Growth, Employment and Poverty Reduction

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Labor Market Policy Core Course: Jobs in a Globalized World
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Why the quantity and quality of employment matters for inclusive growth

Introducing segmented labor markets

The need to rethink the role of employment in inclusive growth strategies

Findings from the World Bank program on Employment and Inclusive Growth

Tools for conducting analysis in your country
The quantity and quality of job creation is important for inclusive growth.
Because ...

- The creation of **more better jobs** is an **important transmission channel** between growth, income inequality and poverty
  - an essential element of the inclusive growth agenda

- **Mismatches and frictions** in the labor market are:
  - potential **barriers to growth**;
  - critical factors in determining the **impact on growth and income distribution** of macroeconomic shocks;
  - important determinant of **impact of structural reforms** — in trade, education, etc — on growth.
Poverty Reduction and Growth in China

Figure 2.11: The poverty-growth scissors: 1981-2004

Source: The headcount indices are the percentages of national population below the basic needs poverty line using per capita income as the measure of welfare, taken from Ravallion and Chen (2004) for the period 1981-2001. The estimates for 2001-2004 are based on calculations from NBS survey data undertaken for the poverty assessment, and are spliced with the 1981-2001 series. Per capita GDP is from NBS (2005), China Statistical Yearbook: 2005; it is deflated by the national CPI also from the same source.
The structure of the LM affects inclusive growth through its impact on

- *growth* potentials;
- the *distribution* of the benefits of growth;
- the *extent* to which different groups in the population participate in the growth process.

→ i.e. the structure of the labor market impacts both *efficiency* and *equity*. 
Growth accounting is commonly used **methodology**:

\[
\frac{\dot{Y}}{Y} = s_k \frac{\dot{K}}{K} + s_l \frac{\dot{E}}{E} + \hat{g}
\]

**Transmission channels:**

The LM structure affects growth through its impact on accumulation of E and K.
Barriers to growth:

The prospects for sustainable growth in per-capita GDP may be severely impaired by:

- Labor supply shortages due to adverse demographic trends (ECA) or inefficiently-low participation rates (MENA),
- Skill shortages,
- Inefficient input allocation and price setting may limit firms’ capacity to choose optimal combination of inputs.
The capacity to sell labor is the main potential source of income for the poor:

- The impact of growth on employment is an important determinant of the extent to which growth is shared.

- The employment intensity of growth often conceived as an indicator of how much growth is ‘shared’.

- Focus on estimates of employment elasticity of growth.

In LICs, access to a job is not sufficient to guarantee adequate living standards as 41% of the world’s employed are estimated to be working poor (<$2/day; ILO).
Introducing segmented labor markets
The LM consists of various segments that offer qualitatively distinct types of employment for individuals with identical productivity endowments—i.e., ‘preferred segment’ and ‘least preferred segments’

There is limited access to ‘preferred segments’:
- Not all who want a job there (and can reasonably aspire to get one) can get it.

Three main issues to be addressed:
- The wage/employment setting mechanisms within each sector,
- The way the segments are connected
- The role of frictions and barriers to mobility
Basic Implications of Segmentation

- Cross-segment differences in marginal products may persist over the long-run.
- Wages may differ from marginal product at least in some sectors (oligopsonistic/bargaining/efficiency wage models/wage floors).
- Labor supply may be abundant in some sectors but restricted in others.
- Barriers to mobility prevent optimal reallocation of labor across segments (efficiency losses).
- Poverty would be reduced and welfare enhanced if the causes of segmentation were addressed and those working in the least-preferred segments could gain access to the preferred jobs.
Segmentation and Efficiency

LM conditions—i.e., regulation, skill composition, etc.—are important barriers to inter-sectoral labor mobility.

- Segmented structure of the labor market is a source of inefficiency as TFP losses may arise from the resulting factor misallocation.
- These losses may be substantial:
  - Reallocation of labor away from agriculture explains 20% of cross-country variations in TFP growth [Temple & Woessmann, 2006].
• Segmentation may threaten the equitable distribution of the benefits of growth.

• The sectoral pattern of growth may be as important as the overall level in determining the extent to which it is poverty-reducing.

  - If the ‘preferred’ sector(s) is also the most dynamic, growth may reinforce pre-existing differentials in MVP and earnings.

  - Barriers to cross-segment labor reallocation may prevent workers in the ‘least preferred’ sector(s) from benefiting from increased employment opportunities in the ‘preferred’ sector.
Policy Implications of Segmentation

- Education may not guarantee access to the preferred segments if employment in these segments is rationed.
  - Increased education is an effective policy option only if (i) it increases sectoral mobility of labor and/or (ii) it increases returns in the least-preferred, non-rationed segments.

- It may be more effective to target the sectors in which the poor are not, so that growth in these sectors can pull the poor out of the less productive sectors.

- Identifying and addressing barriers to mobility and other sources of segmentation (i.e., matching efficiency, inefficient regulation) is a priority objective of development policies.
The need to revisit the role of employment in inclusive growth strategies
• Focusing on quantity of employment ONLY is not enough.

• Focusing on aggregate employment elasticity of growth may give misleading perceptions.

• Focusing on changes in average earnings may also be misleading.
This calls for the need to focus on:

- Employment intensity of growth in high-earnings sector(s),
- Impact of growth on upward inter-segment mobility,
- Its impact on the returns to labor in the low-earnings sector(s).
Findings from Country Analysis

The structure of the LABOR MARKET
Understanding the Structure of Labor Markets (1)

• Describing the structure of employment
  – Employed/unemployed/OLF,
  – Self/wage formal/informal, sectoral distribution,
  – Who is in each category? What are their typologies?

• Evidence of differences in returns to individual characteristics across sectors, employment categories, regions, etc.
  – Are some jobs better than others? Which are the good jobs?
• Assessing evidence of queuing for ‘good jobs’ (qualitative and quantitative)

• Identifying barriers to mobility (qualitative and quantitative)

• Assessing extent of lack of skills as a barrier to job creation

• Understanding wage setting mechanisms within each sector.
• Unemployment is a luxury. It is very low and highly concentrated amongst the highly educated and in urban areas. It is positively correlated to growth.

• Participation rate is a fuzzy concept,
  – especially for women
  – especially if it includes 15-24 year olds

• Employment rates are very high ➔ concern with quality NOT quantity of jobs.
Some Results (2)

• Substantial inter-segment differences in returns to labor (controlling for individual characteristics), especially between:
  – Agriculture and other sectors,
  – Rural and urban labor markets,
  – Formal/informal and waged/other,
  – Lowest returns for family enterprise workers in agriculture

• Differences in returns to education across segments
• There is evidence of queuing for good jobs and barriers to moving out of agriculture (Nicaragua).

• No evidence of skill constraints and mismatch:
  – Exception: Madagascar & Rwanda.

• Evidence of inter-segment differentials in returns to education and in some countries, NO returns to schooling in the ‘least preferred’ jobs segment.

• LM regulation NOT a major constraint in LICs but in MICs some regulations act as a barrier to job creation in the good segment (minimum wages, severance pay and payroll taxes).
Findings from Country Analysis

The links between Growth, Poverty, and the Labor Market
• Profiling per capita growth through growth decompositions into:
  – Demographic changes,
  – Sectoral structure,
  – Productivity/employment intensity,
  – Intersectoral labor shifts.

• Linking the profile of growth with poverty changes using both cross-country sectoral data and country specific micro data.

• Identifying the determinants of changes in labor income at household level.
The findings support the implications of the segmented LM model:

- The aggregate employment intensity of growth is not a good indicator of the extent to which growth is inclusive.

- But the sectoral patterns of employment/productivity intensity are. In particular:
  - Movement out of agriculture and increases of agricultural productivity are correlated with poverty reduction.
  - Increases in secondary sector employment are correlated with decreases in poverty but increases in secondary sector productivity are not.
  - The correlation of employment growth in the tertiary sector with poverty reduction is unclear.
Finding 1: Aggregate employment intensity does NOT matter

- **Nicaragua (2001-2005)**: Employment increased 4% per year (1%>labor force) but there was no change in poverty due to:
  - Increased employment was primarily in low-paying sectors, ie agriculture
  - New well-paid employment concentrated in maquila required complete secondary education (barrier to access for the poor).

- **Ghana (1991-2005)**: poverty nearly halved while the employment rate decreased by 9%.
  - 88% of growth accounted for by increased productivity and the rest to an increase in active population.

- **Bangladesh (2000-2005)**: poverty decreased by roughly 20% while the employment rate stayed unchanged.
  - Poverty reduction linked predominantly to increased productivity and wages within economic sectors, within job categories and within rural/urban areas.
**Finding 2: What MATTERS is the sectoral employment and productivity intensities**

- Cross-country: poverty reduction ↑ with
  - employment intensity of growth in the secondary and tertiary sectors
  - productivity intensity in agriculture.

- A 1% growth rate associated with an equal increase in
  - secondary sector employment shares ➔ poverty ↓5%
  - agricultural productivity ➔ poverty ↓7%
  - tertiary sector employment shares ➔ poverty ↓3%,

- Productivity intensive growth in secondary and tertiary sector is not robustly correlated with poverty.
Finding 3: Skills as main factor behind the poverty impact of growth

• Cross-country: when skills are very low, the role of agricultural productivity in overall growth is limited
  ➔ poverty impact is also low.

• ICA surveys:
  – lack of skill is NOT a constraint to employment growth in manufacturing in Nicaragua but
  – it is a ‘major’ or ‘most severe’ obstacle for nearly one third of the formal firms in Madagascar

• In all our country studies, at individual level, lack of education/training is an important barrier to
  – access to employment in secondary sector and well-paid jobs in the tertiary sector and
  – ↑ productivity in the primary and tertiary sectors.
What if I want to conduct this analysis in my country?
• **Cross-sectional data**
  - Need data from two different periods
    • with employment status and category
    • with individual earnings (at least for wage workers)
    • with poverty data
  - Eg. Typical LSMS
  - LM-MD

• **Macro level data**
  - GDP Value Added, by sector
The Labor Market Micro-level Database (LM-MD) was developed to facilitate the production of policy relevant labor market analysis. The Database currently includes data from 16 data sets and 8 countries from across the globe. To the extent possible, these data variables were constructed in order to be comparable across time within a country and across countries, with priority given to the former. An Introductory paper explaining the LM-MD project, along with a Methodological Report and Codebook are included in the section below.

Additionally, you will find:

- An EXCEL file with aggregate statistics of labor market outcomes across all data sets, facilitating cross country comparisons
- An EXCEL file with detailed labor market and poverty indicators for each data set of particular country, which include changes over time
- Detailed micro-level data in STATA format that can be obtained for additional analysis
- Clear documentation on how the data were prepared — including special READ_ME files relevant for each particular data set created. It is imperative that analysts read these files to see the highlights of any assumptions made.
- Links to the complete data set (and questionnaires) that were used to create the LM-MD data sets.

Methodology and Aggregate Statistics

- An Introduction to the Labor Market Micro-level Database (LM-MD) - DRAFT
- Methodological Report for the Labor Market Micro-level Database (LM-MD) - DRAFT
- Labor Market Micro-level Database (LM-MD) Codebook - DRAFT
- Aggregate Statistics (153kb XLS)
Employment LAB

This diagnostic toolbox aims to profile and monitor labor market outcomes and their linkages with growth, employment, earnings, and poverty reduction. Click here for more information.

GUIDES
SOFTWARE
DATA
NOTES

ABERT LABS
Create Labor Market Diagnostics

JOOGS DECOMPOSITION TOOL
Analyze links between Growth and Employment Generation

SimPLE
Simulate Impact of Economic Policy and Shocks on Poverty and Welfare

MOBILITY STATA CODE
STATA Code for Conducting Earnings Mobility Analysis

COUNTRY-LEVEL
USEFUL LINKS

PERMANENT PAGE: http://go.worldbank.org/3JGW_JWZ0

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