African countries are seeing solid economic growth.

Prospects remain strong but a slowing global economy poses downside risks.

Africa’s employment agenda is to increase the productivity of all workers, especially those in the informal sector, where most Africans work.

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This document was produced by the Office of the Chief Economist for the Africa region.
Summary

- The global economic recovery is losing momentum, on faltering growth and heightened economic uncertainty in advanced countries and a moderation of growth in developing countries.
- Sub-Saharan African countries appear to be resilient to global events, but elevated global risks on the downside are weighing down their prospects.
- The devastating drought in the Horn of Africa is hurting people and their livelihoods in the affected areas.
- Despite a decade of strong economic expansion, the pattern of employment in Sub-Saharan Africa remains largely unchanged. The informal sector—including household enterprises—absorbs most of the labor force entrants and youth, into low-skill, low-productivity jobs.
- The challenge for policymakers is to lift the productivity of jobs, especially in the frequently ignored informal sector.

I. Recent economic trends

- Recent developments in high-income countries have pulled down global growth and significantly weakened overall prospects of the global economy.
- Notwithstanding a more difficult global economic environment and the effects of a devastating drought in some parts, the Africa region’s GDP growth is forecast to attain pre-crisis levels in 2012.

RECENT GLOBAL ECONOMIC DEVELOPMENTS

Through July 2011, the global economic recovery was proceeding much as expected. After turning negative in the wake of the Tohoku earthquake, world industrial production was growing strongly (expanding at an 8.8 percent annualized rate in the two months ending June 2011); commodity prices were stabilizing, and as a result, inflationary pressures were easing and real disposable income growth picking up—setting the scene for an acceleration of output into the second half of the year.

In August, investor confidence fell. The European debt crisis worsened with concerns of contagion from periphery countries to other eurozone economies. Weaker than expected second quarter economic activity in major economies and a downgrading of U.S. sovereign debt (by Standard and Poor’s) further rattled the markets, resulting in a significantly weaker outlook for the global economy. The events of August—which highlighted anew the Americans’ and Europeans’ difficulty of achieving a credible plan that puts government finances on a sustainable path in the medium term while supporting the recovery in the near term—will certainly impinge negatively on economic outturns. Even in a benign scenario, investment in both high-income and developing countries is now projected to be weaker and consumer savings higher. Hence, growth forecasts
have been substantially downgraded and the chances of a serious crisis increased. Global GDP is now projected to increase by 2.8% in 2011 (versus 3.2% in June forecasts of the World Bank), and global growth in 2012 and 2013 is also projected to be about 0.4 percentage points lower than in earlier forecasts. Risks of a much more serious downturn have increased. Risk premiums on Italian, French and even German debt have risen and pressure on the debt of Greece, Ireland and Portugal remains intense. Indeed, were a market-induced credit event to occur, depending on the extent to which larger European economies were involved, world output in 2012 could be reduced by 2 to 4 percentage points.

However, most of the current downward revision to growth is concentrated among high-income OECD countries that are now expected to grow 1.6% (vis-à-vis 2.1% in June). Developing country growth has been marked down less noticeably to 6.1% (from 6.3% in June).

OUTLOOK FOR SUB-SAHARAN AFRICA

Notwithstanding the recent perturbations in the global economy, as well as the drought in the eastern parts of the continent, Africa’s growth prospects for the forecast horizon remain robust. Recent economic developments are however expected to reduce the growth momentum in the region and shave off between 0.1% - 0.2% of GDP growth in the region. After attaining 4.6% in 2010, growth is forecast to reach 4.8% in 2011—just shy of the pre-crisis average growth level and lower than the 5.1% forecast earlier—and pick up to 5.2% and 5.5% in 2012 and 2013 respectively, assuming no further significant downward spiral in the global economy.

The downside risks to the current forecasts for Sub-Saharan African economies are significant, given the elevated levels of uncertainty in the global economy in general and high-income economies in particular. If the situation in high-income economies deteriorates significantly beyond what is currently envisaged in the baseline scenario, growth in African countries could be significantly downgraded, beyond the current moderate slowdown. Using a downside risk scenario where growth in Europe slows down by a percentage point below earlier forecast (i.e. from 1.7% to 0.7%), we estimate that GDP growth in Sub-Saharan Africa could slow down by a further 0.8%, thus dipping to 4%. Furthermore, this time around African countries will be more constrained in their policy options. Because they (appropriately) undertook expansionary fiscal policies to offset the contractionary impact of the 2008-9 global crisis, they have less fiscal space than they had in 2008.

Prior to the crisis, more than a decade of steady growth and debt relief had strengthened African countries’ fiscal balances: By 2008, 72% of African countries had posted primary fiscal balances compared with 28% in the early 1990s (IMF, Regional Economic Outlook 2009). The fiscal stance in response to the crisis was related to the available fiscal space and risk of debt distress (Krumm

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**FIGURE 2, 3**

Growth in Sub-Saharan Africa remains robust

**Fastest growing African economies in 2011**

<table>
<thead>
<tr>
<th>Country</th>
<th>Percent growth in GDP</th>
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<tbody>
<tr>
<td>Ghana</td>
<td>8.0%</td>
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<tr>
<td>China</td>
<td>7.5%</td>
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<td>Congo</td>
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<td>Ethiopia</td>
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<td>India</td>
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<td>Mozambique</td>
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<td>Nigeria</td>
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<td>Rwanda</td>
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<td>Democratic Republic of Congo</td>
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<tr>
<td>Zimbabwe</td>
<td>6.6%</td>
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<tr>
<td>Angola</td>
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<td>Botswana</td>
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<td>Tanzania</td>
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<td>Brazil</td>
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<td>Mozambique</td>
<td>6.1%</td>
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<tr>
<td>Russia</td>
<td>6.0%</td>
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</table>

Source: Development Prospects Group, World Bank Group

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Assessing policy performance and fundamentals of African countries

Sub-Saharan African economies rebounded relatively quickly from the impact of the 2008-09 global financial and economic crisis. One contributing factor was that years of sound macroeconomic policies by a broad swath of countries (and debt relief by donors) had helped these countries build fiscal space to implement countercyclical policies to mitigate the impact of the crisis.

Using the Country Policy and Institutional Assessment (CPIA) scores, the picture that emerges for non-fragile countries in Sub-Saharan Africa is encouraging. 1 The overall 2010 CPIA score of this group is 3.6, which compares favorably with the 3.5 CPIA score of IDA countries outside of the region.

Non-fragile countries show particular strength on macroeconomic management, with an average score of 3.9, compared with 2.8 for fragile states in Africa and 3.7 for IDA countries in other regions. This outcome reflects sustained efforts by non-fragile countries to improve macroeconomic policies. These countries also tend to show better performance in areas of structural policy, social policy and governance than other country group.

There appears to be greater convergence in policy performance among the non-fragile group of countries than the fragile group, as evidenced by the much larger coefficient of variation of the latter group. This suggests considerable heterogeneity in the fragile state group.

Following the crisis, some countries have re-built buffers—reserves—through new savings, such as the Republic of Congo and the Democratic Republic of Congo. By contrast, Nigeria continues to see a drawn down of reserves, which are below the 2008 peak level.

**EFFECTS OF SLOWDOWN IN THE GLOBAL ECONOMY ON SUB-SAHARAN AFRICA – TRANSMISSION CHANNELS**

For Sub-Saharan African economies, trade, especially with Europe, remains the main channel through which the current perturbations in the global economy will be transmitted. The importance of Europe is underlined by the fact that even though African countries are increasingly diversifying their export markets, in particular to Asian countries, European Union member states still remain the

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1 The CPIA is a comprehensive rating exercise that covers a country’s economic policies and institutions based on 16 criteria and this exercise is conducted annually by the World Bank staff. It covers four broad areas: macroeconomic stability, structural policies, social and environmental policies, and governance. The resulting ratings – on a scale of 1 to 6 – also play an important role in allocation of the Bank’s soft loans and grants.
region’s largest trading partners, accounting for some 37% of non-oil exports. With the ongoing fiscal consolidation in Europe associated with debt concerns, and a general slowdown in economic activity, demand for exports from Sub-Saharan Africa is likely to be affected. After growing by a tepid 0.8% (q/q) in Q1 2011, growth in the European Union slowed down to 0.2% (q/q) in Q2 2011. For every additional 1 percent of fiscal consolidation carried out in the eurozone and a 2.5 percentage point reduction in investment due to increased investor nervousness, it is estimated that global GDP would shrink by 0.6%, and Sub-Saharan Africa’s GDP by 0.1%.

The effects of the slowdown in Europe will differ across African countries, depending on their exposure to the hardest hit European economies (Greece, Ireland, Portugal, Spain and Italy), as well as the composition of exports. While exports to these eurozone economies account for only 9% of total African non-oil exports, in Cape Verde some 92% of exports are destined for these five economies. Other African economies with a high exposure to these countries include Guinea and Mauritania with 25% and 19% respectively. For most countries in the region, this share is less than 10%. Nonetheless, if the debt crisis were to escalate and encompass some of Sub-Saharan Africa’s major trading partners in the eurozone, the region’s exports would suffer a serious slowdown.

A country’s vulnerability depends on the product composition of exports destined to these markets. Given that in periods of economic downturn purchases of consumer durables, luxury and other non-essential items are deferred, countries exporting such products are more likely to see a sharp drop in exports. Already the current downturn in Europe has led, to a lowering of forecasts of Kenyan horticulture exports growth, from an initial estimate of 15% to 8% in 2011. EU countries account for some 82% of Kenya’s horticulture exports.

The CFA franc zone countries are vulnerable to uncertainties in the eurozone. Historically, these countries have benefited in terms of monetary and price stability associated with a peg to the euro. Between 2000 and 2010, member countries of the zone registered an average inflation of 2.9% compared to over 10% for the rest of the region. However, they also saw a stronger appreciation of the real effective exchange rate of the CFA franc (and associated loss in competitiveness) compared to other currencies in the region, and an average real GDP growth rate (4.4%) that trailed the rest of the region by around 1 percentage point.

Another implication of a slowdown in the global economy is the attendant drop in commodity prices—especially oil and metals. Growth in Africa remains closely linked to the evolution of international commodity prices. Heavy reliance on one or two primary commodities makes most African economies highly vulnerable to external shocks. In 2009, 70% of merchandise exports consisted of fuel, metals, and agricultural products. This share has remained broadly unchanged since 1996, although a decline in agricultural product share has been offset by a near doubling of metal exports. More importantly, 16 of 47 African economies earned over 50 percent of their export earnings from a single primary exports.

Oil prices, which have fallen by 11.3% from their highs earlier this year, are likely to curtail growth prospects in oil-exporting Sub-Saharan African economies; lower oil prices also mean less fiscal revenue from oil, with consequences for government spending on infrastructure and social programs. Growth in these countries is likely to slow down in the second half of 2011,
especially if the fall in oil prices is sustained through the year. The slowdown is likely to be stronger in the lesser diversified economies. In Angola and the Republic of Congo, where the oil sector accounts for over 60% of GDP, it is estimated that for every 10% decline in oil prices, the loss in export revenues will translate into a decline of 2.7% and 4.4% in GDP, respectively. In Nigeria, where the oil sector accounts for 15.9% of GDP, a similar decline in oil prices would have a much smaller impact—about 1.8%. To be sure, in both Angola and the Republic of Congo, new oil that is expected to come on stream in 2011 and 2012 should help compensate for lower oil prices.

The moderation of oil prices is providing a welcome relief for the region’s oil importers, who were hard hit by the spike in oil prices earlier this year. Indeed, median inflation in Sub-Saharan Africa rose to 11% for the first half of 2011 compared to 7.2% for the same period in 2010. Some of the countries facing the highest acceleration in inflation are oil importing countries such as Ethiopia, Kenya, Malawi, Mauritius, Swaziland, and Uganda, though higher food prices, exchange rate depreciations and monetary expansion also played a part in pushing prices up.

The slowdown in the global economy could also impact Sub-Saharan African economies through the financial channel. This channel is most likely to work in the few economies with relatively deeper financial markets, such as South Africa, Nigeria and Kenya. In the immediate aftermath of the US credit rating downgrade by S&P, with the attendant flight to safe assets by investors, stock markets in South Africa, Nigeria and Kenya, like other global bourses, were hit hard. Similarly, spreads for foreign denominated Sub-Saharan African bonds have increased in line with the increased uncertainty in the global economy.

Foreign direct investment is another important channel for transmitting growth shocks in the EU and in other major partner countries, which is likely to be exacerbated in Africa because it is closely linked to mineral prices.

Remittances are also vulnerable to deterioration in source country conditions, as we saw in 2008-9, as are aid flows. Tourism, which is a major sector in countries such as Cape Verde, Mauritius and Seychelles, could also be impacted by a weak global economy. Again, the impact will vary by country.
Private participation in infrastructure in Sub-Saharan Africa

Private activity in infrastructure in Sub-Saharan Africa remains modest in comparison to needs. From 2000-10, 249 infrastructure projects with private participation were implemented in 42 countries in the region. The investment commitments associated with these projects totaled $61.3 billion. Including the additional investment in existing projects, the total investment for the region was $106 billion, or 8% of activity in developing countries by amount of investment.

Private activities in infrastructure were concentrated in a few countries and sectors. Two countries—Nigeria and South Africa—attracted over 50% of private investment in infrastructure in the region. Telecom accounted for 81% of regional investments, with 100 projects in 39 countries. Transport and energy were a distant second and third, accounting for 11% and 8% of regional investment, respectively. Given the large energy and other infrastructure deficit in Africa, improving the regulatory environment and policies will be critical to boosting private participation.

MACROECONOMIC EFFECTS OF Drought

In addition to the turmoil in the global economy, parts of Sub-Saharan Africa are facing specific challenges, the most severe of which is the drought in the Horn of Africa—the worst in over 50 years. The most affected economy is Somalia, but parts of Ethiopia, Eritrea, Kenya and Tanzania are also suffering from the poor rains and dry weather conditions. An estimated 13.3 million people are in need of humanitarian assistance across the Horn (OCHA, September 2011).

With agriculture accounting for about 20% to 40% of GDP in most sub-Saharan African countries, and with about 93% dependent on good rains, the impact of poor rains on GDP growth in Sub-Saharan African economies can be significant. Initial estimates suggest that in the average Sub-Saharan African economy, every percentage decline in growth in the agricultural sector cuts GDP growth by 0.26 percentage points. However, the decline in GDP will differ by country depending on the size of the agricultural sector in the country’s economy and the strength of the agricultural sector’s linkages with the rest of the economy. First quarter 2011 GDP figures for Kenya already show that growth in the agriculture sector slowed down to 2.2% compared to 5.7% over the same quarter in 2010. Coffee delivery fell by some 28% in the first quarter of 2011 in Kenya and for the first half of 2011, tea production fell by 16% (year-on-year) on account of the unseasonal hot and dry weather conditions and poorly distributed rainfall in tea growing areas.

A simulated shock of a 10% reduction in crop and livestock production in the pastoralist areas in Ethiopia (2010/11)—the areas most affected by the current drought—shows agricultural growth declining by
0.6 percentage points and industry and services sectors by about 0.2 percentage points. The overall effect would be to dampen GDP growth by 0.4 percentage points (Hashem Ahmed, 2011). Households directly impacted by the drought-related production shocks are likely to be severely affected as they lose income and livelihoods. To the extent that these shocks are reflected in prices at the local and national level, net consumers of food in both rural and urban areas lose. A persistence of drought or a worsening of the severity of the drought would have more adverse effects. For example, a shock simulating three years of drought (i.e. through 2012/13) would shave 0.3 percentage points off GDP growth in 2012 and 2013.

Food prices remain high

Global price of food remains elevated over year ago levels and close to the 2008 peak level. According to the World Bank’s Food Price Index, food prices in August were up 26 percent over year ago levels, and just 4 percent shy of their peaks of 2008. Major grain prices have risen by varying amounts over the past year, with wheat up 33 percent, maize 77 percent, and rice 25 percent. Prices of other commodities are higher as well, for example sugar (50%) and soybean oil (33%). The overall trend is accompanied by considerable variability in monthly prices. For example, wheat prices declined by 7% in July before posting an 8% increase in August.

In Sub-Saharan Africa, the effect of international food prices on domestic prices is heterogeneous even within countries. In Western, Central and Southern Africa, the prices of domestically produced cereals are increasing within normal seasonal bounds and benefiting from generally good harvests. Low levels of crop production due to drought, compounded by high transport (fuel) cost in Eastern Africa have pushed up food prices in the region, with Ethiopia, Kenya, Somalia and Uganda being the worst affected. Prices of key staples have increased by 94 percent year-over-year in Tanzania and up to 256 percent in Somalia.

Beyond the indirect impact on agricultural sector output, poor rains have reduced hydroelectric power generation in an environment where the lack of adequate power supply is already a binding constraint to economic activity. Tanzania has carried out extensive power rationing in 2011. Some 90% of large firms in the country have their own generators, which being much more expensive significantly reduce firms’ profit margins. In Tanzania, growth forecasts have already been lowered by some 0.3% on account of the lower rains, power outages and higher inflation rates. There has also been some power rationing in Kenya. The Kenya Manufacturers Association estimates that generator power costs alone could account for some 40% of overall costs. The estimated impact of the drought, high food and fuel prices combined with below normal rainfall is about 1 percentage point reduction in GDP growth in Kenya (GFDRR (2011): Kenya 2011 Drought Response Financing Plan).

The GDP impact of the drought does not adequately capture the effects on households. In general, droughts affect poorer households disproportionately. For instance in Kenya where some 3.8 million people are estimated to have been affected, the poverty head count in the drought affected areas averages 70% compared with a national poverty rate of 47%. Similarly, in Ethiopia the majority of the 4.8 million people affected by the drought live below the poverty line. In both countries, cereal prices have risen sharply, significantly reducing the purchasing power of poor households, who spend 60-70 percent of their incomes on food.
II. The challenge of employment in Africa: Raising the productivity of the informal sector

Like other regions, Africa’s growth has not created enough productive jobs to absorb the 7-10 million young people entering the labor force each year. Unlike other regions, most Africans are not unemployed—they are working in low-productivity jobs in the informal sector. While continuing to create formal-sector jobs, African countries need to increase the productivity, and hence earnings, of these informal sector workers, many of whom are in household enterprises.

RECENT EMPLOYMENT TRENDS IN SUB-SAHARAN AFRICA

African countries posted strong growth in the decade before the global financial crisis. Despite this improved growth performance, the pattern of employment in the region has changed slowly. The sectoral share of employment has shown limited movement between 1998 and 2009, with agriculture accounting for nearly 60% of labor, the services sector 30% and industry 11%. This near stagnation in trend, albeit with some variation across countries, reflects the limited underlying structural transformation of African economies. Although there has been a decline in the percent of employed who are poor, the fact remains that the majority of African workers are engaged in low-productivity, low skills jobs.

Each year about 7-10 million youth enter the labor force, and the region’s youth labor force participation rate is among the highest in the world. But job growth in the wage sector in low income countries has not kept pace with his rapid increase. As a result, most youth end up working in non-wage employment—i.e. family farming and non-farm household enterprises. Household survey data show that a higher percentage of employed youth live in relative poverty than unemployed youth and that a higher percentage of employed youth are relatively poor than working adults. These results suggest that youth engage in less productive employment, instead of being in school, because of economic necessity. In short, they have to work to survive.
THE INESCAPABLE MATH OF INFORMAL ENTERPRISE EMPLOYMENT GROWTH

Many low income countries still have a very low share of the labor force in private sector wage jobs (of any kind – casual or with a formal contract). So even rapid growth of the formal sector is unlikely to keep pace with the number of new entrants in the labor force. For example, the fast-growing economies of Uganda, Tanzania, Rwanda, and Ghana saw more than a 10% per annum growth in wage job creation in the last decade. But since this growth came from a very small base, the share of the labor force with primary employment in wage jobs is still frustratingly low. In Uganda, an average of 420,000 people entered into employment every year between 2003 and 2006. Although wage jobs grew at 13% per annum during that period, they only accounted for one out of five of the new jobs created. The majority of the non-agricultural employment created was in household enterprises and microenterprises.

The cross country comparison also suggests another trend—movement out of agriculture as a primary employment and into household enterprises (the non-farm self employed and family workers). Although figure 17 only shows primary employment (and therefore understates the shift), and is a cross country comparison not a within-country one, it does suggest that as income grows (e.g. Cameroon, Ghana, Senegal) and primary employment moves out of agriculture, the bulk of the shift is into enterprise non-farm employment, not wage employment. This might be specific to West Africa (where there is a long tradition of HEs), but it is still striking. A similar trend can be observed in lower income East Asian countries such as Viet Nam.

So what can African countries expect if they maintain high GDP and wage job growth? Figure 18 shows a
simple simulation for a country such as Uganda, where the share of private wage jobs was about 10% before the economic crisis. If growth in GDP returns to the pre-crisis levels and continues to be as labor intensive as in the past, they could expect at most 25% of the labor force would be in these jobs at the end of the decade. The largest share with agriculture, and a sizeable portion in household enterprises, with many households doing both. A country such as Tanzania or Mozambique, with a smaller share and slower wage job growth in the past, might be able to achieve half that.

Thus, the employment challenge for low income countries is to focus not just on transforming low productivity agriculture into a sustainable livelihood for rural and peri-urban households, but to also focus on raising the productivity of these household enterprises.

**HOUSEHOLD ENTERPRISES: WHERE AN INCREASING NUMBER OF AFRICANS WORK**

The fastest growing livelihood sector in most low income African countries is the non-farm self employed and family workers, or household enterprises sector (HEs). Households use underemployed labor and assets to increase income and diversify their livelihoods, often lifting themselves over the poverty line and into the growing middle class. Employment, growth, and poverty reduction strategies need to move these informal enterprises out of the shadows and into the forefront by devising policies to raise their productivity and reduce their vulnerability.

Depending on the country, 30-60 percent of households operate some type of unincorporated enterprise. Enterprise activity is less frequent than family farming, which is still an important source of food and cash for over 80% of households in poor countries such as Mozambique and or Burkina Faso, but less so in richer, more urbanized countries such as Ghana and Senegal. But it is much more frequent than wage employment, despite strong growth in this sector over the past 10 years.

**What is a household enterprise?**

In the development literature informality is typically defined to include the characteristics of not being subject to or avoiding government regulation, and income vulnerability. Informality can apply to an employment relationship, or a characteristic of an enterprise. Household enterprises fall in the enterprise side of informality, and the very low end.

A household enterprise is a non-farm business operated by individuals working without any employees outside the family. This group within the enterprise sector can also the referred to as “nano-enterprise” sector, to distinguish it from the micro-enterprise sector, which includes enterprises with a few employees.

The most obvious HEs are the hawkers in streets and those selling goods in fixed markets stalls, though these traders only make up about half of HEs as the other half work out of their own home. The majority of HEs are in services, but some are also found in small scale manufacturing. Typical activities include: hair dressing, tailoring and weaving, repairs of bicycles and shoes, hair dressing, and preparation of food. About half of HE operators are women. HE operators tend to have completed primary education, but are usually not new entrants to the labor force as some capital is needed at start-up. Although usually labeled “informal”, the majority pay fees and taxes to local authorities in order to operate and often they have procured local registration – making them “formal” by some definitions.
WHY ARE HOUSEHOLD ENTERPRISES IMPORTANT?

In rural areas, as incomes in the agriculture sector grow, and as households add other income sources by using their off season labor to earn extra cash, local demand for goods and services increases, fueling growth of HEs. In urban areas, HEs provide income earning opportunities for workers who do not have enough education to qualify for regular, stable wage jobs. At least half of the urban labor force has no secondary education at all; many did not complete primary education. These workers will not qualify for most wage jobs at medium and large enterprises. Experience has taught employers that without the literacy, numeracy, and problem-solving skills that basic general education provides, on-the-job training will not stick. HEs offer the only livelihood opportunity outside of agriculture. And those who need flexibility in hours of work or want to work for themselves choose to operate HEs. HEs in urban areas tend to be more profitable, and to be reported as a primary economic activity for the individual and household, while in rural areas they may only operate part time. HE also works well as an income diversification strategy. In urban areas, it is not unusual to find a household with wage, HE and agricultural income sources.

HEs survive and grow because they provide low-cost goods and services demanded in a growing, but less developed economy that lacks a diverse modern service sector. In urban areas, mobile retail traders substitute for convenience stores, shopping malls, and the internet. HEs provide the barber shop and take-out food. They manufacture low-quality goods such as home-made bricks, roof thatching, furniture, iron work, which typically will not be demanded as incomes increase further and mass produced or higher quality goods enter the market. For this reason, services tend to dominate the sector and to persist longer than manufacturing activities. HEs mostly sell goods and services to households--they are not linked into supply chains, except in a few cases where wholesalers themselves use informal retail networks to reach consumers. The mobile phone card sales network is an example.
Given the retail nature of their sales, HEs depend on growth in both agriculture and wage incomes to survive. Many of their products are services with a high income elasticity of demand, so HEs thrive as incomes increase. As such, while they rarely kick off a growth process, HEs can help sustain it in low and middle income countries by allowing more employment, more hours of productive work per person, and higher incomes. They have played this role in the past in the “Asian tiger” countries. But HEs are not a development option for remote, chronically poor agricultural areas, for example, as there will not be enough demand to sustain them.

HEs are not the solution to the lack of wage jobs either. Even profitable HEs are not likely to grow. Evidence from other regions as well as Africa shows that few HEs ever hire employees outside the family.

CAN HOUSEHOLD ENTERPRISE EMPLOYMENT REDUCE POVERTY?

Although HEs are often lower productivity activities, HE income plays an important role in poverty reduction and equitable growth. HE earnings are usually higher on average than the available alternatives—working in even lower productivity agriculture, either in wage or non-wage work. HEs are a vehicle to share growth. They fill in the gaps in the labor productivity and income distributions. An economy that only contains super low productivity traditional agriculture and high productivity manufacturing and high-end services is highly unequal. But studies also show that the variance in earnings is higher as well—not all HEs succeed. As figure 21 shows for Rwanda, while the median earnings reported from either agricultural wage work or family farming is lower than the median earnings from any type of non-farm activity—wage or enterprise—the dispersion is greater for the non-farm sector as well. Agriculture is a low paid, low productivity, low risk activity, which puts food on the table but not much else. HEs offer the possibility of a better income, but with risk. Wage employment also offers this option, but only for those who qualify. In this environment, it is not surprising that many households choose to devote at least some of their labor time to agriculture, to offset the risk of the non-farm sector.

Strong correlations between growing rural HE income and poverty reduction have been observed in a number of Asian countries. Empirical evidence from African countries shows that HEs tend to be found in richer areas, and that households with these enterprises are less likely to be poor—they tend to be clustered in the middle quintiles. Stronger evidence from recent panel data in a few Eastern and Southern African countries is showing that adding an HE does make household income and consumption grow faster regardless of wealth level, implying that the causality may run from starting an HE to poverty reduction.

WHAT SUPPORTS HOUSEHOLD ENTERPRISE GROWTH AND PRODUCTIVITY?

Recognizing that the informal will be normal is the first step in developing effective policies and programs to help households create sustainable enterprises. Often the main obstacles to recognizing the “nano-enterprise” sector are political and social. Informal enterprises are not necessarily attractive. For this reason, they tend to be chased out of the business areas in capital cities. They have been criticized in some development circles for not offering the income and benefits of wage employment, so national governments hesitate to include them in their strategies. Yet, they are an important mechanism to facilitate growth and structural transformation in lower income African countries. Until the
Development of the private medium and large enterprise sector reaches a level that can provide wage employment for all those who qualify and want this type of job, and the education of the labor force ensures that the majority will qualify. HEs will be the best option for many workers. Two thirds of new entrants to the labor market in low income African countries have not had any secondary education. These workers will be in the labor force for the next 30-40 years.

HE earnings and sustainability are strongly linked to primary education completion. Furthermore, evidence suggests that post-school training in either business practices such as bookkeeping or in technical areas cannot make up for the lack of at least 6 years or more of basic education. So programs to support HE growth should be targeted at those with this basic educational foundation—which is a big and growing part of the current labor force in many African countries.

Most post-school training programs offered by the public sector have not been shown to be effective in supporting HEs—and not only in African countries, but around the world. Some reasons for this disappointing result are that programs are too ambitious, and are not flexible and demand driven. But the most important reason is that these programs are generally implemented without even the most basic evaluation systems. Programs implemented by NGOs seem to deliver slightly better results, but this is based on only a few cases. Given this poor record, careful experimentation, piloting and monitoring needs to take place before training programs are scaled up.

HEs can benefit from access to affordable financial services. National financial sector policies play a key role in ensuring that affordable products tailored to HEs are marketed. But the focus needs to go beyond access to credit and include savings products and mechanisms to transfer money. Also useful would be programs to enhance financial literacy and basic business skills.

Nano and microenterprise success depends on the local economic environment, and for this reason, local governments (LGs) are key players in efforts to improve the productivity of HEs. HEs need access to locations for their work which are clean, safe, and facilitate their growth. LGs usually have responsibility for administering land and regulating private sector activities, as well as the construction and management of infrastructure important for HE activities such as outdoor markets, drainage and maintenance of local roads, and street lighting. But communication between LGs and HEs is often poor. National governments can help through supporting HE development in national strategies, and training LGs to develop urban strategies and city zoning plans that include HEs. HE associations at either the local or the national level can play a positive role by connecting HEs with markets, opportunities for training or support, and policy makers. HEs often need public, NGO, and/or donor support to set up and maintain these associations.

Finally, more “formality”, in the sense of more regulation of household enterprises, may not be the answer. Indeed, the costs and benefits of more regulation need to be carefully weighed in addressing this issue. For one thing, HEs do not by definition have an employment contract with anyone, so regulating them as employment makes little sense. Second, in many countries, it is legal for an HE to do business in their own name (meaning they do not need to register with a government entity to operate); changing this will not address some of the constraints facing HEs. Lastly, HEs are already regulated by local authorities, in that they may need a license to operate (e.g. motorcycle taxi, bar); if they regularly use a market stall they register and pay monthly fees to guarantee their spot. They often have local taxes imposed on them as well.
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