Bank dam project in Lesotho in 2004. Uganda also started blacklisting corrupt firms and sales staff. Blacklisting and stigmatizing may also improve the general attitude towards corruption.

Security of property rights encourages the private sector

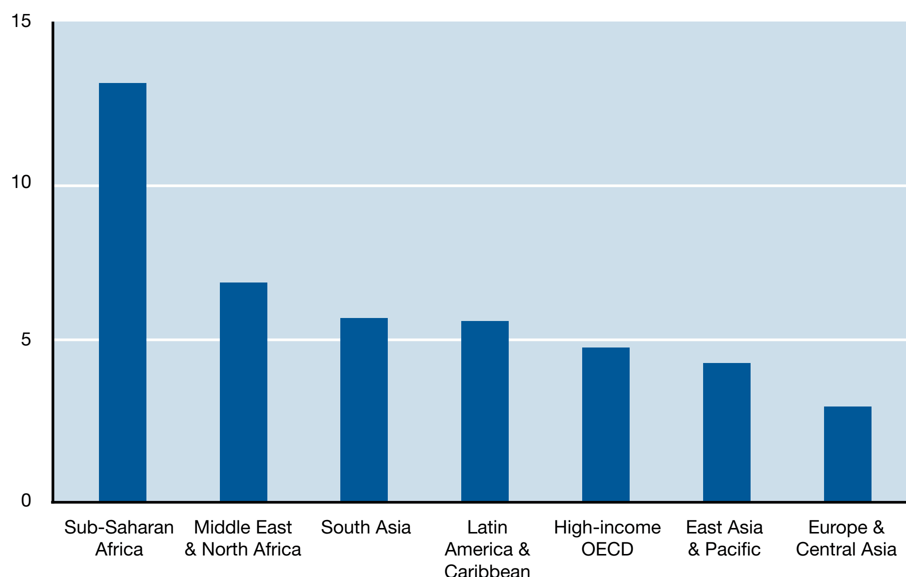
The way property rights are defined and enforced affects the efficiency of resource use and the levels and types of investments. For example, a firm that has acquired the right to establish a plant on a piece of land, and has the private ownership of a machine, still needs access to water, electricity and the labour of others to realize the full potential of these resources.

Security of property rights is one of the features most cited for promoting investment. Insecurity discourages investment because investors live in the fear of confiscation, fraud or theft. When the risk of expropriation is high, businesses are reluctant to invest in fixed assets, preferring activities that can be easily moved, do not depend on a certain location and do not require costly and heavy machinery. This hurts resource allocation because entrepreneurs choose not the most economically attractive type of activities but the activity with the least risk of expropriation (Saleh 2004).

To secure property rights, the registration of property, still a long process in many African countries, needs to be facilitated. In Ghana, Rwanda, Côte d'Ivoire, Angola, Nigeria, Togo and Egypt, it takes more than six months to register a property, with Ghana the longest at 382 days (World Bank 2004a). The average cost to register a property in Africa far exceeds the average in other regions, while the number of procedures is in line with other regions (figure 7.4). Most African countries have to revise their bureaucratic fees, which seem excessive. But, in three African countries (South Africa, Namibia and Mozambique), however,

Figure 7.4

Cost to register property (% of average value of property to be registered)



Source: *Doing Business 2005 database, World Bank.*

property registration is even faster than the Organisation for Economic Co-operation and Development (OECD) average.[2] Africa can therefore learn from best-practice examples on the continent (World Bank 2004a).

Secure property rights can significantly reduce costs for a business. The ability to use property as collateral is usually a requirement for credit, and without land titles the search for collateral becomes difficult. Formal property titles lower the cost to lenders of determining the creditworthiness of borrowers. Many countries still do not allow land ownership for foreigners, discouraging foreign direct investment. Protection of property rights also means that the state has to take effective measures to prosecute and punish theft of property rights. The transferability of property is also important. Individuals must be able to acquire property rights through sale or any other legal means. If land titles cannot be transferred, their use for collateral is limited, because the bank could not take over the land in case of default.

Women are particularly affected by insecure property rights. In many countries women's land ownership is severely restricted. In Ethiopia the legal framework has improved this, but men still consider their wife's property as common property, and banks expect the husband to sign a loan agreement with his wife, especially when collateral is needed.

Difficulties in contract enforcement hamper business activity

Contracts are of value only if they can be properly enforced. If contract enforcement is not possible, businesses will be reluctant to enter a contract with businesses they do not know, reducing the scope of economic activities. They will operate only on a cash-and-carry basis—or even ask for advance payment. Improving contract enforcement is therefore crucial to encourage private sector activity.

Enforcing contracts in Sub-Saharan Africa is among the most difficult in the world, with an average of 35 procedures and 434 days required to enforce a contract. In South Asia, where contract enforcement is easiest among the developing regions, it requires only 29 procedures and 375 days (table 7.3).

"Positively, Tunisia leads the world in contract enforcement"

Table 7.3
Contract enforcement in regional comparison

Region or economy	Procedures (number)	Time (days)	Cost (% of debt)
East Asia and Pacific	27	325	87.5
Europe and Central Asia	29	412	17.6
Latin America and the Caribbean	35	463	23.3
Middle East and North Africa	38	437	17.9
High-income OECD	19	229	10.7
South Asia	29	375	39.7
Sub-Saharan Africa	35	434	42.9

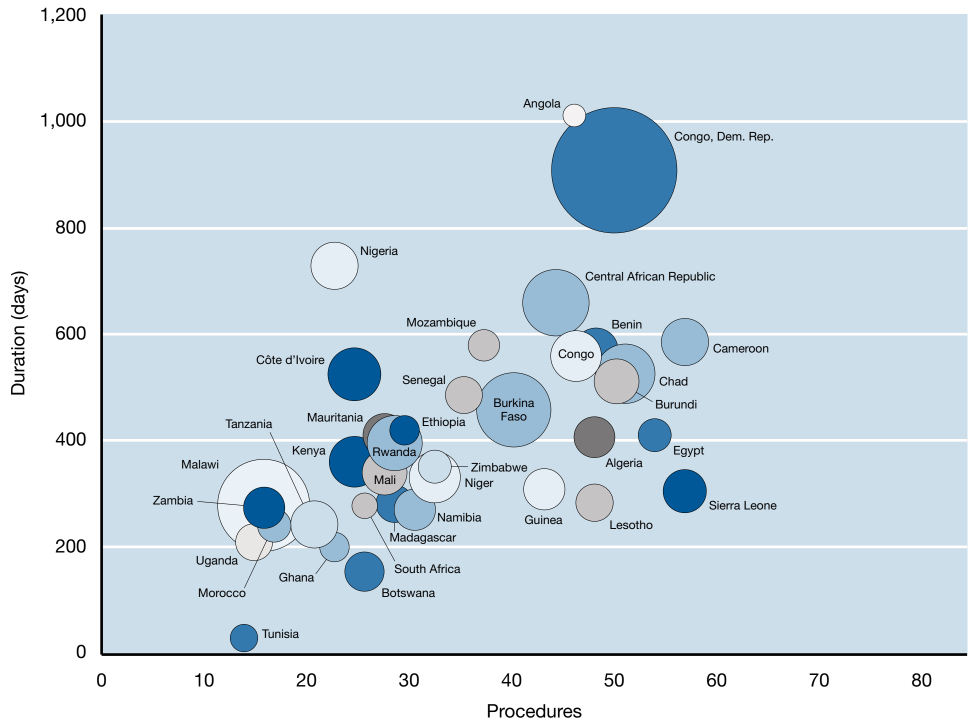
***Source:** Doing Business 2005 database, World Bank.*

After reform, Tunisia has become the world's best-practice example with 27 days to enforce a contract, the fastest worldwide. In the second fastest country worldwide, the Netherlands, it takes 48 days. In some other African countries contract enforcement takes so long and is so costly that many firms do not consider it worthwhile to even start the procedure (World Bank 2004a). In 18 African countries contract enforcement takes more than a year (figure 7.5).

> *Mandatory legal aid can slow-down cases*

Figure 7.5

Difficulty of contract enforcement: number of procedures, days to enforce and cost



***Note:** Cost is reflected by bubble size.*

***Source:** Doing Business 2005 database, World Bank.*

The first reform step is to review the legal system to identify the bottlenecks. In some countries the filing process is extremely long. For example, in the Democratic Republic of Congo it takes 245 days (or 33 per cent of the time of the total procedure) before the case comes to the judge. In Angola, however, cases come to the judge fairly quickly (86 days) but judgement is extremely slow (484 days).

Best-practice examples and prominent reform experiences reveal that successful reform must include the following measures (World Bank 2004a):

- ***Bring the case to court without lawyers***. Abolishing mandatory legal assistance and the requirement that the complaint must be legally justified would facilitate the process significantly and reduce the cost. In Tunisia the creditor files a claim in court, and the court issues a summon to the debtor without a requirement to appoint a lawyer.

- ***Reduce written documents***. Introducing new oral procedures can reduce the average time of cases significantly. In countries with a high illiteracy rate, still the case in Africa, oral procedures would give a stronger sense of fairness to many plaintiffs.

- ***Information systems and judicial statistics.*** The lack of reliable information systems and workflow statistics in many courts limits the ability of judicial reformers to identify bottlenecks and hinders the monitoring of progress in a case. An electronic system of recording and following up on cases from the time they are filed to the time judgement is issued would contribute to settling cases. In Mexico such a system revealed that more than 60 per cent of the cases do not go beyond the initial filing of the claim.

- ***Summary proceedings.*** Many countries have introduced summary proceedings for small debts and stricter deadlines for each procedure. Botswana uses an expedited court proceeding that does not require a trial. The creditor can apply for a summary proceeding when the defendant is unable to raise credible opposition to the plaintiff's complaint.

- ***Random case management.*** Random case management can speed the process and reduce corruption. This reform measure was successful in Slovakia, where cases are now sent to whichever judge has the lightest load. This ensures faster service and makes it more difficult to know which judge to go to for a favourable ruling.

Specialized courts are often recommended, but they can be a double-edged sword and are likely to be premature in countries where the judiciary is still developing. To be successful, reforms should go hand-in-hand with the training of judges as currently undertaken in Malawi, Sri Lanka and Uganda.

In countries with a weak judicial system out-of-court resolution mechanisms such as mediation can be a short-term solution. However, this is not desirable in the long run because of the lack of transparency.

Harnessing the power of networks to promote SMEs

Economic interest groups are important in the growth of SMEs because they can help reduce transaction costs. Since SMEs have disadvantages in markets because of their size, they need the support of network contacts, because strategic alliances can

compensate for the lack of scale. In some instances, economic interest groups take the form of clusters of enterprises or services (OECD 2004). Networks can better engage in collective action, which would be too costly for a single firm. So, supporting networks can be more efficient for government and donors than providing assistance to individual enterprises.

Another asset of networks is the common trust among network members. Once built up, it reduces costs because members need less time for careful assessments and contract negotiations and save on the cost of legal assistance. Networks are found to have a strong effect on building trust and on information-sharing among agricultural traders in Benin, Madagascar and Malawi (Fafchamps 2003).

"Small-scale lending is an immediate priority"

Building networks is important for women entrepreneurs. Firm surveys revealed that women have only limited networks, because of their domestic roles and responsibilities paired with constraints on mobility and the possibility of interacting with men. Many male entrepreneurs were employed before they decided to start a business, whereas most women start the business to support the family and did not work previously. Chambers of commerce are often perceived as male-dominated or elitist, not fully meeting the needs of female members. Women's membership in formal business organizations in Africa is so far very low, but they should be encouraged to participate in them (Richardson, Howarth and Finnegan 2004).

Many SMEs in Africa owe their existence to deliberate public policies and institutions that promote and coordinate their activities. These institutions could be much more effective if they did not suffer from persistent underfunding. SME promotion has been successful in Kenya and Tanzania, where policies have been comprehensive enough to address the critical areas of concern to SMEs. In Kenya, for example, the leather goods manufacturing industry was nurtured by the Kenya SME promotional agency (UN-ECA-SA 2005).

Promoting an entrepreneurship culture

To harness the job-creating potential of SMEs, it will be necessary to promote an entrepreneurship culture where starting a business is not a second-best solution to finding employment in the public sector.

Firm surveys in Tanzania, Uganda and Zimbabwe show that the entrepreneurial attitude was the key to successful businesses (Trulsson 1999). Most of these businesses were started because the business owner saw a good business opportunity. In fact, many entrepreneurs descend from an entrepreneurial family. Most mentioned their entrepreneurial attitude and the skills and commitment of their workforce as success factors. Many others mentioned operating in a market niche as an important success factor.

Entrepreneurship can be promoted by incorporating entrepreneurial skills in high school and university curricula. Many universities in industrial countries offer courses in entrepreneurship. For example, the University of Southampton, United Kingdom,

offers a nine-month postgraduate course for graduates wishing to start a business. African universities could offer similar courses. Rhodes University in Grahamstown, South Africa, invites practising entrepreneurs to talk to students, to share their experiences and provide hands-on advice.

Entrepreneurship training also contributes to enterprise development. The United Nations Development Programme launched a project to develop entrepreneurship in the Mexican region of Chiapas, a poor region without a clearly established entrepreneurial class (UNIDO 2004). In the programme 100 entrepreneurs were trained in production, entrepreneurship and marketing. As a result of the training, many businesses moved their operations from the informal to the formal sector and improved their marketing abilities.

Profit-oriented entrepreneurial training has been successful in Malawi, although Malawi has neither an enabling environment for SMEs nor a large enterprising society. Local trainers confirmed that the income they received as trainers was attractive to them. Participants were highly satisfied by the training skills they acquired, and more than half of them increased their profits after the training. This type of training contributes to a better performance of businesses and can improve the entrepreneurial attitude (Bärenz and Rösch 2003).

Getting the financial sector ready for small-scale lending

In most African countries, banks are not ready to lend to SMEs because small-scale loans bear high transaction cost and risk, while the return for the bank is relatively low. Supervisory and capital adequacy requirements often discourage serving small borrowers, who lack conventional forms of collateral. Extensive evidence from Africa confirms that the smaller the firm, the less likely it is to obtain formal loans, whereas a large firm's access to credit depends mainly on expected profit (Bigsten and others 2003). So, promoting small-scale lending is an immediate priority area that requires a number of institutional and policy reforms in the financial sector in Africa. Best-practice examples indicate that key financial sector reforms should include microfinance programmes, flexible collateral systems and credit reporting agencies.

Learning from microfinance strategies to widen SMEs access to credit:

Microfinance institutions have evolved around the world to develop innovative products and mechanisms that overcome the constraints of rigid collateral systems and high lending costs, and broaden access to credit by SMEs and poor people, especially women (box 7.5).

Box 7.5

Microfinance can empower women and reduce poverty

Targeting women enhances the contribution of microfinance to employment creation and poverty reduction for a variety of reasons. First, many women have good business ideas and entrepreneurial skills that are not properly used due to lack of finance and laws that restrict their access to banks. Second, while men keep about 32–50 per cent of their salaries and contribute the rest to collective household funds, women contribute everything. Empowering women through microfinance improves family well-being, especially female health and education. Third, through microfinance women gain social respect, self-esteem, physical mobility and greater economic independence and security. In many countries reducing the gender bias contributes to faster economic growth, better governance and higher standards of living.

Attempts to empower women through microfinance often increase the pressure and work loads for women and lead husbands to withdraw some support to the household. But evidence from 62 microfinance institutions worldwide strongly demonstrates that the benefits of women empowerment far exceed costs.

Using microfinance programs to empower women and reduce poverty is conducive to the growth and sustainability of microfinance institutions because women tend to be better borrowers. On average, delinquency and default rates are far lower for female microfinance clients than male ones. Policymakers should thus pay special attention to legal and institutional reforms for promoting women's microenterprises and microcredit services.

Source: *Cheston and Kuhn 2002.*

"The benefits of empowering women far exceed the costs"

Experiences of microfinance in Africa and the policy lessons

Extensive evidence from Africa shows that these institutions complement the banking sector in extending financial services to poor people and draw from traditional community-based methods of financial services in the continent (Basu, Blavy and Yulek 2004; Hirschland 2003; Elhiraika 1999). The evidence highlights many features of microfinance institutions that can have important policy implications.

First, savings by poor people can exceed demand for credit. Microfinance institutions in Africa mobilize more savings in rural areas than banks: they do not require high opening and minimum account balances, they lower the cost of depositing and withdrawing funds by customers by locating closer to them and they simplify procedures to make operations easy for clients to understand. Poor people view safe and liquid savings facilities as a means to smooth consumption throughout the year as well as an insurance against income shocks.

Second, many microfinance institutions in Africa successfully rely on group-based saving and loan schemes that increase access to loans by group members because their combined savings serve as collateral against loans and reduce transaction costs and default

rates that enables them to develop into less constrained and more competitive intermediaries. Individual saving and lending programmes become more important as the industry matures because group-lending schemes might be restrictive and overly risk-averse with only the safest groups of borrowers and projects qualify for finance (Basu, Blavy and Yulek 2004).

Third, the formalization of traditional techniques of saving and lending and the use of innovative strategies enables microfinance institutions in some African countries (Benin and Swaziland) to be self-sustainable (Basu, Blavy and Yulek 2004; Elhiraika 1999). In Ghana and Guinea microfinance institutions' performance has also improved through greater commercial orientation, better loan management and improved financial reporting (Basu, Blavy and Yulek 2004).

Fourth, the evolution of microfinance in Africa appears to have accelerated financial and economic integration. Indeed, formal and informal microfinance institutions are becoming more linked with formal financial institutions in some African countries (Schoombee 1998). While banks serve government and customers in the formal private sector, microfinance institutions concentrate on rural households, poor small borrowers and SMEs. Thus, banks and microfinance institutions in these countries play complementary roles in the financial sector. Microfinance institutions benefit from links with banks in safekeeping for deposits, liquidity management and use of excess savings. They can even obtain loans from banks to cover short-term liquidity crunches, with their assets (loans) serving as collateral (Elhiraika 1999).

Governments should build institutional capacity to get the financial sector ready to serve small borrowers and SMEs (Hallberg 2000). To do so, the authorities should:

- Develop a comprehensive policy framework that provides a legal and regulatory environment as well as capacity building for microfinance institutions to register, achieve self-sustainability and upgrade their services to compete in the modern financial sector. The framework for promoting microfinance institutions should be based on deposit mobilization, adequate capitalization, incentive-compatible governance and independence from government ministries and political pressure that induce rent-seeking and restrict interest rates.

- Discourage providing direct financial support from government, nongovernmental organizations and donors that can impair the ability of microfinance institutions to achieve both outreach and self-sustainability. If necessary, direct government or donor assistance should be well targeted and given through a central agency or apex institution in a way that helps microfinance institutions meet short-term financing needs without impairing innovation and efforts to attain self-sustainability in the long run.

- Ensure that the microfinance institutions' regulatory framework is flexible enough to accommodate the needs of different microfinance institutions and avoid over regulation, which can stifle competition and make it costly for them to deliver low-cost services to clients.[3]

- Ensure that supervisory institutions and personnel are adequately trained and have the competence to supervise and monitor microfinance institutions effectively.

- Define the activities that microfinance institutions can do initially and the capacity needed for them to expand the range of these activities before they become full-fledged financial intermediaries.

- Support capacity building through training microfinance institutions' employees on bookkeeping and reporting standards, strengthening internal controls and lending mechanisms and increasing the use of technology.

Reforming collateral requirements

Collateral-based lending excludes many potential entrepreneurs from obtaining loans, especially start-ups because only a few fixed assets are considered as credible forms of collateral. To prepare the financial sector in developing countries for increased lending to SMEs, it is necessary to reform the collateral system to allow a larger range of collateral, such as movable items and even non-collateral-based lending (World Bank 2002). This requires a reform of banking regulations, a more prudent credit appraisal procedure, and reform of enforcement mechanisms and property rights besides building institutions to create mutual trust.

A recent survey suggests that to instigate a pro-poor reform of the collateral system, the authorities must take three steps (World Bank 2002). First, determine the assets owned by poor people that can serve as collateral, and develop the necessary legal framework to support their application. Second, establish priority of claims over pledged assets through public or private registries that are easily accessible without prohibitive charges. Third, educate judges on collateral law and priority of claims to make ruling easy and more predictable. The law should make it easy for lenders to seize and sell collateral in the case of default without court ruling if there is no dispute between lenders and borrowers.

"Collateral-based lending limits private sector development"

Credit registries for creating mutual trust

Out of a sample of 27 African countries, only 10 countries had public credit registries, and only 3 (Botswana, Namibia and South Africa) had private credit registries (World Bank 2004a). So the potential influence of credit registries in expanding access to credit by poor people and SMEs has yet to be properly explored in Africa. In addition to collecting information on the cash flows of a borrower's bank account or business over a certain period of time, banks rely on collateral to secure loan repayment. They also design incentives and monitoring procedures to reduce default. The creation of credit registries[4] or credit reporting agencies can reduce the information cost as well as the need for collateral.

Policymakers and other stakeholders in Africa should seriously consider the establishment of credit registries as a means of expanding SMEs' access to finance. The demand for credit registries increases with the size of the market for credit and the heterogeneity of customers. In brief, for those lenders who are willing to pay subscription fees, credit registries

can equalize access to information, raise competition and lower credit cost. Borrowers are also made more mobile and can obtain loans from more sources than before. This signifies that credit registries and information sharing can be helpful for both lenders and borrowers. Indeed, 43 Latin American banks consider information provided by credit registries as more important than collateral or the financial standing of the borrower or his history with the bank (Miller 2000).

Preparing labour markets for the job boost

Labour markets in Africa suffer from market failures. First, institutions to coordinate labour demand and supply are limited. Many job-seekers are not informed about vacancies in the private sector and therefore do not search for them. Second, the state often feels the need to intervene in the labour market to protect workers. Although labour protection is important, it may not fulfil its purpose if overprotection of labour discourages employment in the private sector, which is the case for several African countries.

Creating effective job centres with links to training institutions

Informal mechanisms, such as family or friends, are the most common ways for coordinating labour demand and supply in Africa. Consequently, the private sector is not always able to attract the most qualified and most suitable staff, while qualified people do not find an adequate job if they lack the necessary network contacts. This underlines the need for state intervention to establish job centres where jobs can be advertised and job-seekers can find information on vacancies.

In many countries the public sector is the preferred field for university graduates. Evidence from Ethiopia and Tunisia, for example, has shown that university graduates are prepared to wait a long time in the job queue to obtain a public sector job, rather than seek a job in the private sector (Adenikinju and Oyeranti 2000). Governments often indirectly encourage this attitude by taking over the role of the employer of the last resort. The Moroccan government created additional civil service posts in the last few years to tackle high unemployment, despite its commitment to reduce public spending.

To coordinate labour demand and supply, detailed information is needed on vacancies in the private sector, the nature of skills required, gender, age and qualification profiles. It is also important to improve labour statistics to allow governments to refine their labour market policy, target vulnerable groups and offer training courses to provide the skills needed by the private sector (Kausch and Trommershäuser 2002).

Job centres should take the role not of an administrator but of a job consultant or employment advisor. Staff at job centres have to identify the qualification profiles demanded by the private sector and assist or advise job seekers accordingly. These centres should cooperate closely with training centres to ensure that training provides the right skills. They should also visit firms to actively promote the job-seeker's profile.

Box 7.6

Faith-based organizations acting as a job-placement agency and training centre: the example of South Africa

The South African National Zakah Fund (SANZAF), a Muslim faith-based organization in Durban, originally founded to collect the religious tax and to spend it on pure charity projects, has taken over a more sustainable role. The aim is to get people away from charity in the long-run and to enable them to be self-sufficient. To this end, SANZAF has become a job-placement agency and training centre.

SANZAF cooperates closely with a network of Muslim enterprises in Durban to find jobs, at least on a temporary basis, for unemployed job seekers. Businesses now contact the SANZAF to find workers in a short time almost without transaction costs. The pay is often below average, but it is a chance for long-term unemployed workers to go back to work and move away from charity.

The organization also has a small craft shop where men and women can learn the profession of a carpenter or a tailor. With these skills they might be able to open a small business on their own.

The organization also provides training on how to apply for a job, perform in job interviews and go to work on time.

Source: *Steinmayer 2004.*

“Credit registries can reduce information costs”

Since experience with governmental placement agencies has not always been successful, the job-matching task could be taken over by the private sector, with the state assuming a regulatory role. Since private firms in Africa might not be able or willing to pay a fee, public-private partnerships could be a good model, with the government paying a fee to the private agency for each successful placement. Even nongovernmental organizations can be a placement agency in partnership with a private sector company (box 7.6).

Labour protection or labour market flexibility?

State intervention in the labour market is often considered necessary to protect workers from unfair treatment. But if protection reaches a level that discourages labour demand by prohibitively increasing costs in the private sector, it may reduce opportunities for regular employment in the formal sector. Moreover, groups that might be disproportionately more affected by the cost of job regulation are the most vulnerable groups—including women, young people, the unskilled and the poorly educated. It is thus necessary to balance labour market flexibility and employment security acceptable to both parties. This balance is achieved when labour input can be easily and quickly adjusted to meet labour demand, while assuring a reasonable level of protection for workers.

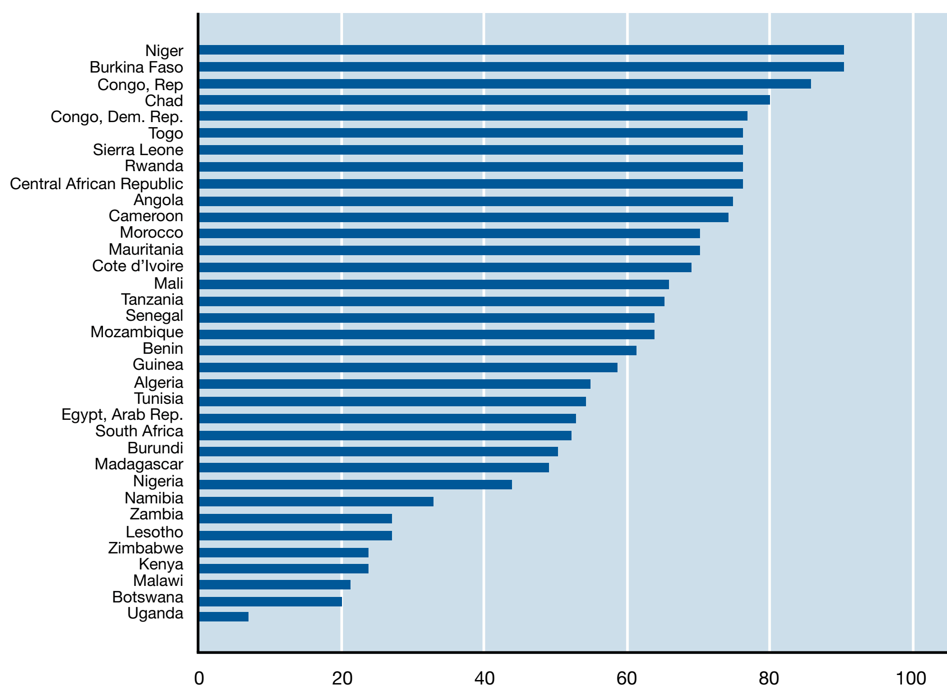
High firing cost and restrictions on temporary contracts tend to create inflexible formal labour markets. If temporary contracts are not allowed and firing costs are high,

employers would prefer to hire less risky workers. Inflexible labour markets especially discourage the employment of vulnerable groups, such as women and young people. Formal employment in Africa is the most rigid in the world (World Bank 2004a). But it has to be taken into account that the largest share of Africans are self-employed, either in agriculture or in the informal sector, and are thus not covered by labour regulations. Rigid labour regulations can encourage businesses to remain in the informal sector and discourage new labour-intensive investment, especially foreign direct investment.

The five African countries with the least rigidities on employment are Uganda, Botswana, Malawi, Kenya and Zimbabwe—the five with the most are Niger, Burkina Faso, Congo, Chad and the Democratic Republic of Congo (figure 7.6).

Although minimum wages are desirable to ensure a minimum level of living, they may discourage employment in the SME sector if they are excessive or if the threshold for pay-

Figure 7.6
Rigidity of employment in Africa



Labour market flexibility and employment security must be balanced

***Note:** Rigidity of employment here is measured as an index on a scale between 0 and 100, with 0 meaning a fully flexible labour market and 100 the most rigid labour market. The index consists of measures of the difficulty of hiring, which includes the possibility of fixed-term contracts and the ratio of the minimum wage to the average value-added per worker, the rigidity of working hours (including the possibility of night and weekend work) and the difficulty of firing.*

***Source:** Doing Business 2005 database, World Bank.*

ing minimum wages is too low. In Burkina Faso the minimum wage is 82 per cent of the value added per worker (Rama 1998). In South Africa many small enterprises in Cape Town's apparel sector do not desire to grow above the number of eight workers because they would be forced to pay minimum wages (Steinmayer 2004).

Firing costs, measured by the severance pay in weekly wages, are extremely high in some African countries. In 15 African countries severance pay is equivalent to the pay of one year or more (World Bank 2004a). The severance pay is equal to the pay for 47 months in Morocco and 40.5 months in Burkina Faso.

Studies of Morocco show that difficult firing regulations hamper job creation (Agénor and El Aynaoui 2003). Dismissing an employee implies a long legal process that usually results in a high severance pay determined by the court. Because it is so complicated to fire an employee, employers enter into costly direct agreements with the employee himself, reducing the employment chances for those with less influential networks.

"High firing costs deter formal hiring"

Employers are reluctant to hire workers, and dismissed employees have no incentive to look for new jobs quickly because they can live for several months on the severance pay. But without any severance pay, dismissed workers could fall into extreme poverty immediately. To enhance employment in SMEs it will be important to deregulate excessive severance pay requirements.

Conclusion

Creating an enabling environment for the private sector to grow and create jobs is an important government responsibility. Although the macroeconomic environment has improved in many African countries since the 1990s, stabilization programmes appear to have no significant impact on private investment in Africa as a whole, while the increase in growth is insufficient to reduce poverty considerably. So, further and deeper second-generation reforms are necessary to improve the business environment, prepare the financial market for small-scale lending, and ensure adequately flexible and efficient labour market institutions.

To create an enabling environment for SMEs and private sector growth, African governments must improve physical infrastructure, encourage informal businesses to register, simplify the registration procedures, secure property rights, improve contract enforcement, promote an entrepreneurship culture and encourage networking among SMEs. Promoting microfinance institutions is an essential part of efforts to prepare the financial sector to provide wider and sustainable services to poor people and to SMEs. Fostering microfinance institutions requires dynamic and adaptive regulation and supervision, reform of the collateral law, the creation of credit reporting agencies and closer links between microfinance institutions and banks. And microfinance programmes should be gender-sensitive and involve financial products that take into account women's needs and constraints.

Labour markets must be flexible enough to stimulate employment, especially for vulnerable groups. Worker protection laws—minimum wages or hire-and-fire regulations—have to be carefully designed and regularly revised to minimize any adverse effects on business growth and labour demand. To hold down search costs and facilitate employment, governments should create and support job centres that not only match employers and potential employees but also provide reliable labour market statistics, training and skills development opportunities as well as advisory services.

Endnotes

1 This section is largely drawn from UNECA (2004b).

2 The OECD average is 34 days, whereas it takes 20 days in South Africa, 28 days in Namibia and 32 days in Mozambique.

3 The regulatory framework may vary across countries and over time (see Basu, Blavy and Yulek 2004). For example, in Benin and some other West African countries there is a dedicated microfinance law that covers saving and loan cooperatives, whereas in Ghana the activities of rural banks are regulated under the commercial bank act.

4 Credit registries are private or state-run reporting agencies that collect and disseminate information on the repayment performance as well as other aspects relating to the creditworthiness of a customer.

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Economic Commission for Africa

Poverty in Africa is substantially higher than in other developing regions. More enigmatic is that poverty on the continent is chronic and rising. At 46 per cent, the share of the total population living on less than $1 a day threshold is higher than in the 1980s and 1990s- this despite significant improvements in the growth of African GDP in recent years. The implication: poverty has been unresponsive to economic growth. Underlying this trend is the fact that most people have no jobs or secure sources of income.

Various reasons have been given for Africa's lack of response of poverty to economic growth. First is the inadequacy of the growth rate. African countries need to grow by an estimated 7 per cent a year to reduce poverty enough to achieve the first Millennium Development Goal of halving the number of poor people by 2015. This growth is far higher than the average of nearly 4 per cent witnessed in the last decade.

Prerequisites for creating decent employment include the transformation of African economies from low productivity traditional agriculture to high value agriculture and agroprocessing- and to the growing industrial and services sectors, taking advantage of the opportunities presented by globalization. Political leadership is required in order to prioritize broad-based employment creation in national development programmes, including poverty reduction strategies.