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ILO/SIDA PARTNERSHIP ON EMPLOYMENT AN INCOMPLETE TRANSFORMATION: SDG 8, STRUCTURAL CHANGE, AND FULL AND PRODUCTIVE EMPLOYMENT IN ETHIOPIA

Per Ronnås and Aditya Sarkar

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An incomplete transformation: SDG 8, structural change, and full and productive employment in Ethiopia

Per Ronnås and Aditya Sarkar

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Executive summary

Ethiopia can look back upon almost two decades of impressive economic and social development, spurred by effective implementation of a series of development strategies. Rapid growth in the yields of its main crops has greatly enhanced food security and helped to lift a large part of the rural population out of poverty. GDP growth averaged 9 per cent between 2001–02 and 2017–18, largely driven by agricultural growth and public investment-led growth in urban areas. Between 2005 and 2015 the number of productive jobs¹ increased from 20 to 33 million. Illiteracy has declined and, on the whole, the generation of Ethiopians growing up today have access to better educational and economic opportunities than their parents.

In the years to come, however, the pace of productive job creation will need to increase even further if the ambitious SDG goal of achieving productive employment and decent work for all by 2030 is to be achieved, that is, to an estimated 2.8 million per year, twice as many as were achieved annually in the period 2005–15. Approximately 2 million of these would need to be in the form of new jobs, mainly in order to provide jobs to approximately 1.8 million new entrants into the labour force each year, but also to eliminate unemployment. In addition, some 820,000 working poor would need to be able to access productive employment annually in order to eliminate poverty and working poverty, either through increasing productivity and returns to labour in their current jobs, mainly in agriculture, or accessing new productive jobs created elsewhere in the economy. Ethiopia will benefit from a strong demographic tailwind in the years to come, easing the task of productive job creation in two main ways: (i) the annual rate of labour force growth will fall from 3.7 per cent in 2010–15 to around 2.9 per cent in 2020–30, and (ii) the age dependency ratio is expected to fall from 0.77 in 2020 to 0.67 in 2030.

Rapid economic growth, but with structural weaknesses

Economic growth has been lopsided and partial. Major qualitative changes in the nature of economic transformation will be needed in order to maintain the momentum of rapid economic development in the years ahead. GDP growth has been fuelled primarily by construction, funded by massive public investments in infrastructure, distributive services, and agriculture. The development of manufacturing has, at least until recently, been disappointing, despite significant policy efforts focused on the development of industrial parks and to attract FDI. Two macroeconomic worries have also emerged: (i) a growing trade deficit and looming foreign exchange constraint, and (ii) low levels of public revenues, which have fallen in recent years as a share of GDP largely because revenues from duties on imports have declined as a consequence of trade liberalization.

A more profound weakness is that economic growth does not appear to have been associated with a commensurate productive and structural transformation of the economy and the labour market. Despite very rapid agricultural growth, economic diversification outside the big cities has progressed slowly. The growth of non-agricultural enterprises has, at least in rural areas, so far been largely horizontal. There is little evidence of vertical growth and a lacklustre development of SMEs has become an Achilles' heel, hindering vertical economic integration. This “missing middle” is also contributing to an increasingly dual economy with a large-scale, capital-intensive, and often foreign-funded and export-oriented modern sector, on one hand, and a traditional sector of very small enterprises typically using primitive technology, on the other. This divide also has a distinct geographic dimension as the large-scale modern sector is confined to large cities and to some large commercial farms,

¹ Defined as jobs yielding an income sufficient for a worker and their dependent to maintain a consumption level above the poverty line.

while rural areas remain overwhelmingly agricultural. The weak economic diversification is even more surprising as agricultural growth has been both broad-based and rapid. One would have expected that such a rapid growth in agricultural labour and farm incomes would have injected greater demand into the local economy, triggering growth also of non-agricultural activities.

This missing middle and the weak link between rapid economic growth and any broad-based structural transformation of the economy is undoubtedly one of the main reasons why high economic growth rates have not translated into any major structural change in employment. For instance, the share of non-agricultural employment, as well as the share of wage employment, increased by only a few percentage points between 2005 and 2013 (the latest year for which country-wide statistics are available). The urban labour market is characterized by a severe imbalance between supply and demand. In 2018, open unemployment stood at 19 per cent, with much higher rates for women and for young people. Underemployment is widespread, while low returns to labour force people to work very long hours to make ends meet. A large gender wage-gap reflects both occupational segregation and discriminatory wage practices.

The past 15 years have seen major advancements in education, albeit from very low levels. Between 2004 and 2016 the share of the adult population that had completed at least four years of education increased from 14 to 27 per cent. Gender differences in educational attainment have by and large been eradicated among younger cohorts. However, rural–urban disparities, as well as disparities between poor and better-off households, remain very wide. Less than half of the rural adult population were literate in 2016 and a mere 6 per cent had more than eight years of primary education.

Challenges ahead

The economic transformation needs to become more broad-based and comprehensive.

The public investment-led development of the past decade is not sustainable and growth needs to be put on a different and more broad-based footing. The focus on export-led industrial development to the relative detriment of agriculture appears unrealistic, especially in the short to medium term. A balanced development policy for Ethiopia would need to focus on a continued transformation of agriculture, combined with economic diversification driven by domestic demand and as well as by manufacturing and export-led growth.

A more comprehensive approach is needed to sustain the momentum of agricultural development and support a transformation towards modern and intensive small-scale farming. The rapid growth of agricultural production over the past 15 years was all the more impressive and encouraging as it was achieved by small-scale farmers and resulted mainly from an increase in yields. Ethiopia has a history of equitable land distribution and some 15 million small-scale agricultural households, holding, on average, a mere one hectare of land, have been the main actors behind the agricultural growth, as well as its main beneficiaries. It appears that the rapid growth in yields was achieved largely through increased use of fertilizers. With the important exception of maize, improved seeds are rarely used and almost all cultivation remains rainfed. Sustaining the momentum of agricultural growth will require a much more comprehensive approach:

The use of yield-enhancing inputs and practices needs to become more broad-based and balanced.

Irregular and uncertain supply of water imposes a major constraint on the development of agriculture in Ethiopia as access to irrigation remains low.

Climate change poses a major threat to agriculture in Ethiopia. High risks of crop failure are inherent in rainfed agriculture and will increase further with climate change. Expansion of irrigation, development of resistant varieties of seeds, and

innovative insurance schemes are some of the counter-measures that should be explored.

The continued very low levels of education and, indeed, literacy, among farm holders will impose a growing constraint on the scope for transforming Ethiopian agriculture away from its subsistence orientation into a modern, market-oriented, and efficient economic sector.

Last but not least, a sustained agricultural transformation is dependent on a diversification of the rural economy in order to develop backward and forward linkages, as well as to provide exit opportunities for agricultural labour.

Weak economic diversification, weak SME development, and the need for horizontal and vertical economic integration across sectors. For the vast majority of rural households off-farm economic activities still provide only a minor source of employment and income. While there is some evidence of an incipient opportunity-driven shift of labour from agriculture to more productive economic pursuits in the non-agricultural sectors, there is also evidence of a parallel distress-driven shift of labour out of agriculture as rural households are forced to turn to casual agricultural wage work or self-employment in low productivity services. More efforts are required to foster a dynamic diversification of the rural economy and that of small towns. This will require interventions on several fronts:

A focus on releasing constraints on SME development and fostering the development of micro-businesses into SMEs, requiring, among other things: (i) improved entrepreneurship and business management capacity, especially among young people; (ii) improved access to finance, (iii) development of support services, and (iv) reform of existing schemes for SME development.

Promotion of regional/local economic development strategies with broad-based local participation and ownership.

Making the fostering of rural–urban economic linkages and vertical linkages between small-, medium-, and large-scale firms a central objective of overall industrial policies.

Education has become an Achilles' heel

Bridging the rural–urban education gap has become a major challenge. The risk that a rural child will never be able to go to school is four times higher than for an urban child and only two out of five rural children complete primary education compared with four out of five urban children. At the same time, the very low levels of literacy among the adult population in rural areas imply a need to further strengthen and expand existing schemes for basic adult education, in particular in rural areas and with a particular emphasis on rural women.

Poverty and child labour deprive children of education and their prospects of becoming productively employed as adults. Poverty is a major obstacle to accessing education. Four out of ten children from the poorest household quintile have never been to school compared with less than one out of ten children from the richest quintile. Access to secondary education is still confined largely to children from the richest households. Child labour is widespread, particularly in rural areas and among children from poor households. Less than a fifth of the rural children (aged 5–17) can attend school unfettered by any obligation to work.

Strategies for human resource development and for economic development need to be harmonized at all levels. The educational attainment structure in Ethiopia has a broad base at the bottom, a weak middle, and a fairly strong top, resulting from an elitist education policy in the past and massive investments in primary education in recent years. Not only is the middle narrow, but funding for secondary education continues to be squeezed. Much higher priority needs to be given to secondary education to bring human resource development in harmony with the country's overall development vision and strategy. The

balance between general and technical, vocational and professional education at the secondary and post-secondary levels also needs to be revisited and revised as part of a policy to develop TVET into a good option endowing the students with the skills and capabilities needed to access jobs as skilled professionals.

Releasing the human development constraints on inclusive and sustainable development. Ethiopia's educational attainment structure and still limited coverage and the huge rural–urban and poverty-related inequalities in access to education impose a serious obstacle to inclusive development and limit the scope for moving out of the low-technology, low-wage manufacturing segment and climbing the technological ladder. Major efforts are required to sharply increase access to both primary and, not least, secondary education for rural young people— who make up the vast majority of the country's youth – to prevent human capital from emerging as a major constraint on sustaining rapid productive transformation and economic growth in the years to come. This will require not only a sustained rapid expansion of education facilities in rural areas, but also forceful measures to sharply reduce child labour and to eliminate it entirely in its worst forms.

The gender gap has been closed in education but remains wide on the labour market and at work

Women make up more than 40 per cent of the agricultural labour force and head a quarter of all farm households, yet have less access to land and other factors of production than men. In business, women tend to have less access to resources to grow and formalize their businesses, leading to smaller firms with lower profitability. The gender wage gap remains very large overall as within-sector and very high female unemployment rates testify to the difficulties women face on the labour market. Achieving equality between men and women on the labour market and at work deserves priority and will require a wide range of policy interventions.

Engaging young people in the labour market

Young people currently aged 15–24, together with those who will reach working age between 2020 and 2030, will make up approximately 61 per cent of the working age population in 2030. They will be better educated and much better connected with and informed about the outside world than the older generation and, undoubtedly, have higher aspirations and new visions. However, they will arguably also face greater challenges than previous generations. Rural young people will be more land constrained than their parents. Education and skills will become increasingly important as they are called upon to lead a transformation of agriculture from subsistence farming to modern commercial agriculture and as they will increasingly need to seek productive employment and careers outside agriculture. In urban areas, young people face major difficulties in getting a foothold in the labour market, as reflected in very high youth unemployment rates. The disadvantages of being newcomers on the labour market and lacking work experience, particularly in a situation in which the number of jobseekers far exceeds the number of vacancies, is likely to be the most important reason behind the high youth unemployment.

Catching those at risk of falling behind

Consumption among the bottom 15 per cent in rural areas contracted between 2005 and 2016. This suggests that amidst the general trend of upward mobility there has also been a counter-trend of impoverishment. Indeed, in parallel with opportunity-driven economic diversification there is also evidence of a distress-based and entirely supply-driven economic diversification as agricultural households turn to whatever non-farm employment and economic activities they can find to supplement on-farm income when the latter no longer suffices to make ends meet.

Today's large inequalities in access to education are particularly worrisome as they will translate into inequalities in access to productive jobs and decent work tomorrow. A large segment of rural young people are at risk of being left by the wayside of development. With too little land to make ends meet and with insufficient education and skills to access productive non-farm wage jobs or to become successful entrepreneurs they are at risk of getting stuck in perpetual poverty.

Introduction

Sustainable Development Goal (SDG) 8 exhorts countries to “promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all”. It was formulated in response to profound challenges, including a disconnect between economic growth and job creation, high rates of working poverty, and lack of opportunities for decent and productive work. By adopting SDG 8, the international community sought to place job creation at the heart of economic policy-making and development plans.

As part of the systematic follow-up and review of the implementation of the 2030 Agenda, this chapter examines the opportunities and challenges associated with promoting productive and decent employment for all in Ethiopia. It finds that much progress has already been made: unprecedented economic growth has reduced poverty by half through growth in productive jobs. These achievements are all the more remarkable considering that until the early-to-mid 1990s, Ethiopia was synonymous with conflict and famine and was one of the poorest countries in the world. Yet, substantial challenges and iniquities remain; these are the focus of this chapter.

This chapter has seven sections, which are organized as follows. The first section sets out the scale of the challenge facing Ethiopia, and briefly outlines the history of Ethiopian development planning. The next three sections examine, in turn, the trajectory of economic growth, trends in demographic dynamics and human development, and characteristics of Ethiopia’s labour market. Section 5 turns the lens on employment challenges faced by young people. Section 6 is the analytical centrepiece of the chapter. It begins by asking: *what are the constraints and challenges for achieving productive employment and decent work in Ethiopia?* Keeping in mind the 2030 deadline for meeting SDG targets, it uses a medium-to-long term lens to analyse poverty reduction trends in Ethiopia, and examine the principal pathways through which people can access productive employment, as well as the primary challenges that they face in doing so. Section 7 concludes by tying together the various strands of analysis and offering some broad policy recommendations.

One major caveat: statistical data on Ethiopia are highly fragmented and often outdated, and comparability across different surveys and reports is limited. The data also sometimes lead to contradictory conclusions; these mentioned are in the text. While every effort was made to use multiple sources, including secondary research and ethnographic studies to supplement the analysis, there are points on which the data are simply too sparse to offer anything more than tentative conclusions.

1. Strategies for economic and political development

Processes of economic development in Ethiopia, as elsewhere, have been closely tied to changes in Ethiopia's political system. The historical development of the Ethiopian state and the organization of Ethiopian society have had a direct impact on the country's development challenges. Furthermore, diagnoses and choices of strategies to try to overcome developmental challenges have varied as political and governance priorities have shifted over time.

1.1 The state and development planning in Ethiopia

The Ethiopian state originated in Ethiopia's northern highlands, which historically were characterized by grain cultivation through ox-plough agriculture, and deeply hierarchical social organization. These areas were relatively densely populated and formed the nucleus of a state able to defend itself against European colonialism. At the same time, however, they produced little that could generate income from a global economy and were subject to progressive ecological degradation, barely producing enough to sustain the existing population. The subsequent conquest of vast areas to the south and to the west of the highlands in the nineteenth century provided the imperial Ethiopian state with a much expanded economic base, including export crops, such as coffee.² Prior to the outbreak of the Second World War, the imperial Ethiopian state continued to exercise its power through an exploitative system in which land was alienated on a large scale to those who held power in government (see Clapham, 2019, p. 34).

After a brief period of Italian rule, the imperial state was restored in 1941. The reign of Emperor Haile Selassie, which lasted until 1974, was characterized by increasing foreign direct investment in commercial agriculture, and the creation of new parastatals, such as the Imperial Highways Authority, the Imperial Board of Telecommunications of Ethiopia, and Ethiopian Air Lines. Some development schemes were implemented, but often in politically peripheral parts of the country and with little concern for the interests of indigenous residents. During this period, land continued to be appropriated by powerful individuals connected to the regime, especially in coffee-growing regions (see Fantini and Puddu 2016, pp. 93–94, 101–106).

The military regime (known as the “Derg”) which overthrew the imperial government in 1974 nationalized all rural and urban land, and created a system of peasants'/urban dwellers' associations, known as *kebeles*, which still exists today. Land reforms resulted in relatively equitable land distribution and the dominance of small-scale farms. The redistribution of land reduced the risk of landlessness, but weak property rights also acted as a disincentive to long-term investments in agriculture. These reforms also inhibited outward migration and led to intensified pressure on land, because peasants had rights to land only in their “home” areas (Clapham, 2019, p. 37). Rapid population growth and measures such as forced collectivization, villagization, and state control of agricultural marketing led to slightly lower real output per person employed in 1992, compared with 1950 (Tafesse, 2019, p. 470).³

In 1991, the Ethiopian People's Revolutionary Democratic Front (EPRDF) overthrew the Derg. The EPRDF and one of its powerful constituents, the Tigray People's Liberation

² See Zewde (2001) for a detailed discussion. See also Donham and James (2002).

³ Of course, it is worth noting that declining per capita yields was characteristic of most of Sub-Saharan Africa between the 1970s and the 1990s as a result of population growth, combined with stagnating production.

Front (TPLF), had a considerable rural support base, and a professed ideology of putting the rural population at the forefront of development efforts. One of its first priorities was therefore to respond to the difficulties faced by those working in agriculture. Successive EPRDF-led Ethiopian governments have since articulated a relatively cohesive and overarching vision for economic development in a series of national development plans.⁴ Former Prime Minister Meles Zenawi argued that neither the “Washington Consensus” nor the state-led developmental model of East Asian countries were completely appropriate for Ethiopia. Instead, what was required was an activist state, centralizing the collection of economic “rents” and allocating them for developmental purposes (De Waal, 2018, p. 2).⁵ Crucially, the EPRDF maintained most of the Derg’s land policies, arguing that land privatization would lead to distress sales and the displacement of the peasantry (Lavers, 2012). As a result, land continues to be state-owned, with restrictions on its sale and lease. Rural residents have been guaranteed access to land through a law that grants them a right to obtain agricultural land for free (Bezu and Holden, 2014a, p. 259). Given widespread land scarcity, however, inheritance has become the primary method for young people to access agricultural land. This has led to increased land fragmentation, and gender disparity in access to agricultural land, despite laws guaranteeing equal acquisition and user rights to male and female citizens (ibid. p. 264). Rural–urban migration continues to be discouraged (Dorosh and Schmidt, 2010).

The underlying ideas for the first generation of development plans were first articulated in an approach described as Agriculture Led Development Industrialization (ADLI).⁶ In the early 1990s, there was only a small non-agricultural/urban sector in Ethiopia, with the vast majority of the population involved in (subsistence) agriculture.⁷ Agriculture suffered from low yields and labour productivity. Poverty was prevalent in rural and, to a lesser extent, urban areas, and food consumption constituted between 56 and 60 per cent of consumer budgets (Dercon and Gollin, 2019, p. 456).⁸ School enrolment and literacy levels were very low (see Rekiso, 2019), connectivity was poor, and the country became landlocked with Eritrea’s independence in 1993. In responding to these challenges, ADLI drew its intellectual inspiration from economic models that argued that increases in agricultural productivity could lead to structural change in the economy.⁹ More specifically, Ethiopian policy-makers argued that agricultural productivity growth, especially among smallholders, would stimulate industrial demand through: (i) higher rural incomes, (ii) lower food prices in urban areas, (iii) increased savings in rural areas, leading to mobilization of capital for domestic industry, and finally (iv) the expansion of domestic markets for non-agricultural goods (Dercon and Gollin, 2019, p.454). The policy also aimed to encourage investment in industries with the most production linkages to agriculture/rural areas (Moller, 2015, p. 24).

Implementation of this approach began only with the 2002 (three-year) Sustainable Development and Poverty Reduction Plan (SDPRP), which was replaced by the more ambitious PASDEP (Plan for Accelerated and Sustained Development to End Poverty)

⁴ For useful historical background, see Clapham (2018) and Admasie (2016).

⁵ Meles Zenawi’s logic was that because the government’s economic power in most African countries was significantly larger than that of the private sector, it created incentives for rent-seeking through capture of political office. Centralizing rents allowed the state to allocate them for developmental purposes, while also reducing the incentives for elite rent-seeking behaviour. At the same time Meles believed that an activist state was also necessary if Ethiopia were to ever compete in a globalized world. Of course, rent-centralization creates further opportunities for corruption, but Ethiopia appears to have been better at countering corruption through institutions such as the Federal Ethics and Anti-Corruption Commission (established in 2001). See Kelsall (2013).

⁶ See reference in Ministry of Planning and Economic Development (1993).

⁷ A total of 85–90 per cent of the rural population was engaged in crop agriculture, and pastoralism and non-sedentary agriculture constituted the rest (see Dercon and Gollin, 2019).

⁸ Drawing on data from the 1995–96 Household Budget and Expenditure Survey.

⁹ The classic work on this is Johnston and Mellor (1961). For an interesting overview and critique see: Dercon and Gollin (2014).

covering 2005–10. These plans were followed by the GTP-I (see Federal Democratic Republic of Ethiopia, 2010) and GTP-II (Growth and Transformation Plans, covering 2010–15 and 2015–20, respectively), which began to move away from the ADLI approach. GTP-II in particular, which is in force now, has a greater focus on export earnings from labour-intensive manufacturing, while retaining its focus on backward linkages to agriculture, value added chains, and import substitution. GTP-II continues to identify agriculture as the main driver of economic growth but notes that emphasis ought also to be placed on increasing the productivity of small-holder farmers, while also speeding up commercialization and the transition to the production of high value crops. The primary difference from earlier development policies is that rising agricultural incomes are not expected to be the sole driver of demand in the economy, but will be complemented by export-led industrialization (Manyazewal and Shiferaw, 2019; Federal Democratic Republic of Ethiopia, 2016).

Coincidentally, the Sustainable Development Goals (SDG's) were adopted a little after the launch of GTP-II. On this occasion Prime Minister Hailemariam Dessalegn acknowledged the huge challenges that Ethiopia was confronting, including the elimination of extreme poverty, the transformation of its economy such that it could generate jobs for young people, the development of human resources, and the creation of a learning society, all while conserving the environment and countering climate change.¹⁰ At the same time, he reiterated Ethiopia's commitment to the important task of implementing the SDGs and to building these into Ethiopia's national planning processes.

Ethiopia is currently in the process of developing its next set of national development policies, during a period of political transition in the country. Some of the institutions involved in the formulation of these policies (notably the erstwhile National Planning Commission)¹¹ have noted that, despite their intellectual coherence, previous policies such as the GTP-II were designed through a top-down process; a greater degree of analysis and consultation is expected to feed into the development of the next generation of development policies.

1.2 The employment challenge ahead

Ethiopia's progress over the past 10–15 years towards poverty elimination and achieving full and productive decent work for all has been impressive. The number of productive jobs¹² increased by an estimated 1.3 million per year, from 19.6 to 32.6 million, between 2005 and 2015. By 2015, an estimated 72 per cent of all jobs could be classified as productive, implying that almost 70 per cent of the labour force was productively employed, up from 60 per cent in 2005 (Table 1.1). This achievement is all the more impressive as it took place in the context of very rapid labour force growth. In absolute terms, however, the deficit of productive jobs increased by about 1 million over the decade 2005–15 (Table 1.1).¹³

¹⁰ Permanent Mission of the Federal Democratic Republic of Ethiopia to the United Nations (2015).

¹¹ At the time of writing, this was known as the Planning and Development Commission.

See <http://www.npc.gov.et/web/guest/about-commission>.

¹² Defined as jobs yielding an income sufficient for a worker and their dependents to maintain a consumption level above the poverty line.

¹³ The deficit of productive jobs is made up of those who are in the labour force but do not have productive jobs, that is, those who are either working poor or unemployed.

Table 1.1. Recent employment trends and projected need to create productive jobs to achieve SDG 8 (full and productive employment for all)

(thousands)	2005	2015	2013
Working age population 15–64	38 475	54 826	86 753
Labour force	32 935	46 931	74 261
Employed	31 288	44 819	74 243
Unemployed	1 647	2 112	0
Working poor	11 639	12 236	0
Productively employed	19 649	32 584	74 243
Deficit of productive jobs	13 286	14 347	0
(percentages)			
LFPR	85.6	85.6	85.6
Unemployment rate	5.0	4.5	0.0
Employment rate	81.3	81.7	85.6
Poverty rate	37.2	27.3	0.0
Productively employed, as a percentage of LF	59.7	69.4	100
Deficit of productive jobs, as a percentage of LF	40.3	30.6	0

Notes: The figures are based on UN population estimates and are approximate. The forecast assumes that labour force participation rates remain unchanged between 2015 and 2015. All figures are based on working-age population defined as those aged 15–64.

The labour force participation rate (LFPR) and employment rate are measured against the total working age population. The unemployment rate, shares of productively employed and deficits of productive jobs are measured against the labour force.

The headcount poverty rate was used as a proxy for the number of working poor, using the current international cut-off point of USD 1.90.

Productive jobs/productively employed are defined as employed people earning enough to permit consumption above the poverty line for themselves and their dependents. The deficit of productive jobs covers those who are in the labour force, but not productively employed, that is, the working poor and the unemployed.

A breakdown of working poverty by sex is less meaningful as poverty is measured at the household and not at the individual level.

Sources: Estimates of working age population are from World Population Prospects (2019). Labour force participation rates, employment, and unemployment rates are from LFS (2013). Poverty rates are from World Bank (2019b). Authors' calculations.

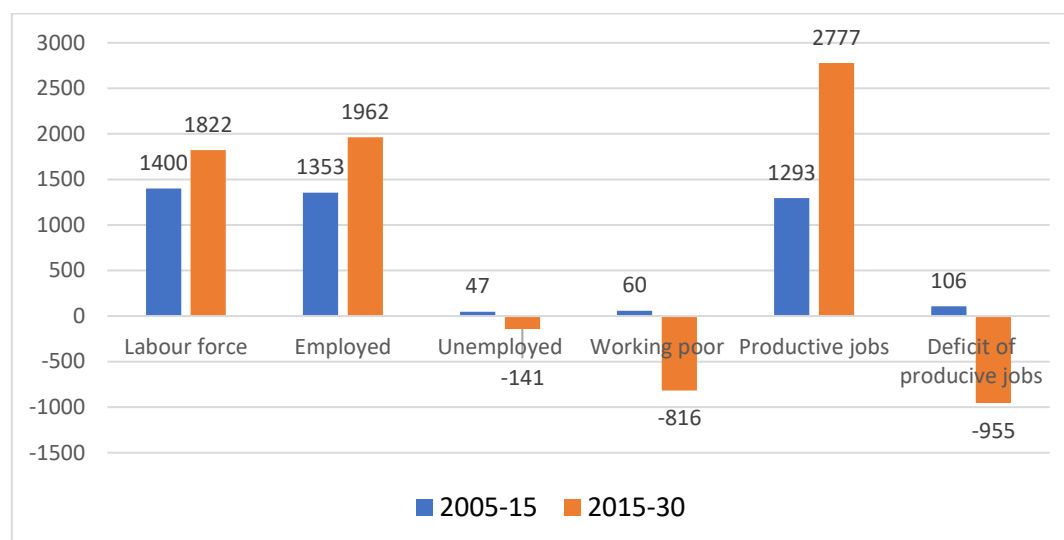
The productive job deficit consists primarily of the working poor; it is a problem of lower productivity and earnings rather than an absolute lack of employment. Working poverty is predominately a rural and agricultural phenomenon. In 2015, one-third of the employed in rural areas were working poor, as against 10 per cent of the urban employed. By contrast, open unemployment is mainly an urban phenomenon. According to the latest labour force survey conducted in 2013, 16.5 per cent of the urban labour force was unemployed, compared with only 2 per cent in rural areas, where agriculture serves as an employment buffer (LFS, 2013).

If the ambitious SDG goal of achieving productive employment for all by 2030 is to be achieved the pace of productive job-creation will need to increase even further. A rough projection suggests that the number of productive jobs would need to increase by almost 2.8 million per year; that is, twice as many as were achieved annually in 2005–15 (Figure 1.1). Approximately 2 million of these would need to be in the form of new jobs, mainly in order to provide jobs to approximately 1.8 million new entrants into the labour force each year, but also to eliminate unemployment. In addition, some 815,000 working poor would need to access productive employment annually in order to eliminate poverty and working poverty.

The job-creation challenge in the years ahead is staggering in terms of the absolute numbers involved. When expressed as annual rates of growth, it appears somewhat less daunting. Ethiopia will benefit from a slowdown in the annual rate of labour force growth

from an exceptionally high 3.7 per cent in 2005–15 to an estimated 3.1 per cent per year in 2015–30.¹⁴ Hence, the supply pressure on the labour market will fall somewhat. Still, the annual rate of growth of productive jobs would need to increase from 5.2 per cent in 2005–15 to 5.6 per cent in 2015–30. As the creation of new productive jobs at a rate of more than 5.6 per cent per year is well-nigh inconceivable, the targets of productive job creation can be achieved only by a combination of (i) increasing productivity and returns to labour in jobs where the working poor are currently found, that is, mainly agriculture, and (ii) creating new, productive, non-agricultural jobs at a rate high enough to absorb not only the large numbers of new entrants into the labour force, but also those working poor moving out of agriculture in search of more productive jobs elsewhere in the economy.

Figure 1.1. Estimated annual change of main employment indicators, 2005–15, and projections for the period 2015–30



Source: Based on Table 1.1.

Different approaches are required for rural and for urban areas. In the former, the focus needs to be on increasing returns to land and labour in agriculture, but also to provide exit opportunities from agriculture in the form of productive non-farm jobs. In urban areas the focus needs to be on the creation of more productive jobs. Urban and rural employment challenges are not separate issues, however, but are deeply interconnected. Addressing unemployment in urban areas without a parallel focus on eliminating the deficit of productive jobs in rural areas would only result in increased rural–urban migration of labour in search of productive jobs and would exacerbate the urban unemployment problem.

¹⁴ Calculation based on Table 1.1.

2. Economic Growth in Ethiopia

Having identified the scale of the employment challenge in Ethiopia, this section begins the process of analysing progress on SDG 8. It provides an analytical overview of economic development against the backdrop of the question, *Is the transformation of the Ethiopian economy effectively contributing to the goal of full and productive employment and decent work for all?* The section is divided into four sub-sections, which deal with: (i) economic growth and the structure of the economy, (ii) the macroeconomic policy environment, (iii) the business environment, access to credit, and patterns of investment into Ethiopia, and (iv) trade.

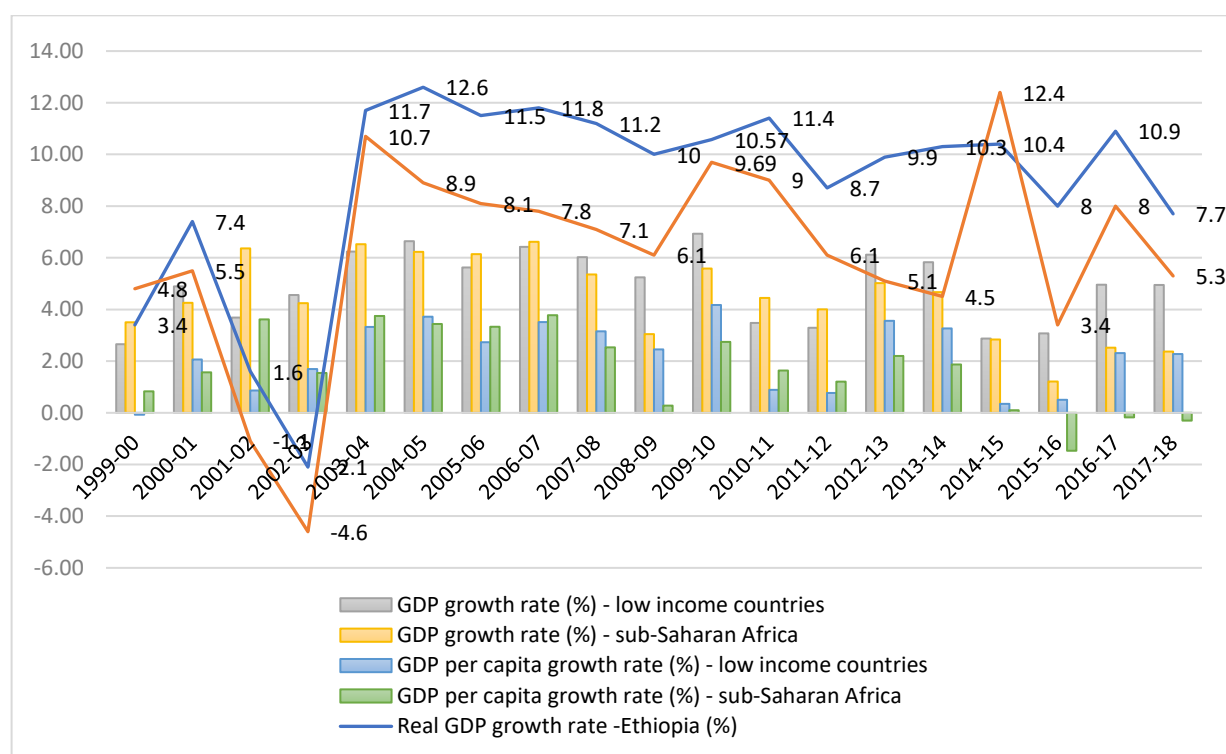
2.1 The Ethiopian economic growth story: An incomplete transformation

In the 1990s, growth was held back by persistent climatic crises as well as conflict in the region. Since then, however, economic growth has been faster than during either the Imperial era or the Derg regime, outpacing other low-income and sub-Saharan African countries (Moller and Wacker, 2017, p. 198). Between 2000–01 and 2017–18, GDP growth averaged 9.1 per cent per year, peaking at 10.3 per cent between 2010–11 and 2014–15.¹⁵ Growth was driven initially by agriculture, but since 2010 has increasingly been driven by steady growth in services and high growth in the industrial sector (see Figure 2.2).

Within industry, however, the growth trajectories of manufacturing and construction have diverged (see Figure 2.2). The growth of the industrial sector has been fuelled primarily by construction, which has been funded through massive public investments in infrastructure, not least in energy, transport, and communications, albeit from a very low level (*ibid.*; see also World Bank, 2015a). Infrastructural investment has been financed by a mixture of restrained government consumption, domestic and foreign borrowing and ODA and has been executed partly through off-budget state owned enterprises (SOEs) (Moller and Wacker, 2017). However, this approach may have reached its limit, and the declining growth rate of construction, and by extension, the industrial sector, in recent years reflects a decision by the Ethiopian government to focus on fiscal consolidation and reduce public spending. The development of manufacturing has, at least until recently, been disappointing, despite significant policy efforts focusing on the development of industrial parks. It constituted just under 6 per cent of GDP in 2017–18, which is lower than the average for Sub-Saharan Africa. Between 2009–10 and 2016–17, however, growth rates in the manufacturing sector averaged 16.7 per cent per annum, before declining to 5.5 per cent in 2017–18. This period of relatively rapid growth occurred from a low base and does not appear to have led to any substantial increase in manufacturing jobs. It does suggest, however, that the export-driven manufacturing policy may be beginning to yield positive results.

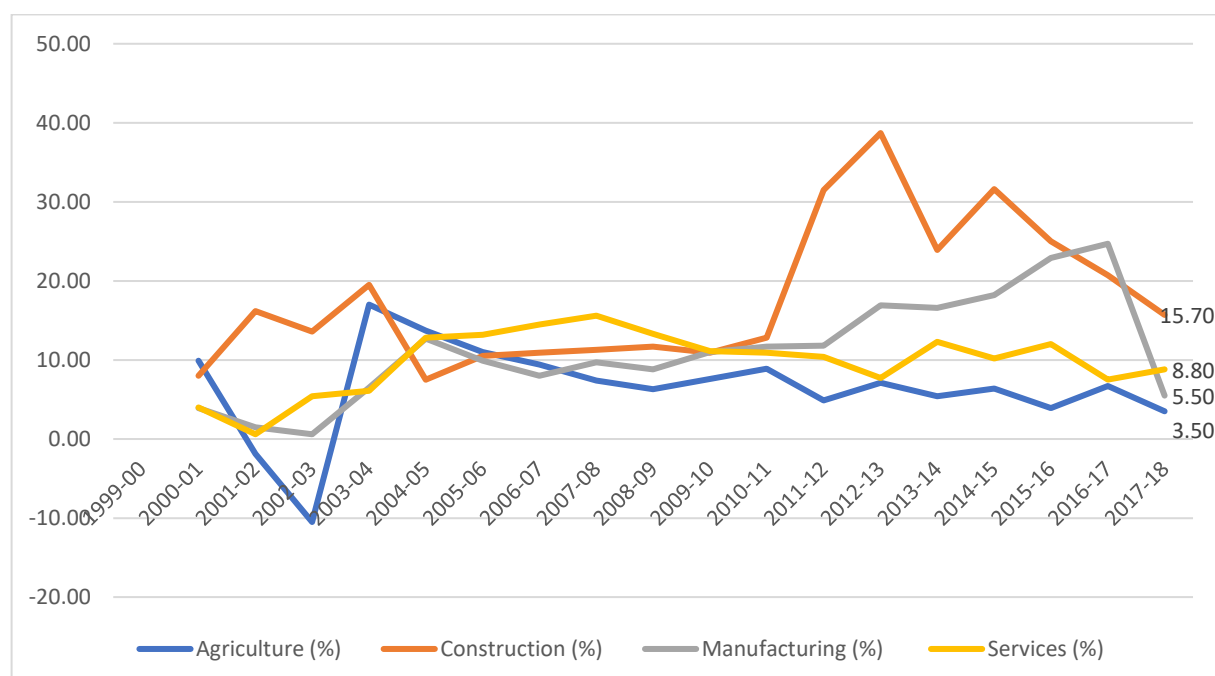
¹⁵ Some controversy remains around the precise rates of GDP growth – in the past, international financial institutions' estimates for growth figures have diverged from the figures reported by the Ethiopian government: see Mandefro and Jerven (2015). The most recent Economic Update on Ethiopia published by the World Bank (2019, pp. 5–8) also points to inconsistencies in growth estimates as a result of the change of the base year in Ethiopia's national accounts. While the practice of changing base years in national accounts is not uncommon, in this instance, the change of base year resulted in a doubling of GDP in constant prices.

Figure 2.1. Real GDP growth rate and real GDP per capita growth rate in Ethiopia (%)



Source: Real GDP growth rate and real GDP per capita growth rate for Ethiopia extracted from data published by the National Bank of Ethiopia; data on GDP growth rate and GDP per capita growth rate for low income countries and sub-Saharan Africa extracted from World Bank, World Development Indicators.

Figure 2.2. Annual growth rate of sectors (%)



Source: Planning and Development Commission (formerly the National Planning Commission, 2019).

The contribution of agriculture to GDP growth has fallen significantly since 2010–11, reflecting declining growth of agriculture from a high level, as well as the increased importance of construction and services (Table 2.1). Within services, growth has been

concentrated in wholesale and retail trade, hotels and restaurants, transportation and communication.¹⁶

Table 2.1. Contribution of sectors to GDP growth (percentages)

	2010–11	2012–13	2014–15	2016–17	2017–18
Agriculture	34.1	27.7	23.4	24.4	17.5
Industry	15.3	37.2	41.0	46.9	43.3
Manufacturing	4.2	6.8	8.3	14.8	5.3
Construction	7.3	29.1	34.0	33.0	38.4
Services	34.4	26.5	35.6	29.1	46.8
Distributive Services	11.6	19.5	24.2	16.0	29.5
Other Services	22.8	7.0	11.4	13.2	17.3
All sectors	100	100	100	100	100

Source: Data from Planning and Development Commission (formerly the National Planning Commission).

Thus, the structure of output in the Ethiopian economy has changed considerably over the past 20 years (Figure 2.). While agriculture remains a very important part of the economy, its share in total output decreased from 66 per cent in 1991 to just under 35 per cent in 2018. In contrast, the share of industry in total output increased from 9.7 per cent in 1999–2000 to about 27 per cent in 2017–18. This was due been to the startling growth in construction, though manufacturing growth has played a role (especially since 2009–10). The share of services in total output has remained relatively stable over the same period, increasing marginally from 37 to 39 per cent.

At first glance, therefore, this seems to be in keeping with an economy developing through “structural transformation”. In its classic formulation, structural transformation is thought to take place when surplus labour in agriculture becomes a labour pool for the development of manufacturing, with its higher value added and greater economies of scale. With increasing incomes, a service sector then develops catering to the growing manufacturing sector, as well as to the rising purchasing power of consumers. In other words, in economies undergoing structural transformation, we would expect to see labour reallocated from low-productivity sectors, such as subsistence agriculture, to more dynamic and higher-productivity economic activities, such as commercial agriculture, manufacturing, and modern services (see Lewis, 1954; Johnston and Mellor, 1961; Dercon and Gollin, 2014).

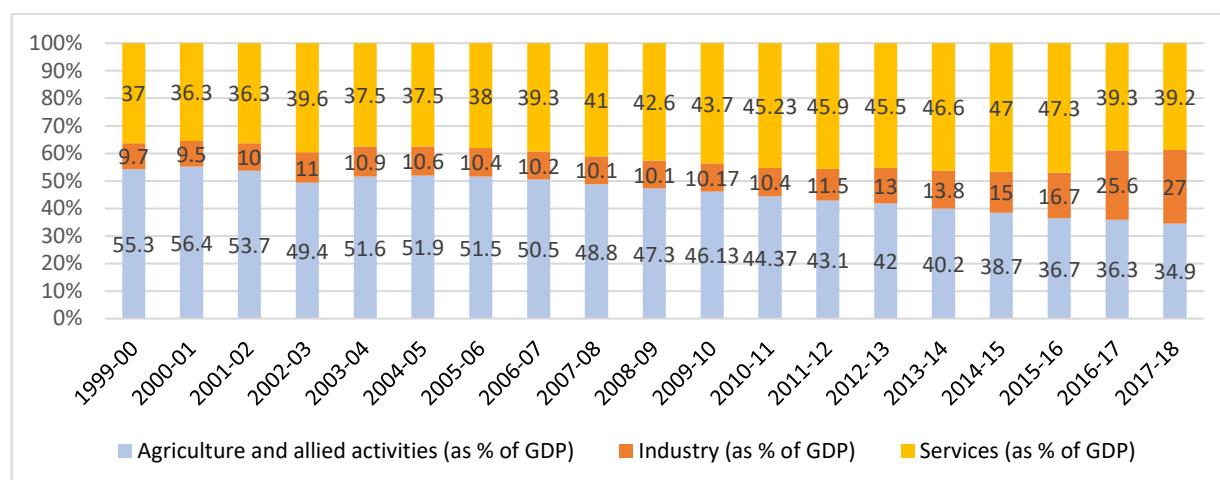
It is doubtful, however, whether the classic progression of structural change is actually under way in Ethiopia. First, these changes in the composition of economic output have not been accompanied by substantial changes in employment patterns.¹⁷ For instance, although the share of agriculture in output has fallen sharply, it continued to employ 73 per cent of the workforce in Ethiopia in 2013. Second, the recorded shift of the workforce out of

¹⁶ These sectors form part of distributive services, which can be understood as services that move commodities, information, and people. Some of these services are final consumption in their own right (for example vacation travel) but most are ancillary to final consumption (for example retailing) or production (for example materials transport).

¹⁷ The absence of recent comprehensive labour force data and a change in definition, reclassifying domestic workers in rural households as employed in services, make a precise assessment difficult. The transformation of employment is further explored in Section 4.

agriculture, to the extent that it has occurred, appears to be largely a statistical artefact due to changes in survey methodology.¹⁸

Figure 2.3. Shares of sectors in GDP (percentages)



Source: Data from the National Bank of Ethiopia (2019).

Finally, there has been a modest increase in the domestic savings rate from 19.2 per cent in 2011–12 to 24.3 per cent in 2017–18, measured as a proportion of GDP, and an equivalent decline in the share of consumption. Over the same period – that is, between 2011–12 and 2017–18 – average investment expenditure stood at 36.9 per cent, even though it has declined marginally over the past two years. There is a wide and persistent gap (averaging –15.7 per cent between 2011–12 and 2017–18) between the domestic savings rate and the rate of gross capital formation, which may be unsustainable over the longer term (National Bank of Ethiopia, 2019; Planning and Development Commission, 2019). This also confirms that investment has largely been funded by external capital in the past decade.

2.2 The macroeconomic framework in Ethiopia

The stated goals of macroeconomic policy in Ethiopia, as articulated in the GTP-II, are “sustaining rapid and inclusive economic growth within a stable macroeconomic environment, including maintaining a stable and low inflation, ensuring structural transformation in the economy, consolidating the gains in human development and reducing poverty and unemployment; as well as enhancing the share of investment and domestic saving in GDP” (Federal Democratic Republic of Ethiopia, 2016, p. 98). Monetary and exchange rate policy are intended to ensure stable inflation, drive increased production and employment, and ensure price stability “by enhancing productivity and competitiveness of the economy” (ibid.). Fiscal policy aims to increase domestic revenue mobilization, maintain the fiscal deficit at sustainable levels, and manage public debt within a stable macroeconomic environment.

Two, not fully compatible perspectives usually inform macroeconomic policy. The first, often associated with international financial institutions such as the IMF and the World Bank, argues that the central focus of governments and central banks ought to be preventing inflation and fiscal deficits (Weeks, 2015). The second perspective is developmental and broadens the objective of macroeconomic policies to also include economic growth, employment targets, and distributional dimensions. Policy-makers in Ethiopia have hewn closer to the second approach but have combined (sometimes contradictory) elements from

¹⁸ This is dealt with in much greater detail in Sections 4 and 5.

different growth models (including those of East Asian countries), rather than following conventional macroeconomic prescriptions from donors (Kelsall, 2013; de Waal, 2018).

2.2.1 Monetary and exchange rate policies

Between 2011 and 2016 the Ethiopian government invested heavily in large infrastructural projects to boost competitiveness. Since 2016 it has begun to pursue a strategy of fiscal consolidation, worried by the widening fiscal and current account deficit (IMF, 2016). Within this cautious macro-outlook, the National Bank of Ethiopia (NBE) has sought to maintain inflation at a low single-digit level, especially by controlling the growth in “reserve money”¹⁹ in the economy over the past two years. As part of its relatively tight monetary policy, the NBE also limited credit expansion schemes to sectors other than exports and manufacturing in the fiscal year 2017–18. Although this ought to have been manifested in constrained domestic lending to firms and individuals, it does not appear to have had this effect, perhaps due to the increasing sophistication of the Ethiopian financial system. It is worth noting that the NBE does not pursue either economic growth or employment targets as explicit targets of monetary policy.²⁰

Historically, inflation in Ethiopia has been driven largely by food-price inflation, which, in turn, has been largely driven by weather fluctuations (Figure 2.4). This trend is particularly visible in years in which inflation increased drastically – for instance in 2008–09, when it jumped to 36.4 per cent. More recently, in end-2017/early-2018, inflation surged to double digits as a result of a one-off devaluation of the birr against the US dollar in October 2017, expansion of public sector credit in 2017, growth in broad money,²¹ and political disruptions (which adversely affected distribution networks). After peaking at 16.8 per cent in June 2018, inflation declined to about 10.8 per cent in early 2019 (World Bank, 2019a, p. 12). The tighter monetary policy adopted by the NBE appears to have been in response to these more recent drivers of inflation. During periods of high inflation in the past, the government has also waived applicable taxes, for example, to ease imports of food and other basic commodities, while trying to reduce the budget deficit and delaying major new infrastructure projects (Manyazewal, 2019).

The NBE maintains a managed float exchange regime, in theory allowing gradual depreciation of the birr against the US dollar (NBE, 2018, p. 2). In practice, although it did permit a one-off 15 per cent devaluation in October 2017, it has kept the exchange rate relatively constant in recent years. In the fiscal year 2017–18, for instance, the birr was allowed to depreciate only by about 3 per cent against the US dollar. As a result, the gap between the official and parallel market exchange rates remains wide, with the market rate for US dollars being much higher than the official rate, sometimes by as much as 30 per cent (World Bank, 2019a, p. vii). Data from the NBE (2018) show that the Real Effective Exchange Rate (REER) Index increased significantly between 2010–11 and 2017–18, that is, up to the one-off depreciation mentioned above.²² An increase in the REER implies that

¹⁹ Reserve money or the monetary base comprises central bank liabilities that support the expansion of credit and broad money. It is defined by the IMF (2017, p. 197) to mean currency in circulation, other deposit taking institutions’ (largely commercial banks) deposit holdings at the central bank, and deposits of money-holding sectors (including local governments) at the central bank.

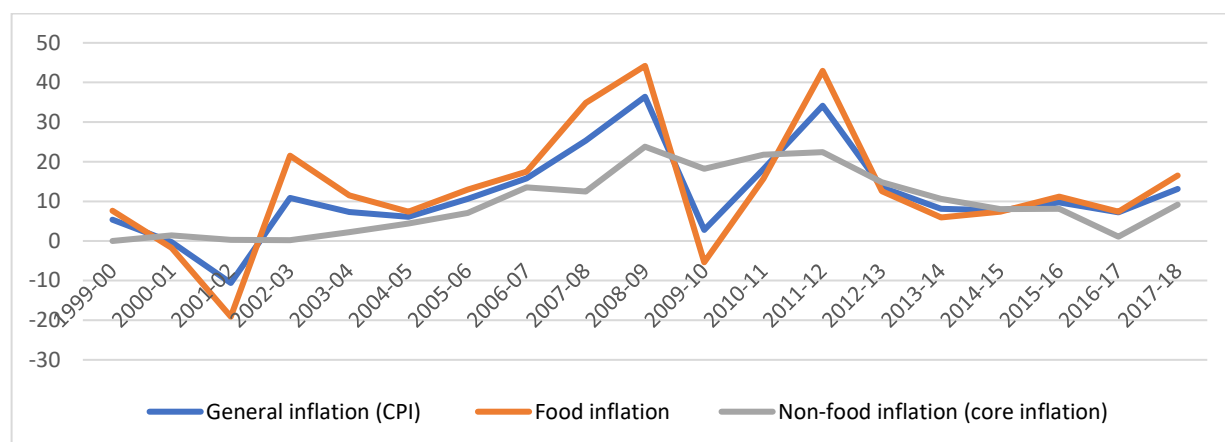
²⁰ Authors’ interviews with the Planning and Development Commission, formerly the National Planning Commission (May 2019).

²¹ This refers to the money supply in a country, that is, it is the sum of all liquid financial instruments held by money-holding sectors that are widely accepted in an economy as a medium of exchange, plus those that can be converted into a medium of exchange at short notice at, or close to, their full nominal value (see IMF, 2017, p. 180).

²² The REER refers to the value of the Ethiopian birr against a weighted average of several foreign currencies divided by an index of costs, in this case the consumer price index.

exports become less competitive and imports become cheaper, a loss in trade competitiveness. In short, the Ethiopian birr remains overvalued.

Figure 2.4. Average annual inflation rate (CPI growth rate), calculated using base year December 2011 = 100 (percentages)



Source: National Bank of Ethiopia (2019).

While substantial short-term exchange rate fluctuations can have a depressing effect on investment by both domestic and international businesses, maintaining a moderately undervalued exchange rate has proven effective in increasing competitiveness in many Asian countries. Some degree of exchange rate flexibility (that is, allowing depreciation to make the currency moderately undervalued, even while staying within the current managed exchange rate regime) and liberalization of the current account might help strengthen competitiveness, reduce foreign exchange shortages, and support reserve accumulation in the Ethiopian context.

2.2.2 Revenue and taxation; fiscal policy

At 13 per cent of GDP, public revenues in Ethiopia are well below the sub-Saharan African average (16 per cent) and inadequate for a developmental state. Tax collection has been hampered in recent years by political disturbances and, more generally, by lacunae in the tax administration process. Increasing tax revenues is a central focus of the government, especially because domestic revenue has declined from a high of 14.8 per cent as a share of GDP in 2015–16, to 12.2 per cent. As a result, the tax policy directorate in MOFED is actively reviewing ways in which this can be achieved.

Import tariffs, in particular, make up a very large share (nearly a quarter) of total fiscal revenue. The fall in fiscal revenues relative to GDP in recent years has largely been due to falling revenues from imports. In turn, this may also be closely tied to the reduction in tariffs and in public sector imports in the past few years. If a rapid trade liberalization or other regional/international trade integration were to take place, revenue losses from foregone import tariffs would prove to be a major challenge for government revenue collection.

2.2.3 Government expenditure and public debt

As part of Ethiopia's current prudent macroeconomic stance, the government has made significant efforts to reduce its deficit by reducing public sector imports, non-concessional borrowing by state-owned enterprises (SOEs), and infrastructure spending. At the same time, efforts continue to improve tax collection, albeit with limited success, after disruptions caused by political protests. Notably, pro-poor spending has been ring-fenced; this forms about two-thirds of the budget (or around 5 per cent of GDP) and includes health, education,

agriculture, roads, and food security.²³ The government has also resorted to using “supplementary budgets” to fund various social programmes, including the “youth revolving fund”, which is meant to help promote the development of micro, small, and medium enterprises (discussed below). The budget deficit is currently just over three per cent of GDP and is projected to increase slightly over the short term.

Public debt is well under 60 per cent of GDP and has remained stable for the past few years as a proportion of GDP: in 2017–18, it stood at 54 per cent of GDP. It is split almost equally between domestic and external debt (in the ratio 45:55). Interest rates on public debt are relatively low, although debt service payments on external debt have risen quite sharply in the past few years (partly because of the devaluation of the birr) and continue to rise (Ministry of Finance, 2018, p. 30). The domestic debt market is fairly underdeveloped and consists of direct advances, treasury bills, government bonds for central government and corporate bonds, long-term and short-term loans for state-owned enterprises (SOEs). The government uses direct advances from the NBE and the issuance of treasury bills to financial institutions at well below market interest rates to finance gaps in its budget (IMF, 2018a). While there was an expansion of borrowing, including on non-concessionary terms, at the height of the construction boom, the Ethiopian government has now imposed stringent controls on external borrowing by the public sector, including SOEs, especially on non-concessionary terms. As a result, all borrowing in FY 2018 by SOEs was from domestic banks (National Bank of Ethiopia, 2018).

It is difficult to get a true picture of public debt in Ethiopia because fiscal reports do not cover extra-budgetary accounts or the operations, including borrowing, of SOEs. That said, debt sustainability analyses conducted by the IMF in 2016 and 2017 (IMF, 2017b) noted that, although public and publicly guaranteed debt were broadly sustainable and that external public sector debt was not high compared with similar countries, government debt amounted to about 351 per cent of export revenues, and the debt servicing ability of the government depended heavily on the export of goods and services (IMF, 2018b).

2.3 Policies on industrial development and the business environment

Ethiopia has pursued active industrial policies since the early 2000s, and has adopted a policy mix aimed at promoting exports and productive investment, import substitution and protection of key sectors, industrial financing, and the use of SOEs to shape strategic sectors. The sectoral focus has been on leather and leather goods, apparel and textiles, meat processing, food processing and beverages, cement and steel, and horticulture. Despite the strategic focus on manufacturing, including financing on preferential terms, it is still far from being an engine for growth and economic transformation, and plays a relatively marginal role in employment creation, output, exports, and in building technological capability. Recent policy changes have yielded positive results in some sectors, such as horticulture, but these are far from universal.

A major plank of Ethiopia’s strategy has been the development of industrial parks. These are intended to attract FDI to help spur export-oriented manufacturing. This strategy has not yet been completely successful, largely because it has been quite difficult to create linkages between domestic manufacturing and exporting firms. Sometimes the problem is simply geographical: exporting firms are often set up in industrial parks where there are few (if any) domestic firms (Zhang et al., 2018). In 2016, in fact, only 4.5 per cent of manufacturing firms were estimated to be exporters (Oqubay, 2019a; Oqubay, 2019b). The

²³ In 2017–18 poverty reducing expenditure amounted to about 5 per cent of GDP, up from 4.3 per cent in 2014–15. IMF (2018a).

remainder of this sub-section touches on the business environment in Ethiopia, issues around access to credit, and the patterns of foreign direct investment (FDI).

2.3.1 The business environment

Ethiopia ranked 159th among 190 countries in the World Bank's Doing Business Report 2019, with its lowest ranking in the categories of Protecting Minority Investors and Getting Credit (World Bank, 2019d). Ethiopia ranked 29th out of 44 Sub-Saharan countries in Doing Business. Its ease of doing business score has improved marginally between 2016 and 2019, while its rank has remained largely static over time. Its rank has not improved between 2017–19 on most indicators but has actually deteriorated in some cases (See Figure 2.5). Among these, notably, are getting credit, getting electricity, and registering property. These findings are corroborated by the World Bank's Enterprise Surveys (2015) where respondents noted that obtaining access to credit was the most important challenge faced by most businesses.

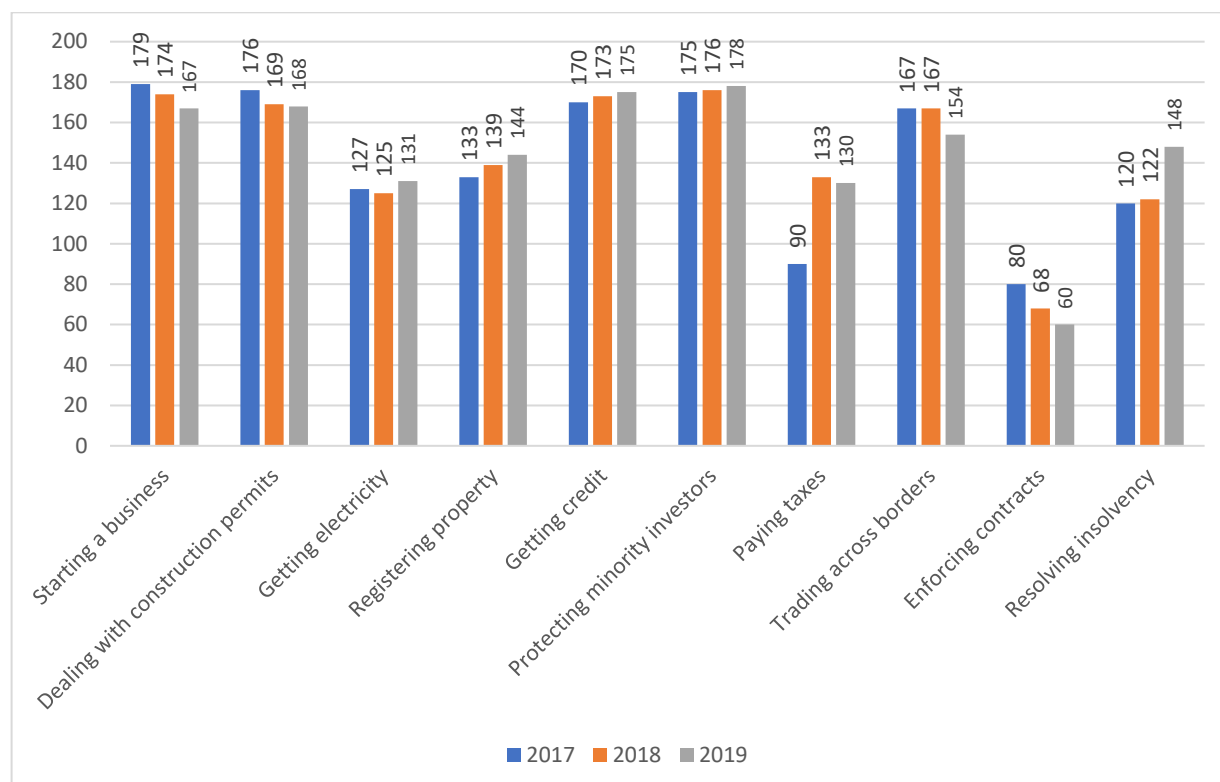
Major constraints faced by businesses today include access to (i) foreign exchange, which can result in delays of between six weeks and three months for business processes, and can lead to the slowing down of manufacturing where inputs are being imported; (ii) credit availability for smaller firms (which lack collateral); (iii) high turnover of workers; and (iv) lack of skilled labour.²⁴

Unsurprisingly, the business and regulatory environment affects men and women in different ways. For instance, women are less able to access credit than men, or have access only to smaller amounts, which limits their earnings and their ability to grow their business (World Bank, 2019c, p. 30). Women also hire fewer workers than men, probably because of the challenges that they face in expanding their enterprises. Women are more likely to operate without business licenses, and, largely because of social norms around domestic work, spend less time on business activities than men (ibid.). Recognizing these general and gender-specific constraints, the Ethiopian government launched a national initiative in late 2018 to try to improve the ease of doing business, including easing the processes around starting a business, getting electricity, access to finance, and paying tax.

It is interesting that a large number of complaints refer to the lack of capital, but there are few complaints about lack of managerial competence. At least for micro and small enterprises low levels of education and management competence are likely to be a major reason behind their failure to graduate from small family businesses to something bigger.

²⁴ Authors' interviews with employers organizations: the Ethiopian Employer's Federation and the Ethiopian Employer's Confederation (May 2019).

Figure 2.5. World Bank Doing Business Rankings – 2017–19 (scores range from 1=best to 190 = worst)



Note: The data are collected in a standardized way, based on a questionnaire administered to local experts, including lawyers, business consultants, accountants, freight forwarders, government officials and so on, who routinely administer or advise on legal and regulatory requirements. The surveys have five major limitations, however: (i) collected data refer to businesses in the largest business city, which may not be representative of the economy; (ii) the data collected focus mostly on limited liability companies; (iii) the issues cited in the report refer to a standardized set, and may not actually encompass all the issues faced by a company; (iv) where an indicator is expressed in terms of time – for example, the time required to start a business – there is a measure of subjectivity; and (v) the methodology assumes that a business has full information on what is required and does not waste time when completing procedures.

Source: World Bank (2019d).

2.3.2 Access to credit

Domestic credit in Ethiopia has expanded rapidly in recent years, and in fact has been one of the primary drivers of the growth in “broad money” in Ethiopia’s economy. The average growth rate of credit has been as high as 31.6 per cent per year for the past eight years and the credit-to-GDP ratio has increased, from 0.19 in 2008–09 to 0.31 in 2017–18 (National Bank of Ethiopia 2019; Planning and Development Commission 2019). However, credit to the private sector remains a much smaller share of domestic credit than is desirable for the promotion of private enterprise: it stood at 36.9 per cent in 2017–18. In other words, there remains a risk that public borrowing and borrowing by state and quasi-state enterprises may crowd out private sector borrowing. Even in 2017–18 some 63 per cent of outstanding loans were owed by the government and SOEs (13 and 50 per cent, respectively).

Over the past eight years, increased lending to the industry, transport and communication, mines, power, and water sectors means that their share of credit has been consistently high (see Table 2.2). Credit growth to the agricultural sector, on the other hand, has been anaemic: in 2017–18, the share of credit to agriculture was a paltry 2.8 per cent, down from 8.7 per cent eight years ago.

Table 2.2. Share of credit by sector %)

Sector	Share (2009–10)	Share (2015–16)	Share (2017–18)
Agriculture	8.7	4.5	2.8
Industry	15.7	23.5	22.6
Domestic trade	8.0	6.3	6.6
International trade	18.5	11.5	11.4
Hotels and tourism	1.6	1.1	1.4
Transport and communication	3.6	5.6	6.3
Housing and construction	19.5	12.9	13.0
Mines, power, and water	21.3	31.8	31.6
Others	2.9	2.3	3.4
Personal	0.3	0.6	1.0

Source: Planning and Development Commission (formerly the National Planning Commission), 2019.

The development of the microfinance (MFI) sector in Ethiopia has been robust, but has yet to play a significant role in facilitating access to finance for micro and small engineering enterprises. As of the second quarter of 2019, there were 38 MFIs operating in Ethiopia, which had mobilized cumulative savings of birr 33.9 billion, 19.5 per cent higher than 2017–18. The sector is growing rapidly.

2.1.1 Foreign direct investment

As noted in Section 1, Ethiopia’s recent economic policies focus on FDI-driven, export-focused manufacturing as an engine of the economy. Net FDI inflows have fluctuated between lows of 2.5 per cent of GDP (in 2014–15) and 5.2 per cent (in 2016–17).²⁵ FDI declined to US\$3.7 billion, or 4.4 per cent of GDP, in 2017–18, due largely to political unrest. The top five countries of origin for FDI are China, India, Sudan, the United States, and Turkey (not counting joint ventures). FDI is concentrated in manufacturing, which has received three-quarters of the total, with much lower levels of FDI flowing into construction (10 per cent) and agriculture (seven per cent). It is also regionally concentrated, with nearly 80 per cent going to Addis Ababa and the Oromia region. The Ethiopian government does provide some fiscal incentives to draw investment into other regions, but so far these policies have had only limited success.

2.4 Trade

Ethiopia’s trade policies do not exist in the form of a single document; rather, they are integrated into other policies, strategies, and programmes. The overarching goal of trade policies is to facilitate structural transformation, in which these policies have only been partially successful.²⁶ While the scope of this chapter does not permit an extensive analysis, some broad remarks on trade policy follow from the macroeconomic analysis contained in previous sub-sections.

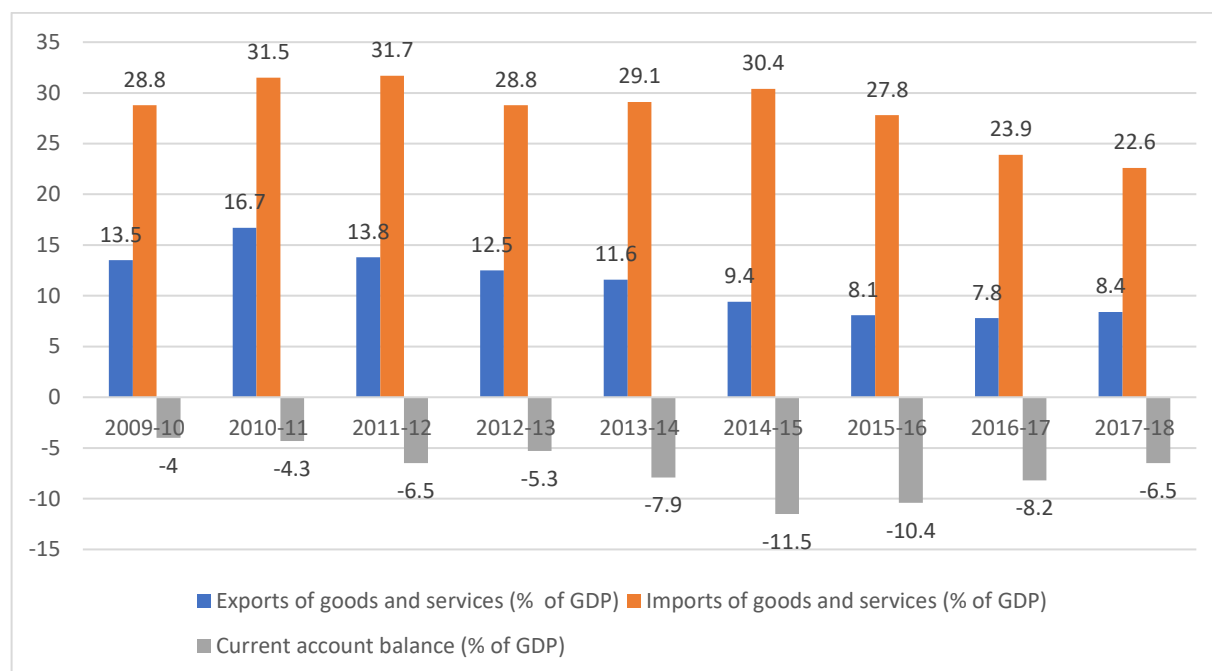
Following a long period of balanced trade, Ethiopia began registering increasing current account deficits after 2010, largely as a result of the rapid expansion of public

²⁵ This section draws heavily on data received from the Ethiopian Investment Commission.

²⁶ Authors’ interviews with the Trade Directorate, Ministry of Trade and Industry, May 2019.

investments in infrastructure. More recently, the deficit has been brought down somewhat to approximately six per cent of GDP in the first quarter of 2019, following reduced public investment spending. While the current account deficit is admittedly large, consumer goods are a minor part of all imports. Raw materials, energy, capital, and intermediate goods make up the bulk of imports, suggesting that imports are in fact being used to facilitate export of goods in the future (see Ghosh and Ramanathan, 2018).

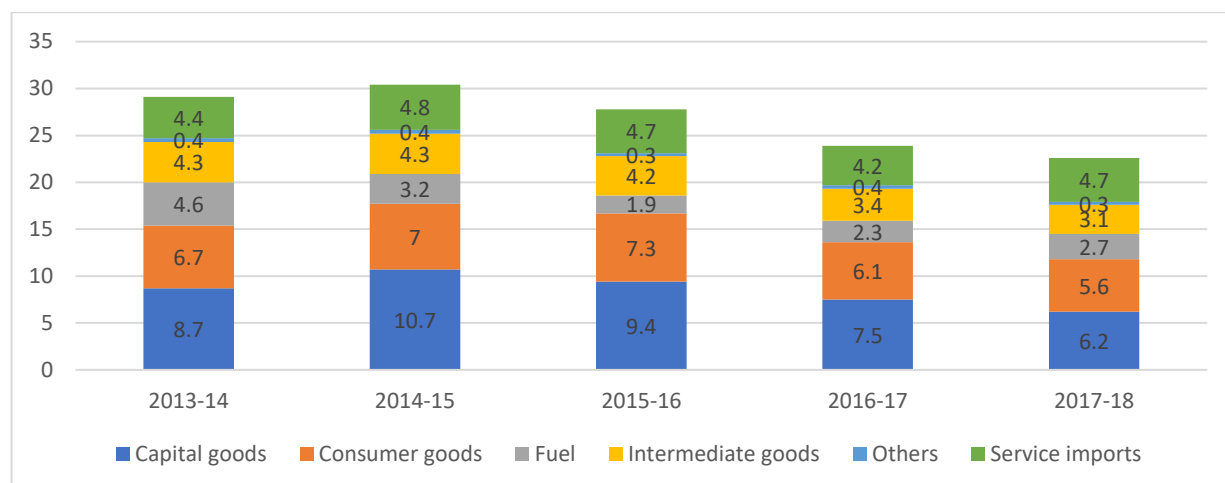
Figure 2.6. Exports and imports of goods and services (% of GDP)



Source: World Bank (2019a).

In recent years, the export of services (driven largely by Ethiopian Airlines) has outpaced the export of goods, which has declined largely due to low commodity prices, especially that of coffee. In fact, the expansion of exports by around 13 per cent reflects the improved performance of Ethiopian Airlines. Coffee represents 30 per cent of goods exports and decreased by five per cent in FY2018, mainly because of a drop of more than 10 per cent in coffee prices. Other export increases were recorded in the leather, textile and garments, chemical, and electricity sectors, reflecting (at least in part) the increasing contribution of new industrial parks. Manufacturing exports are at about US\$ 2.9 billion, far below the government's target of 7 billion, reflecting structural issues, including, as discussed, an overvalued exchange rate. Total exports of goods and services do not exceed 10 per cent of GDP.

Figure 2.7. Structure of imports (% of GDP)



Source: World Bank (2019a).

Despite efforts to promote export-oriented manufacturing, exports remain dominated by agricultural products. Coffee accounted for 45 per cent of total exports in 2000–01 and, at 30 per cent, was still the most important export good in 2017–18. In 2015–16, the top five exporting goods were coffee, oilseeds, gold, chat and pulse. These five exporting goods accounted for 77 percent in 2000–01 and almost 70 per cent of the total exports in 2015–16, suggesting there have been little changes in the structure of exports over the last ten odd years. However, cut flowers have emerged as a major success story in recent years and accounted for 8 per cent of total exports in 2017–18. Export of services, notably air travel, has also become quite significant. By contrast, textiles still accounted for less than 5 per cent of total exports in 2017–18 (NBE, 2019).

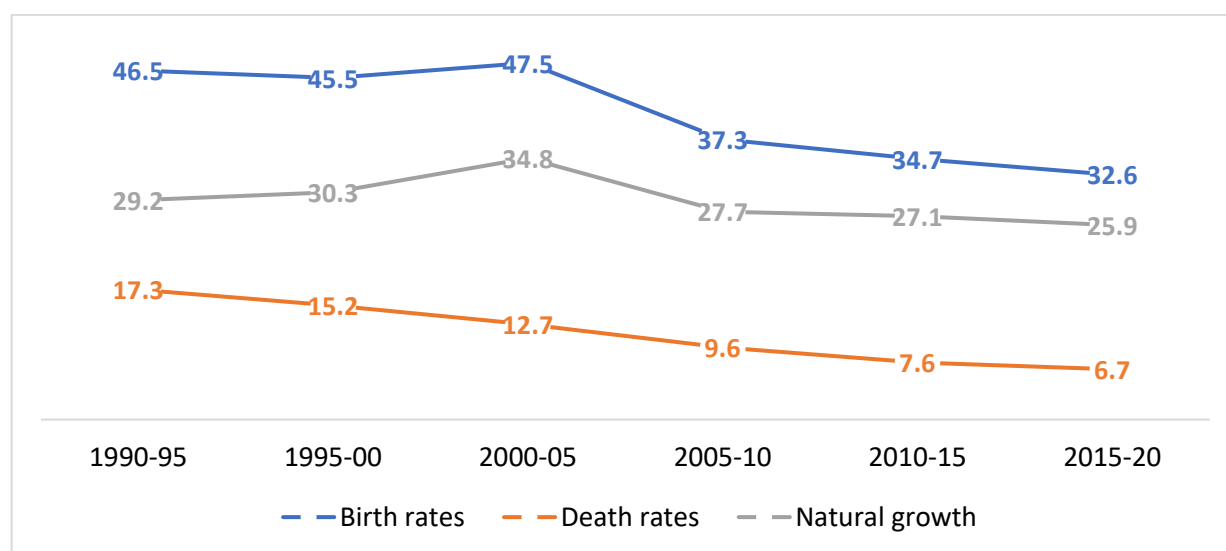
Still, it must be concluded that international trade in general and exports in particular still play a relatively minor role in Ethiopia’s economic development. There is therefore a continued need to rely on domestic demand growth, at the same time as increasing exports and broadening the export base. Focusing solely on export growth is likely to be counterproductive because of the low numbers and small export base.

3. Demographic dynamics and human resource development

3.1 Demographic dynamics

Ethiopia is in the midst of a demographic transition, with a still young and rapidly growing population. Improved health and living conditions have brought down under-five mortality rates from 190 per thousand in 1990–95 to an estimated 55 per thousand in 2015–20 (World Population Prospects 2019). Death rates have similarly fallen significantly, from 17.3 to 6.7 per thousand over the same period (Figure 3.1). Population growth increased in the 1990s as a result of sustained very high birth rates, combined with falling death rates and peaked at almost 3.5 per cent per year in 2000–05. Falling birth rates since 2005 have resulted in a gradual fall in the rate of growth of the population to slightly below 3 per cent per year in 2015–20 and are expected to fall further to around 2.3 in 2030 (Table 3.1).

Figure 3.1. Development of crude birth and death rates and natural growth (per thousand)



Source: World Population Prospects (2019).

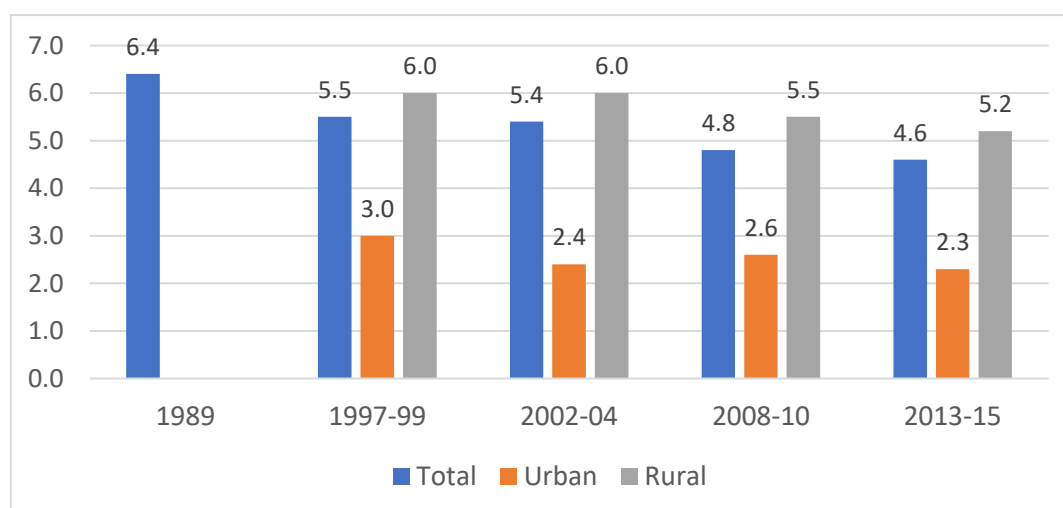
Falling birth rates have translated into a gradual shift of the age structure. The share of children (aged under 15) in the population has fallen from 46.5 to 39.9 per cent in the past two decades and will continue to fall slowly, while the share of the working age population (aged 15–64) has increased from 50.4 to 56.5 per cent. This has resulted in a significant improvement of the age-based dependency ratio, from 98 in 2000 to 77 in 2020 (Table 3.1). Ethiopia is currently about half-way through the so-called demographic window of opportunity. To fully benefit from this demographic tailwind, however, the country needs to create productive employment opportunities at a very fast pace to meet the needs of a rapidly growing labour force. Over the past decade (2010–20) the working age population has grown by more than 3.6 per cent per year, that is by almost 2 million per year. Although the growth rate will slow down in coming years, the working age population will continue to grow by an expected 2.2 million per year between 2020 and 2030. It is against this backdrop of sustained huge supply pressure on the Ethiopian labour market that the challenges of achieving the Sustainable Development Goal of full and productive work for all should be seen. This challenge is greatly exacerbated by the fact that Ethiopia remains a profoundly agrarian economy in which a major part of a rapidly growing population and labour force are confined to deriving their livelihood from a finite amount of agricultural land.

Table 3.1. Demographic dynamics

	2000	2010	2020	2030
Total population, 1 000	66 225	87 640	114 964	144 944
Age distribution, %				
Less than 15	46.5	44.9	39.9	36.3
15–24	19.4	20.0	21.5	19.1
25–64	31.0	31.8	35.0	40.8
15–64	50.4	51.8	56.5	59.9
65+	3.1	3.3	3.5	3.8
Dependency ratio (0–14 + 65+)/15–64	98.3	93.2	76.8	67.1
		2000–10	2010–20	2020–30
Population growth, % CAGR		2.84	2.75	2.34
WAP growth, % CAGR		3.12	3.65	2.94

Source: World Population Prospects 2019 <https://population.un.org/wpp>

At the heart of the demographic dynamics is a fall in fertility. The total fertility rate (TFR) fell from an average of 6.4 children per woman in 1980 to 4.6 children per women in 2013–15 (Figure 3.2). The aggregate fall in fertility at the national level masks large variations. Rural women have, on average, more than twice as many children as those living in urban areas. In rural areas fertility has fallen slowly and remains very high, at 5.2 (Figure 3.2), suggesting that population pressure on land will continue to increase in the foreseeable future. Regional differences in fertility are also very large, ranging from a total fertility rate of 7.2 in the Somali region to a mere 1.8 in Addis Ababa in 2013–14.

Figure 3.2. Total fertility rates by rural and urban areas

Source: DHS (2000), 39; DHS (2016), 77–78.

There is a very close interrelationship between education, fertility, and wealth, in Ethiopia as elsewhere. Fertility falls sharply with increased levels of education, as well as with increased household consumption (Table 3.2). The total fertility rate among women with no formal education stood at 5.7 in 2013–15, but fell to 4.2 for those with primary education and to a mere 2.2 among women with secondary education. The difference in fertility between the poorest and the richest household quintiles is similarly stark. While the correlations between these three factors may well be complex and multidirectional, it is clear that education is important to bring down fertility, that education and fertility have a strong

bearing on household incomes and poverty, and that the economic status of a household has a significant impact on the educational possibilities and performance of children.

Table 3.2. The education–fertility–wealth nexus, 2013–15

	Total fertility rate
Education of women	
None	5.7
Primary	4.2
Secondary	2.2
Above secondary	1.9
Household consumption quintile	
Lowest	6.4
Second	5.6
Third	4.9
Fourth	4.3
Fifth	2.6

Source: DHS (2016). 77–78, 84.

3.1 Development of human resources

The first comprehensive government policy on education and training was issued in 1994. The policy identified access, quality, equity, and relevance as the main challenges of the education system. In practice, however, expanding access and equity were prioritized over quality and relevance. Consequently, there was a rapid quantitative expansion of education, partly motivated by the need to meet the globally agreed target of universal primary education under the MDGs by 2015 (Rekiso, 2019). The current policy framework stresses the need to match education supply to demand, generally, but especially in the context of TVET.²⁷ In addition, a TVET Strategy (2008) governs TVET and is also focused on providing skills and demand-driven training. In practice, however, the curricula for neither tertiary education institutions nor for TVET institutions is demand driven.

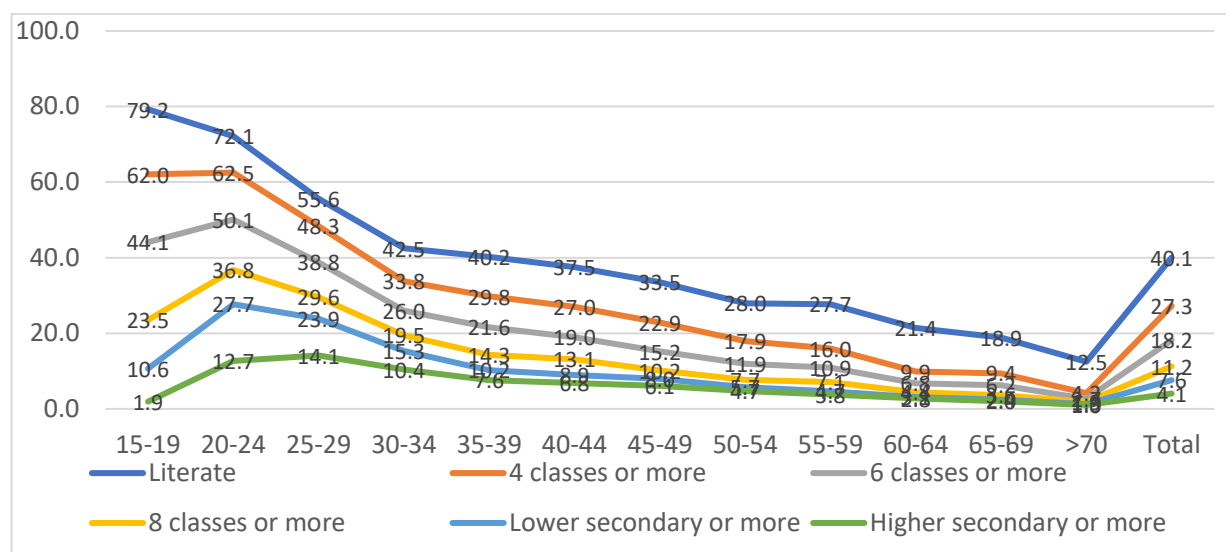
Endemic extreme poverty and very large cohorts of school age children make increasing education levels an uphill battle in Ethiopia. Yet, the past 10 to 15 years have seen major advances in education, albeit from very low levels. The share of the adult population that had completed at least four years of education increased from 14 to 27 per cent between 2004 and 2016. By 2016 some 18 per cent had completed 8 years of primary education and 11 per cent had at least lower secondary education, more than double the rates registered in 2004 (HICE, 2004; HICE, 2016).

Education levels fall sharply with age, reflecting the development of the education system over time (Figure 3.3). Hence, the young cohorts in the labour force are much better educated than the older ones. For instance, by 2016 almost two-thirds of the 20–24 age group had completed at least four years of primary education, compared with only 10 per cent among the 60–64 year olds; 37 per cent had completed at least eight years of primary education; and 28 per cent had at least lower secondary education (Figure 3.3). Levels of education fall sharply as one moves from the 20–24 to the 30–34 age group. Thereafter the levels of education fall much more slowly from one age group to the next, reflecting the major

²⁷ https://planipolis.iiep.unesco.org/sites/planipolis/files/ressources/ethiopia_esdp_v.pdf

advancements in education that have taken place in the past 10 to 15 years, but also the poor state of education over the decades leading up to the Millennium.

Figure 3.3. Completed levels of education by age groups, 2016

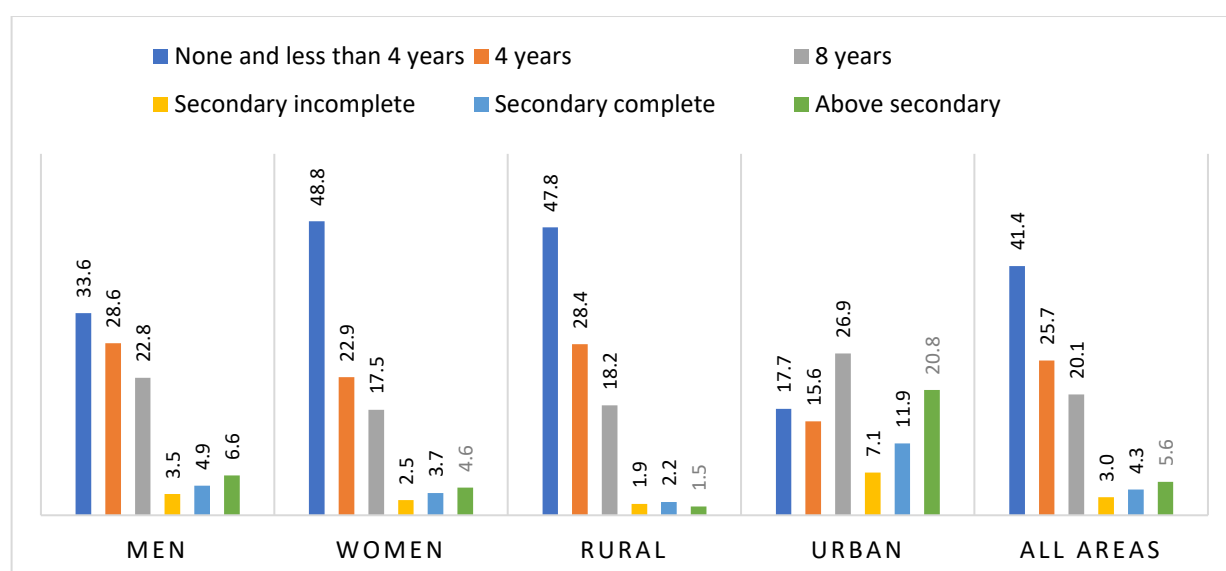


Notes: Lower secondary school covers classes 9–10 and upper secondary school classes 11–12. Figures refer to the population aged 15+.

Source: HICE (2016b). Authors' calculations.

There are major differences in literacy rates and education levels between rural and urban areas, between men and women, and across household expenditure quintiles (Figure 3.4). In rural areas less than half the population was literate in 2016 compared with more than four out of five in urban areas. Female literacy rates are consistently lower than those of men in both rural and urban areas, by approximately 20 percentage points. Differences in literacy rates across household expenditure quintiles are also marked, in particular in urban areas.²⁸

Figure 3.4. Levels education by sex and area in 2016 (%)

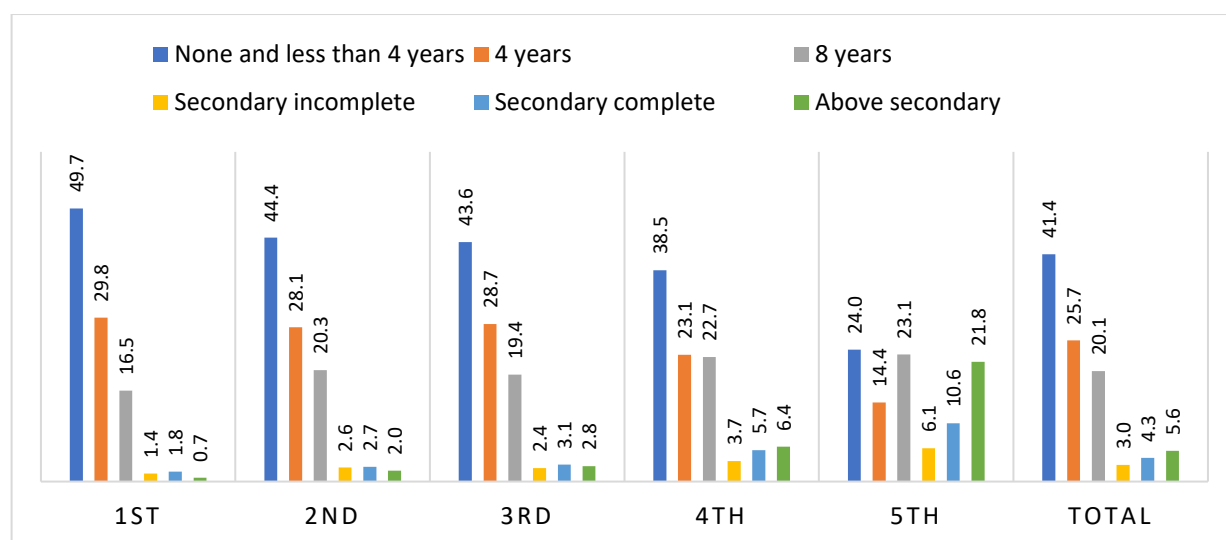


Source: HICE (2016a), Table A10.

²⁸ HICE (2016a), Table A9.

Despite impressive advancements in education over the past 10 to 15 years, education levels in rural areas remain very low (Figure 3.4). Almost half of the rural adult population had not even completed four years of primary education in 2016, more than three out of four had at most four years of primary education, and a mere 5.6 had more than eight years of primary education. These figures contrast sharply with the urban scene where “only” a third of the population had at most four years of primary education and almost 40 per cent had more than eight years of primary education. Gender-based differences in education also remain large. A third of all men, but almost half of all women had not completed four years of primary education in 2016 (Figure 3.4).

Figure 3.5. Levels of education by household expenditure quintiles in 2016 (%)



Source: HICE (2016a), Table A10.

As one would expect, education levels increase with household economic status (Figure 3.5). This increase is far from uniform, however. The differences across the lowest four quintiles are rather small, while the richest quintile stand out with significantly higher levels of education. A plausible explanation is that the highest quintile is largely resident in urban areas.

Shifting the focus to the recent performance of the education system, it is obvious that the young generation enters working life much better equipped with formal education than earlier generations. However, the educational system still falls far short of providing full and equal access to adequate education.

The education system currently provides for eight years of universal primary education free of charge, the first six years of which are compulsory. This can be followed two years of lower and two years of higher secondary education, the successful completion of which is a prerequisite for accessing tertiary education. Branching off from secondary education there is also a vocational training stream lasting two to three years in the fields of teacher training, commerce, technology, agriculture, and military training.²⁹

Despite being both free and compulsory, far from all children pursue, let alone complete, primary education. In 2016, the net attendance rate for primary education was a mere 71 per cent and 22 per cent of those aged 9 to 12 had never been to school (Table 3.3). Less than half of all children completed primary education, suggesting very high drop-out

²⁹ www.scholaro.com/pro/countries/Ethiopia/education-system (accessed August 2019).

rates and implying that at least half of the subsequent young entrants into working life are very poorly equipped in terms of basic education.

Approximately four out of five children do not pursue any education beyond the primary level. In 2016, some 21 per cent of young people had completed lower secondary education and 13 per cent had completed higher education, as the net attendance rate fell from 71 per cent in primary education to a mere 18 per cent in secondary education.

Table 3.3. Educational characteristics by sex and rural and urban areas, 2016 (%)

	Total	Female	Male	Rural	Urban
Never been to school, aged 9–12	22	21	23	24	6
Out of school, primary level	32	32	32	34	14
Net attendance rate, primary	71	72	71	70	83
Net attendance rate, secondary	18	18	18	12	42
Primary completion rate	47	48	46	39	79
Lower secondary completion	21	22	20	11	58
Higher secondary completion	13	12	14	5	41

Source: World Inequality Data Base on Education (2019); HICE (2016a), p. 29.

There are impressive achievements in terms of gender parity in access to education. By 2016 almost all indicators suggested that the educational attainments of girls were at least on a par with those of boys (Table 3.3). This is indeed a major achievement considering the wide gender disparities in access to education in the past.

Rural–urban disparities, as well as disparities between poor and better-off households remain very wide, however. A rural child is four times more likely never to go to school than a child in an urban area and four out of five urban children complete primary education compared with only two out of five rural children. The rural–urban education gap increases at higher levels of education. Almost six out of ten urban children complete lower secondary education compared with little more than one out of ten rural children and the chances that an urban child will complete higher secondary education is eight times higher than for a rural child (Table 3.4). There are also major differences between rural and urban areas with regard to the quality and relevance of education. A World Bank study on secondary education in Ethiopia found large disparities between the quality and relevance of education in urban and rural areas (Joshi and Verspoor, 2013). Studies have found that differences in quality (measured by scores in vocabulary and mathematics tests) of education begin at an early age and persist through the schooling period (Woldehanna and Araya, 2016, pp. 44–45).

Table 3.4. Educational characteristics by household expenditure quintiles, 2016 (%)

	1 st	2 nd	3 rd	4 th	5 th	Average
Never been to school, 9–12	39	26	21	16	7	22
Out of school, primary	47	36	31	25	15	32
Net attendance rate, primary	57	67	75	77	84	71
Net attendance rate, secondary	6	7	12	18	37	18
Primary completion rate	25	30	39	48	76	47
Lower secondary completion rate	4	7	9	17	55	21
Higher secondary completion rate	2	2	4	8	36	13

Source: World Inequality Data Base on Education (2019); HICE (2016), p. 29.

Poverty is a major obstacle to accessing education. Four out of ten children from the poorest household quintile have never been to school compared with fewer than one out of ten children from the richest quintile.³⁰ Only a quarter of the children from the poorest households complete primary education (Table 3.4). This suggests that there is a very high probability that poverty will be transmitted from one generation to the next as basic education is fundamental for accessing productive employment. Access to secondary education is still largely for children from the richest households. More than half of the children from the richest household quintile complete lower secondary education, and more than a third also complete higher secondary education, compared with only a small proportion of the children from the poorest 60 per cent of households.

The rapid improvements in education in the past 10 to 15 years can be ascribed largely to (i) a sustained high priority given to the development of education and (ii) sustained high economic growth, which has much increased financial and fiscal space to invest in education. Public expenditure on education has oscillated between 20 and 25 per cent of total public expenditures and between 4 and 5 per cent of GDP over the past decade.³¹ Hence public expenditure has increased in pace with GDP, that is by slightly over 10 per cent per year in real terms over the 2007–2017 period.

Public expenditure on education has been channelled primarily to primary and tertiary education. Ethiopia boasts one of the more distinguished academic environments in Sub-Saharan Africa, while elimination of illiteracy and expanding the coverage and quality of primary education has been, and remains, an absolute priority. By contrast, secondary education and TVET have received much less attention. In 2014–15 primary and tertiary education received approximately 40 per cent each of total public expenditure on education, while secondary education and TVET, including teacher training, received a mere 10 per cent each. The dismally low proportion of children who move on to secondary education after completing primary education and the fact that in practice the door to secondary education remains closed to all except children from the richest household quintile can at least to some extent be ascribed to the low priority given to secondary education and is one of several strong arguments for much increased public investment in it.

The system of technical and vocational training (TVET) was established in its current form in 2000. It has subsequently expanded rapidly, from 72,000 students in 2002–03 to 300,000 students in 2016–17 (ILO, 2019, p. 50). The TVET system is dominated by public TVET centres and the expansion is the result of an ambitious strategy to increase employability and remedy skills shortages. Yet, there are real or perceived problems of quality and relevance, partly because the system appears to be supply driven with limited private sector participation. TVET is largely seen as a fallback alternative for students failing to proceed to higher education, and thus to attract mainly less talented and motivated students. This perception is reinforced as employers tend to undervalue TVET graduates, resulting in difficulties in finding waged jobs and low pay (*ibid.*, p. 54). In order to address the image and quality problems plaguing the TVET sector the focus has shifted in recent government strategies from expanding quantity to improving quality and relevance. There is also an increased emphasis on linking TVET to SME development and to make them serve as hubs of technology and skills development for SMEs.

The educational attainment structure (EAS), defined as the share of different educational categories (no education, primary, secondary, tertiary, TVET.) in the labour force, sets the limits and shapes the feasible patterns of a country's technological and

³⁰ It should be noted that there is a correlation between disparities between rural and urban areas, on one hand, and between poorer and better-off households on the other, as the better-off households (in particular it would appear the fifth quintile) are much more likely to be urban than poorer households.

³¹ Government Budget for Sustainable and Inclusive Growth (2017); General Government Finance Data (2005–2010).

structural transformation (Nübler, 2014). Hence, it largely defines the space for productive transformation and industrial policies at any given time. A successful productive transformation requires that strategies for human resource development and education policies are closely coordinated with industrial policies and that they are designed to work in tandem to foster a productive transformation that is both inclusive and sustainable.

Empirical evidence shows that countries with a high share of middle level education have the widest range of options for developing and diversifying manufacturing and for broad-based and inclusive development. Countries with a narrow middle, that is, an EAS shaped like an hour-glass, have limited options for developing a broad manufacturing base and for a broad-based technological development. Instead, these countries tend to develop high-tech niches with weak linkages to the rest of the economy (*ibid.*). That is a development pattern that is neither robust nor, as a rule, inclusive.

The current educational attainment structure in Ethiopia has a broad base at the bottom, a weak middle, and a comparatively strong top, resulting from an elitist education policy in the past and massive investments in broad-based primary education in recent years. Not only is there a narrow middle, but secondary education continues to be dwarfed in terms of funding. Despite an impressive expansion of primary education in recent years, Ethiopia's educational attainment structure still imposes a serious constraint on inclusive development and limits the scope for moving out of the low-technology, low-wage manufacturing segment. To release this constraint, investments in primary education need to be sustained and further expanded in rural areas, while broad-based development of secondary education must receive much more attention, with the aim of making not only primary education but also, over time, secondary education universally available to the young. The balance between general and technical, vocational and professional education at the secondary and post-secondary levels also needs to be revisited and revised as part of a policy to develop TVET into a good option endowing the students with the skills and capabilities needed for accessing jobs as skilled professionals.

Comprehensive efforts are needed to eliminate the severe inequalities in access to education between rural and urban areas and related to poverty. Significantly improving access to education for children from poor families in rural areas stands out as probably the single most important challenge for achieving inclusive economic development.

4. Labour market developments

Section 1 of this chapter has already outlined the broad contours of the employment challenge in Ethiopia: almost 2.8 million jobs need to be created per year to keep pace with the rapidly growing labour force. *But what are the characteristics of the Ethiopian labour market?* This section investigates this question in greater detail.

Three overarching trends emerge from the analysis:

First, the decline in the share of agriculture in economic output has not been accompanied by any similar decline of its share of employment. This is surprising, especially in light of the very high economic growth rates, and indicates that economic growth has mainly been driven by within-sector productivity growth rather than by productivity gains from shifting labour from low to high productivity sectors (structural change) and/or that structural change and growth of non-agricultural sectors has not been employment-intensive.

Second, a shift from own-account farming to non-farm employment associated with economic diversification is made up of two very different processes. The first is an opportunity-driven process that is associated with upward mobility and with a rapid productive transformation and structural change. The other process, however, is driven by economic distress and is supply-driven as the poorer strata of the agricultural population are driven to become agricultural wage workers or take up low-productivity service activities. The latter process is typical of stagnant agrarian economies subject to strong demographic pressure. It seems clear that both processes are simultaneously at work in Ethiopia.

Third, wage data in Ethiopia are contradictory and difficult to disentangle. By one estimate, real wages in urban areas stagnated between 2006 and 2016, a remarkable finding during a period of relatively high GDP growth (World Bank, 2016). Our calculations suggest, however, that average real urban wages increased by almost 7 per cent between 2011 and 2018, although there were major differences across sectors. There may be multiple explanations for this, including high inflation between 2006 and 2011–12 and falling real wages in the public sector prior to 2016. Still, wage data tell only a minor part of the story as only one in 10 employed people work for wages. Ethiopia remains an economy in which a large supply of labour is competing for few jobs.

The analysis in this section suffers from a lack of recent, comprehensive employment data. The latest national labour force survey (LFS) was conducted in 2013 and, prior to that, in 2005. Subsequent labour force surveys (UEUS) cover only urban areas. While the Household Income, Consumption and Expenditure Surveys (HICE) include some employment data, inconsistencies in definitions and methodology make comparisons of data from the two sources hazardous. This section relies primarily on LFS data from 2005 and 2015, supplemented by some later data from the urban UEUSs.

The LFS defines the working age population as the population aged 10 and above, rather than the standard 15–64 or 15+. In view of the high share of young people in the population, this has major implications for a number of indicators, not least the employment and labour force participation rates. Where possible this section presents the data according to both the national and the standard definition of working age.

4.1 Characteristics of labour force participation in Ethiopia

In 2013, the labour force participation rate (LFPR) of those aged 15–64 was 85.6 per cent: 91.2 per cent for men and 80.3 per cent for women, respectively, down from 86.1 per cent in 2005 (Table 4.1). The need for both women and men to work to make a living, in view of low returns to labour and lack of social security, and a tendency to transit from education to work at an early age explain the high LFPR for both women and men,

Table 4.1. Labour force participation (LFP) in Ethiopia, by sex and age (in thousands, except where indicated)

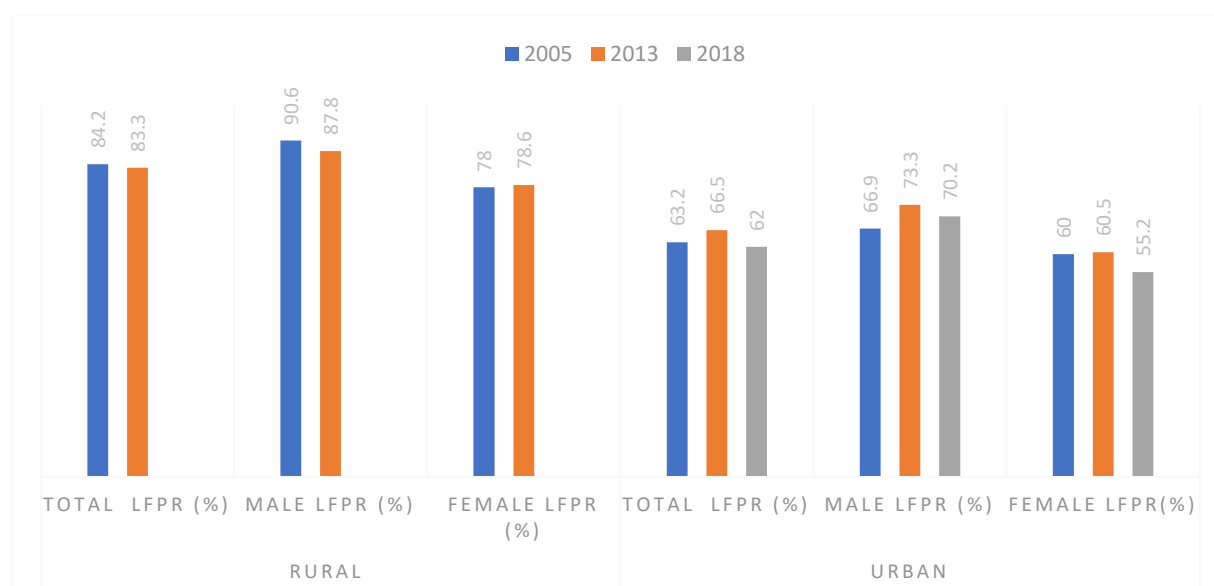
	(A) Working age: 10+			(B) Working age: 15-64		
	Total	Men	Women	Total	Men	Women
2013						
Working age population	55,629.5	27,667.1	27,962.4	41,895.5	20,458.2	21,437.3
In the labour force	44,385.0	23,516.3	20,868.8	35,856.1	18,648.5	17,207.7
Employed	42,404.0	22,886.6	19,517.2	34,030.0	18,087.0	15,943.0
Unemployed	1,981.1	629.6	1,351.5	1,826.1	561.5	1,264.7
Inactive	11,244.5	4,150.8	7,093.7	6,035.1	1,808.6	4,226.5
LFP rate, %	79.8	85.0	74.6	85.6	91.2	80.3
Employment rate, %	76.2	82.7	69.8	81.2	88.4	74.4
Unemployment rate, %	4.5	2.7	6.5	5.1	3.0	7.3
2005						
Working age population	41,018.1	19,908.7	21,109.4	31,384.0	14,850.8	16,533.2
In the labour force	33,088.8	17,288.2	15,800.6	27,021.0	13,633.0	13,387.9
Employed	31,435.1	16,860.3	14,574.8	25,523.5	13,257.5	12,266.0
Unemployed	1,653.7	427.9	1,225.8	1,497.4	375.5	1,121.9
Inactive	7,929.3	2,620.5	5,308.8	4,739.9	1,412.7	3,327.2
LFP rate, %	80.7	86.8	74.9	86.1	91.8	81.0
Employment rate, %	76.6	84.7	69.0	81.3	89.3	74.2
Unemployment rate, %	5.0	2.5	7.8	5.5	2.8	8.4

Notes: Employment and unemployment data use the "current status" approach, that is, it measures economic activity in the week prior to the date of the interview. LFP rate: percentage of working age population who are in the labour force. Unemployment rate: percentage of labour force who are unemployed. Employment rate: percentage of working age population who are employed. In the Labour force: the sum of employed and unemployed. Sources: LFS (2013), tables 3.2, 4.1, 5.2); LFS (2005), tables 3.1, 4.2; ILOSTAT.

At 83.3 per cent, the LFPR was significantly higher in rural than in urban areas (66.5 per cent), reflecting the predominance there of agriculture (Figure 4.1). There were also major differences in LFPR across regions, largely due to differences in the degree of urbanization; for example, for Amhara the figure is 83.2 per cent, Oromia 81.9 per cent, and Benishangul-Gumuz 80 per cent, but only for Addis Ababa City Administration it is only 62.8 per cent.

Young people participated in the labour force to a slightly lesser extent than in the working age population as a whole. In 2013, LFPRs among young people (aged 15–24) stood at 78 per cent; 81 per cent for male and 75 per cent for female young people. These relative rates can probably be explained by the pervasiveness of on-farm employment, where the transition from school to work meets no barriers, rather than any frictionless labour market entry in general.

Figure 4.1. LFPR by rural and urban areas and by sex (%)



Notes: Working age population defined as people aged 10 or above; age disaggregated data were not available to allow a recalculation for those aged between 15 and 64. Additional data on urban areas were available from the UEUS 2018, which was not available for rural areas.

Sources: Urban Employment Unemployment Survey (UEUS) 2018; LFS (2013), Table 4.2; LFS (2005), Table 4.2.

In 2013, about half of the labour force was literate, with male literacy rates (59.4 per cent) much higher than those for women (39.8 per cent).³² In general, the share of the labour force without education has fallen substantially over time, from 71.5 per cent in 1999 to 42.8 per cent in 2013, while the share of the labour force with secondary education has increased to 5 per cent from 1 per cent during the same period. The gender gap remains large. In 2013, 64 per cent of employed women had less than basic education, compared with 39 per cent of men.³³ As noted elsewhere in this chapter, educational outcomes for young people are substantially better than for older participants in the labour force; in 2013, 57 per cent of workers aged 30 or over had never been to school, compared with 25 per cent of young people (15–29 years of age) (JCC, 2019b). The overall trend therefore is towards a more educated workforce on average, with significant differences between rural and urban areas.

The employment rate remained constant between 2005 and 2013 at 81 per cent (Table 4.1).³⁴ It was significantly higher for men than for women – 89.3 versus 74.6 per cent in 2013 – resulting from the combined effect of both lower labour force participation and higher unemployment among women. It was also very much higher in rural than in urban areas: 82 versus 56 per cent based on the national 10 or over working age definition. The employment-to-population ratio is a major indicator of the extent of the involvement of a country's potential labour resources in economic activities. As can be seen, this involvement is higher among men than women and higher in rural than in urban areas. The gender gap reflects the fact that women shoulder the main responsibility for household work and child-care, but structural barriers imply that women also face significant gender inequality in access to employment, as demonstrated, among other things, by women's high unemployment rates. The very high rural–urban differences in employment rates are explained partly by the widespread access to land and prevalence of employment on own farms in rural areas, while the low urban employment rates point to an absolute scarcity of urban employment opportunities. The employment rate alone, however, is far from presenting the whole picture.

³² LFS (2013), Table 4.2 (authors' calculations).

³³ ILOSTAT. "Less than basic" defined as those with only pre-primary or no education.

³⁴ Based on the standard 15–64 working age population.

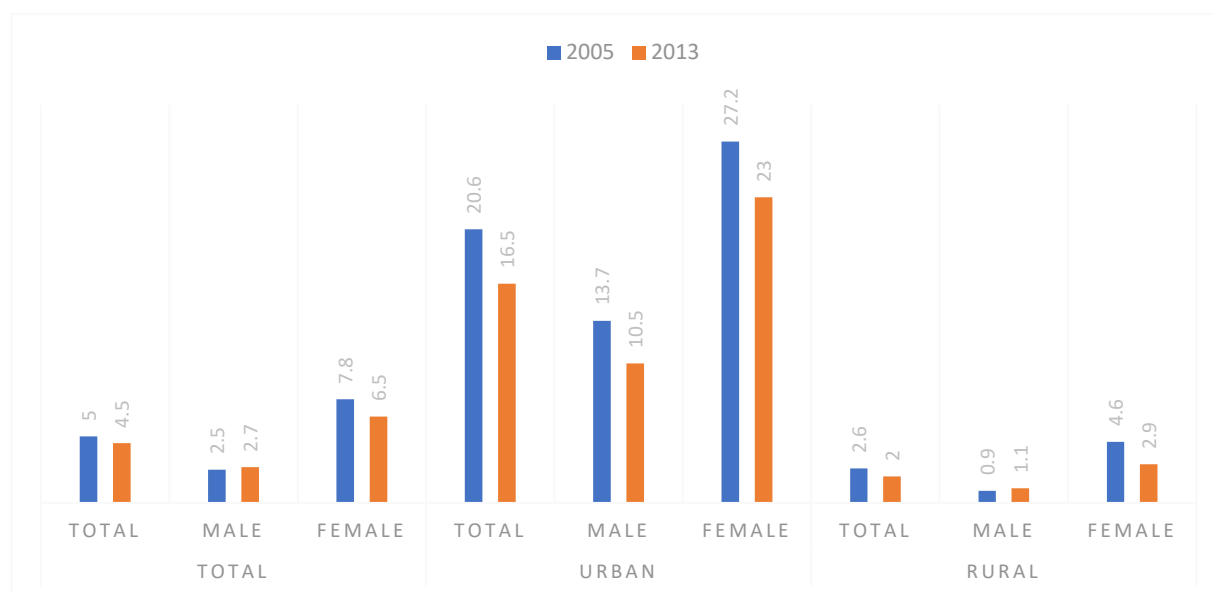
Equally important is the extent of the involvement in economic activities in terms of time and issues of efficiency, productivity, returns to labour, and conditions of work.

The unemployment rate stood at 5.1 per cent in 2013, marginally lower than in 2005, based on the 15–64 working age definition (Table 4.1).³⁵ The low unemployment rates are deceptive as they mask large rural–urban differences and the vast majority simply cannot afford to be unemployed, but must eke out a living as best they can.

There are large disparities between the unemployment rates of men and women, pointing to severe structural difficulties faced by women in accessing productive employment (Figure 4.2). There are also large differences between unemployment rates in urban and in rural areas, reflecting the importance of agriculture as an employment buffer in rural areas, and across age groups. Indeed, the unemployment rate in Ethiopia is largely a function of open unemployment in urban areas. Clearly the deficit of productive jobs takes different shapes in rural and in urban areas. In rural areas, it takes the form of working poverty whereas in urban areas it takes the form of open unemployment.

Youth unemployment rates need to be interpreted with the same caution and caveats as overall unemployment rates. In 2013 the unemployment rate among young people aged 15–29 was 6.8 per cent. At 9.1 per cent, the unemployment rate among young women was twice as high as among young men (4.6 per cent).³⁶ The urban youth unemployment rate (21.6 per cent) was significantly higher than the rural youth unemployment rate (3.1 per cent), and the urban youth unemployment rate increased to 29.4 per cent in 2018 (see Section 5).

Figure 4.2. Unemployment rate by region (urban/rural) and sex (%)



Note: The labour force is calculated with reference to all those aged 10 or above.

Sources: LFS (2005), Table 6.1; LFS (2013), Table 6.1.

Looking at the proportion of unemployed by education, some interesting conclusions emerge (Table 4.2). First, it appears that the largest proportion of unemployed are those with basic or intermediate education, that is, with largely primary and secondary education. Those

³⁵ Using the broader definition of working age (10+) the unemployment rates for 2013 and 2005 were 4.5 per cent and 5 per cent, respectively.

³⁶ LFS (2013), Table 6.6.

with no education tend to form a smaller proportion of the unemployed, probably because of their involvement in the large agricultural sector. This is in contrast to the distribution of the labour force by education, where the largest proportion of the labour force in both 2005 and 2013 had less than basic education, and over 90 per cent of the labour force had basic education (or less).³⁷

Table 4.2. Unemployed population disaggregated by education and sex (%)

Level of education	2013			2005		
	Total	Male	Female	Total	Male	Female
Less than basic	18.7	12.1	22.9	27.2	14.1	35.1
Basic education	56.1	55.9	56.2	39.4	47.7	34.5
Intermediate education	21.7	26.1	18.9	29.9	33.2	27.9
Advanced education	2.9	4.8		2.9	3.9	
Not stated	0.7	1.2	0.3	0.6	1.2	0.2

Note: "Less than basic education" includes no schooling, or those with pre-primary or early childhood education.³⁸ "Basic education" includes both primary and lower secondary education.³⁹ "Intermediate education" includes both upper secondary and post-secondary non-tertiary education.⁴⁰ "Tertiary education" includes the first stage of tertiary education and above.⁴¹

Source: ILOSTAT

4.2 Status in employment

Table 4.3 sets out data on employment by status in Ethiopia, as extracted from the 2013 and 2005 labour force surveys. In general, a high proportion of wage and salaried workers in a country tends to signify advanced economic development, while a sizable number of own-account workers may indicate a large agricultural sector and/or economy (ILO, 2016, pp. 61–62). In the Ethiopian case, wage workers make up just around 10 per cent of employment; the rest are self-employed, and can be characterized as being in vulnerable employment, because they are less likely to have formal work arrangements and as a result, also lack any form of social security and a voice at work.

Wage employment is split about equally between the private sector and the public sector. Wage employment is more common among employed men than women (12 per cent compared with 7.9 per cent). Wage employment is concentrated in urban areas, where it accounted for 45 per cent of all employment in 2013. By contrast, it made up less than 4 per cent of rural employment, implying that economic diversification in rural areas has not advanced very far. Urban wage employment appears to have increased since 2013, in particular among women. The 2018 Urban Employment Unemployment Survey (UEUS) found that 52.3 per cent of those employed in urban areas were actually wage-workers and the rate of wage employment was roughly equal for both men (52.6 per cent) and women (51.9 per cent). This may have been driven by the expansion of sectors such as horticulture and textile manufacturing in urban areas, which tend to employ mainly women.⁴² It is worth noting that the public sector has consistently been the largest employer of those with post-

³⁷ See "Labour force distribution by education (by sex and age) (%)", ILOSTAT.

³⁸ Levels X and 0 for both ISCED 97 and 11. See Methodological note on "Employment by Education", ILOSTAT. See also UNESCO 2012, Table 19, for a discussion on correspondence between ISCED 11 and ISCED 97 levels.

³⁹ Levels 1 and 2 for both ISCED 97 and ISCED 11.

⁴⁰ Levels 3 and 4 for both ISCED 97 and ISCED 11.

⁴¹ Levels 5 and above for both ISCED 97 and ISCED 11.

⁴² On the textile/apparel sector, see Staritz and Whitfield (2019).

secondary qualifications in Ethiopia, and historically the education system was designed to feed the public sector, creating an unsustainable cycle of both education and expectation among those with higher levels of education (Mains, 2012; JCC, 2019b). Public sector employment has increased rapidly in recent years, with the number of civil servants increasing from 630,000 in 2008 to 1.64 million in 2017 (JCC, 2019b).

Table 4.3. Employment by status (percentage of total, except where otherwise indicated)

	Total		Men		Women		Rural		Urban	
	2005	2013	2005	2013	2005	2013	2005	2013	2005	2013
Wage workers	8.0	10.0	9.2	12.0	6.1	7.9	3.6	3.9	42.8	45.1
Public	3.2	4.4	3.8	5.3	2.4	3.4	1.3	1.6	18.5	20.5
Private	3.4	4.4	4.5	5.6	1.9	3.1	1.7	1.8	16.5	19.5
Domestic	1.2	0.9	0.7	0.7	1.7	1.3	0.5	0.4	7.1	4.2
Other	0.2	0.3	0.2	0.4	0.1	0.1	0.1	0.1	0.7	0.9
Employers	0.6	0.4	0.9	0.7	0.2	0.1	0.6	0.4	0.6	0.7
Own account workers	91.5	89.5	89.8	87.5	93.5	92.0	95.8	95.9	56.6	54.3
Self-employed	40.9	40.1	54.8	51.4	24.8	26.9	41	40.3	40.3	39.3
Unpaid family members ⁴³	50.3	48.7	34.6	35.3	68.5	64.4	54.6	55	15	13.3
Coop member	0	0.2	0.1	0.3	0	0.1	0	0.1	0.2	0.9
Apprentices	0.3	0.5	0.3	0.5	0.2	0.6	0.2	0.5	1	0.8
Not stated	0	0	0	0	0	0	0	0	0.1	0
Total	100	100	100	100	100	100	100	100	100	100
<i>Total numbers (in thousands)</i>	31 435	42 404	16 860	22 887	14 575	19 517	27 989	36 021	3 446	6 383

Note: Calculated on the basis of working age population aged 10 or above.

Source: LFS (2013), Table 5.4.

The very low rate of rural wage employment may be somewhat deceptive. A series of micro-studies, including one by ILO, have argued that casual wage work is central to the livelihood strategies of the poorest farmers, and may exceed the importance of own-account farming for many of the poorest rural households (Rizzo, 2013, p. 3). This is not captured adequately by official statistics as data that classify workers according to their primary activity typically miss large numbers of casual workers. This would suggest that two processes are occurring simultaneously: a high dependence on casual wage labour among the poorest strata indicates that cultivation of their own land is not sufficient for these farmers to sustain themselves, and this results in a distress-driven shift from own account farming to other activities. This is very different from the opportunity-driven shift of labour from agriculture to non-farm employment associated with a dynamic economic development. Even though they do not clearly manifest in statistical indicators, the distinction between these fundamentally different processes is discussed in Section 6.

⁴³ This category is now referred to as “contributing family workers”.

4.3 Employment by sector

A primary characteristic of structural transformation is the reallocation of labour from low-productivity agriculture to higher productivity manufacturing and services. At first glance, some of these characteristics appear to be visible in the Ethiopian economy: employment in agriculture and allied activities fell from 80.2 per cent in 2005 to 72.7 per cent in 2013 (Table 4.4). At the same time, employment in services increased rapidly, from 13.3 per cent to 19.8 per cent, largely due to a jump in female employment in services.

Table 4.4. Employment by main economic sectors, 2005 and 2013 (%)

	Total	Men	Women	Rural	Urban
2005					
Agriculture	80.2	84.3	75.5	88.5	13.0
Non-agricultural sectors	19.8	15.7	24.5	11.5	87.0
manufacturing	4.9	2.6	7.5	3.7	14.3
construction	1.4	2.1	0.7	0.9	5.4
trade and repair services, hotels and restaurants	7.7	4.5	11.4	4.6	32.6
public administration	1.2	1.4	0.9	0.5	6.5
education and health	1.2	1.3	0.9	0.5	6.5
in private households	0.8	0.1	2.6	0.2	5.9
2013					
Agriculture	72.7	79.5	64.7	83.2	13.5
Non-agricultural sectors	27.3	20.5	35.3	16.8	86.5
manufacturing	5.1	3.5	6.8	3.1	15.2
construction	1.9	2.8	0.9	1.0	7.5
Trade and repairs, hotels and restaurants	6.5	4.4	9.2	3.3	25.1
public administration	0.7	0.9	0.4	0.2	3.6
education and health	2.2	2.4	2.0	0.9	9.5
in private households	7.3	1.9	13.6	7.3	7.0

Notes: Agriculture includes forestry and fishing, manufacturing includes electricity, water and sewage. All figures refer to current status, that is, employment during the week preceding the survey. The share of urban in total employment was 11.0 per cent in 2005 and 15.6 per cent in 2013.

Sources: LFS (2005), Table 5.4; LFS (2013), Table 5.3.

Unfortunately, however, this is partly the manifestation of a statistical quirk rather than a “true” structural transformation.⁴⁴ Although the relative share of those employed in agriculture fell between 2005 and 2013, this was partly a result of the reclassification of large numbers of rural workers, especially women, as persons employed in private households.⁴⁵ When employment in domestic households are excluded, the picture is one of a very small shift in employment (2.5 percentage points) from agriculture to the non-agricultural sectors; much of this “shift” is accounted for by employment in education and health care, and not

⁴⁴ Wage employment, excluding domestic workers increased, albeit modestly, over this period.

⁴⁵ In the 2013 LFS, a new category was introduced – “activities of households as employers” – which included activities such as domestic work and, apparently, firewood collection.

in manufacturing or private sector services.⁴⁶ Within services, the largest number of people were recorded as being employed in domestic households. This was closely followed by employment in the wholesale and retail trade services sector, which also employed the largest number of people in the service sector in 2005 (Table 4.4). This also appears to be borne out by the fact that the number of women employed in agriculture appears to have declined much more sharply than the number of men over the same period, from 75.5 per cent to 64.7 per cent. At the same time, the number of women employed in services increased sharply, from 16.2 to 27.3 per cent.

Two other critical points are worth noting: first, the relative lack of change in the number of people employed in the construction sector suggests that the construction boom has been capital- rather than labour-intensive. Second, the relative share of the population employed in manufacturing in fact fell between 2005 and 2013, even though the absolute numbers increased. The point here is that the sectoral changes in output in the Ethiopian economy (discussed in the previous section) have not been accompanied by a change in employment patterns. A preliminary conclusion is that rather than moving into productive employment, rural poverty in the agricultural sector may be transposing itself into urban poverty in the form of employment as domestic workers at very low wages and in informal services, such as street-vending, rag-picking, restaurant work, and other low-productivity activities (see Campbell, 2013, pp. 25–26). This is probably occurring in parallel with more positive and opportunity-driven change in the Ethiopian economy, although it is difficult to disentangle these two processes without more detailed statistical data. The remainder of the analysis in this section appears to point in the same direction.

4.4 Underemployment

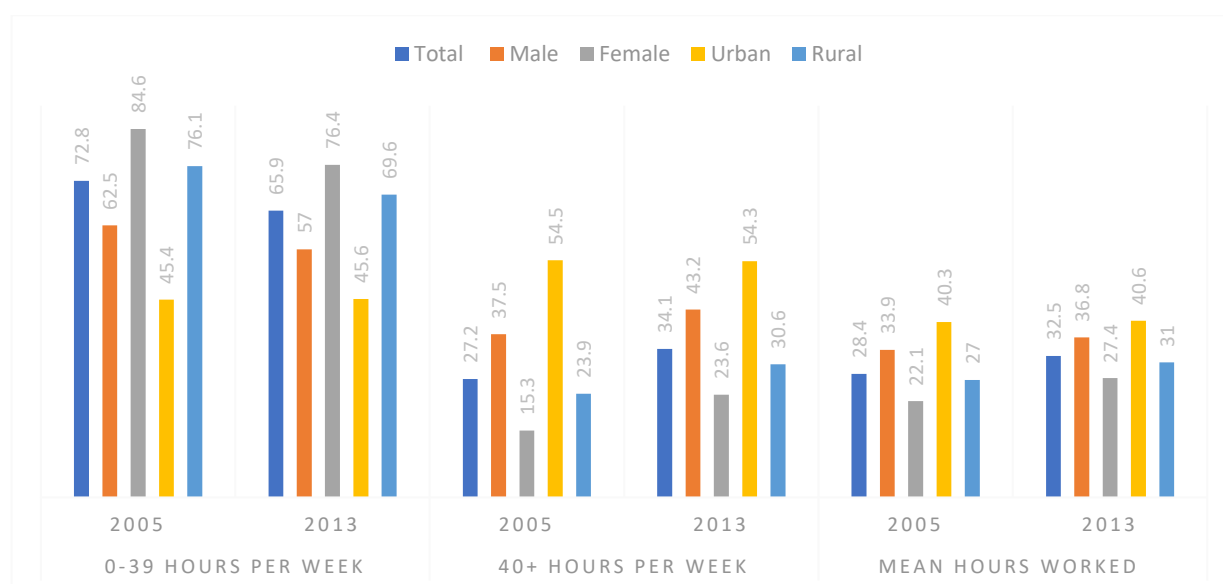
A person is said to be underemployed either when they (i) work less than full-time (typically 40 hours a week) and are both available and willing to work additional hours, or (ii) when they are doing work that does not make full use of their skills. The latter form of underemployment is notoriously difficult to estimate in Ethiopia as elsewhere, however.⁴⁷ The 2018 UEUS estimates that 43 per cent of the urban employed were seeking and available to work additional hours, 60 per cent of whom were already working at least 40 hours per week.⁴⁸ The large proportion of the urban employed who were working full-time and still wanting to work more hours suggests very low returns to labour per hour, which compels people to work very long hours to make ends meet.

⁴⁶ If domestic workers are excluded, the share of workers employed in agriculture accounted for 80.8 per cent of those who were employed in 2005, and for 78.4 per cent of the employed in 2013. The share of workers in education and health increased from 1.2 per cent in 2005 to 2.3 per cent in 2013. Authors' calculations, based on Table 5.3 of the LFS 2013, and Table 5.4 of LFS 2005.

⁴⁷ This is notoriously difficult to do.

⁴⁸ UEUS (2018), Table 5.28.

Figure 4.3. Proportion of employed by hours worked, by sex and rural/urban areas (%)



Note: The working age population is defined as those aged 10 or above.

Sources: LFS (2013), Table 5.5; LFS (2005), Table 3.8. Authors' calculations.

Figure 4.3 shows the average number of hours worked per week by sex and location. It appears that more than half of all men and women work fewer than 40 hours a week in Ethiopia. Less than full-time employment is the rule in rural areas, while the urban employed work longer hours than the rural employed. Clearly, while agriculture goes a long way to ensure full employment in rural areas, it does not provide full-time employment. Yet, these conclusions should be treated with some caution. First, hours of work are difficult to recall accurately and there are often misunderstandings among respondents concerning what activities count as employment.

4.5 Employment in the informal economy

The definitional distinction between formal and informal employment still differs across countries and surveys, implying a need for some caution in the interpretation of statistics.

The National Labour Force Surveys of 2005 and 2013, as well as the 2018 Urban Employment Unemployment Survey include data on employment in the informal sector in urban areas. In the absence of national level data on informality, the urban data offer a reasonably good proxy for estimating the proportion of informal employment in non agricultural employment.⁴⁹

Table 4.5 sets out the share of informal employment in urban areas. It suggests that this share has fallen somewhat over time, in particular among men. Informality is much more prevalent among women. Unfortunately, lack of detailed statistics precludes an analysis of the causes behind this gender-based difference. Possible causes include (i) a large share of women in petty trade and (ii) the high share of women working in domestic households (ILO, 2016, pp. 83–84).

⁴⁹ This is an indicator for SDG 8.3, which enjoins states to “promote development-oriented policies that support productive activities, decent job creation, entrepreneurship, creativity and innovation, and encourage the formalization and growth of micro-, small- and medium-sized enterprises, including through access to financial services”.

Table 4.5. Informal employment as percentage of total urban employment, by sex

	2005	2013	2018
Both sexes	26.2	25.8	21.7
Men	23.7	18.1	17.1
Women	29.2	36.5	28.2

Sources: LFS (2005), Table 5.6; LFS (2013), Table 5.8 and UEUS (2018), Table 5.31.

There are some reasons to be sceptical about these numbers; they do not fit the findings from a large number of qualitative studies that have pointed to the rapid pace of urbanization in Ethiopia, nor can they easily be reconciled with the increasing rates of rural–urban migration and the consequent involvement of the newly urbanized in the informal sector, in occupations such as mobile street trading, shoe shining, and coffee vending or as informally contracted workers in the construction sector.⁵⁰ One recent study on Dire Dawa city, for example, found mobile street vending – that is, selling items ranging from books and small electronic goods to roasted chickpeas and sunflower seeds, while on the move – is associated predominantly with younger migrants from the southern part of the country (Feyissa, Midega and Wakjira, 2018, pp. 20–22).⁵¹

Young people are particularly likely to migrate as a livelihood strategy, arguing that there are “no opportunities for them” in rural areas (Atnafu, Oucho and Zeitlyn, 2014, p. 10). In short, the statistics do not appear to be in consonance with conclusions from qualitative research on the prevalence of informal work.

4.6 Wages and hourly earnings

Recent data on real wages, adjusted for inflation, are available only for urban areas. Still, some preliminary trends can be assessed from data from the 2013 LFS and the 2011 and 2018 UEUS. The 2013 LFS assessed the mean average wage to be 1,305 birr (around US\$ 45 at the current exchange rate) for the country as a whole. The female mean monthly wage was only about 57 per cent of the male mean monthly wage. A large proportion of those in salaried employment earned very low wages; around 68 per cent of all wage-employed earned less than or just around the mean monthly wage. In urban areas in 2018, the mean monthly wage for men and women was 3,132 birr (around US\$ 107 at current exchange rates) (Table 4.6).

⁵⁰ The 2013 LFS found that 44.4 per cent of the total population in urban areas were migrants.

⁵¹ See also Research and Evidence Facility, EU Emergency Trust Fund for Africa (2018).

Table 4.6. Urban wages in 2011 and 2018 (at 2018 prices) and compounded annual growth rate, by sector, 2011–2018

	Average wage / month in 2011 (birr)	Average wage / month in 2018 (birr)	Change 2011–18 (birr)	CAGR 2011–18 (%)
All sectors	1 921	3 132	1 211	7.23
Agriculture	1 350	2 505	1 155	9.23
Manufacturing	1 580	2 314	734	5.61
Construction	1 941	3 247	1 306	7.63
Trade and repair services	1 415	2 162	747	6.24
Transport and storage	2 176	3 439	1 263	6.76
Hotel and restaurants	732	1 422	690	9.95
Financial and insurance	3 007	5 158	2 151	8.01
Professional and tech services	–	–	–	–
Public administration	2 745	3 703	958	4.37
Education	2 490	4 113	1 623	7.43
Health	2 425	3 878	1 453	6.93
Employed in private households	396	1 018	622	14.45

Note: CAGR refers to compound annual growth rate, and “price index” for December 2011–December 2018 = 180.7.

Sources: UEUS (2011), Table 5.7; UEUS (2018), Table 5.7.

Average wages vary widely across sectors. Generally speaking, wages are still higher in the public than in the private sector. Wages for those employed in hotels and restaurants and, in particular, in private households are well below half the national average. Wages in the manufacturing sector also appear to be conspicuously low.⁵²

But wage data in Ethiopia are somewhat contradictory. On one hand, a series of reports point to stagnating real wages: a World Bank report from 2016 notes that real urban wages were in fact at roughly the same level between 2003 and 2014, with some increase between 2012 and 2014 (World Bank, 2016, p. 51). Going even further, the Jobs Creation Commission created by the Government of Ethiopia concludes that, overall, urban wages remained at the same real level between 2006 and 2016, and only increased after 2016 because of sharp public sector wage increases. On the other hand, our analysis suggests that real urban wages actually increased by about 7 per cent per year between 2011 and 2018, that is, almost in step with GDP growth (Table 4.6). However, notable exceptions were the public administration and manufacturing sectors, in which the annual rate of growth was well below the average rate of increase. In other words, comparing wage data from the 2011 and 2018 UEUS appears to contradict the World Bank’s findings. These discrepancies may to some extent be due to the use of different reference periods, for example, high inflation between 2006 and 2012 and freezes on public wages in some earlier years.

⁵² As the 2018 wage data refer to urban areas only, the agricultural wage level is of less significance.

Table 4.7. Average monthly wages and gender wage gap, by sector in 2018 (Urban areas only)

	Monthly average wage (in birr)			Gender wage gap (%)	Average wage as % of total average	Women as % of total employed in sector
	Both sexes	Men	Women			
<i>All sectors</i>	3 132	3 757	2 323	61.8	100.0	44.0
Agriculture	2 505	2 878	1 907	66.3	80.0	35.2
Manufacturing	2 314	2 699	1 749	64.8	73.9	45.0
Construction	3 247	3 484	2 324	66.7	103.7	17.1
Trade and repair services	2 162	2 529	1 621	64.1	69.0	52.6
Transport & storage	3 439	3 445	3 372	97.9	109.8	7.0
Hotel & restaurants	1 422	1 861	1 232	66.2	45.4	71.2
Financial & insurance	5 158	5 763	4 313	74.8	164.7	39.3
Professional & tech services	4 846	5 351	4 145	77.5	154.7	39.5
Public administration	3 703	4 095	3 027	73.9	118.2	36.7
Education	4 113	4 705	3 318	70.5	131.3	42.7
Health	3 878	4 624	3 354	72.5	123.8	57.1
Employed in private households	1 018	2 040	770	37.7	32.5	81.2

Source: UEUS (2018), Tables 5.7 and 5.25.

The gender wage gap remains very large (Table 4.7). In 2018, the average urban female monthly wage was only about 62 per cent of the male mean monthly wage. A major reason why women earn much less than men is gender segregation on the labour market. Female wage workers are overrepresented in sectors and occupations in which wages are well below the national average. Domestic workers, four out of five of whom are women, earn less than a third of the average national wage. Hotels and restaurants and trade and repair services are other low-wage sectors with a high concentration of female wage workers. The main exception to this rule would seem to be the health sector. By contrast, men dominate in well-paid sectors such as finance, professional and technical services and public administration.

However, gender wage gaps are also very large within sectors (Table 4.7). In 2018, female urban average wages were less than two-thirds of male wages in manufacturing, trade and repair services and hotels and restaurants and less than 75 per cent of male wages in all but two sectors (transport and storage, which employs very few women, and professional and technical services). The large gender wage gaps within sectors may in some instances be due to gender-based occupational segregation within sectors, for example, male doctors and female nurses in the health sectors, but it is difficult to escape the conclusion that Ethiopia still has some way to go before achieving the goal of equal pay for equal work.

4.7 Social protection

Social protection is a key element of national strategies to promote human development, political stability, and inclusive growth and ensures that people enjoy income security and have effective access to health care and other social services. Policies aimed at achieving full access to productive employment and social protection policies complement each other. Social protection not only provides economic security to those unable to earn their own living, but can also empower people to take advantage of economic opportunities, by reducing the cost of risks.

The core functions of social protection can usefully be divided into three broad categories. Social protection usually encompasses three broad sets of public action: publicly provided state (contributory) contingent insurance (pensions, unemployment insurance), social sector policies (for example, fee waivers), and targeted non-contributory programmes (social safety nets, in other words) that transfer resources to poor households (Hodinott and Tafesse, 2019).

Social safety nets – primarily public works and, to a lesser extent, unconditional transfers – are the largest component of social protection in Ethiopia; this is known as the productive safety net programme (PSNP). Spending on the rural safety net programmes currently runs to approximately 12 billion birr (US\$ 600 million) with an additional 2 billion birr (US\$100 million) being spent on safety nets in urban areas. The 14 billion birr spent on safety nets is equivalent to 1.2 per cent of GDP. Approximately 10 million people benefit from these safety nets with an additional 600,000 school children benefitting from school meals. Most participants (~85 per cent) do labour-intensive public work, building assets of benefit to their communities. A small number of beneficiaries (~15 per cent) who lack the ability to do this work receive unconditional transfers, called Direct Support.

For women, this can even be understood as providing a form of paid maternity leave (ILO, 2017, p. 37). The PSNP provides pregnant women in food-insecure and poor households, regardless of their employment status, with cash benefits after six months of pregnancy and during the first 10 months after delivery, exempting them from participating in public work. However, women in several field sites reported that they continued working throughout their pregnancy as they feared losing their entitlement to benefits if they interrupted their work (ibid.).

A second component is financial assistance triggered by an event such as illness, disability, or unemployment. Eligibility and benefit levels are typically based on employment and contribution history, rather than current poverty status. Coverage is low – less than 1 per cent of the population receives payments from contributory social insurance – and government expenditures on these amount to approximately 2 billion birr, or 0.25 per cent of GDP. All of these programmes are administered under the broad umbrella of the National Social Protection Strategy of 2016.⁵³

There is currently no form of unemployment insurance, although some pension schemes exist for workers in the formal sector. A health and workplace insurance scheme for workers (the Social Health Insurance Proclamation, 2010) was passed by the legislature but has never come into effect, despite repeated demands from COSATU. There is also currently no minimum wage in Ethiopia, although efforts are under way (with technical assistance from the ILO) to put the relevant legislation in place.⁵⁴

⁵³ Available at:

<https://www.cmpethiopia.org/content/download/2676/11160/file/National%20Social%20Protection%20Policy%20of%20Ethiopia.pdf>.

⁵⁴ Authors' interview with COSATU representatives, May 2019.

5. Engaging young people

Whether or not Ethiopia will succeed in achieving the SDG goals, especially the goal of “inclusive and sustainable economic growth, [with] full and productive employment and decent work for all” (SDG 8), depends on successful integration of the young into the economy and the world of work, making it possible for them to realize their full potential. Young people⁵⁵ currently account for about 38 per cent of the working age population (aged 15–64). To put this in perspective, in 2030, approximately 61 per cent of the working age population will be made up of the current youth cohort (aged 15–24) and those (around 33 per cent) who are yet to reach working age. They will be better educated and much better connected and informed about the outside world than the older generation and, undoubtedly, have higher aspirations. Making full and productive use of this human potential presents a unique opportunity for Ethiopia, but also a major challenge.

Overall, Ethiopian young people are better equipped in terms of education to access productive jobs than their parents were a few decades ago. Almost half of the young people entering working life today⁵⁶ have completed at least eight years of primary education, compared with 17 per cent of the working age population as a whole,⁵⁷ with only minor differences between male and female completion rates. Differences in completion rates between children from rich and poor households, however, remain large. In 2016, a child from the richest household quintile was three times more likely to complete eight years of primary education than a child from the poorest household quintile. Conversely, three out of four children from the poorest household quintile and 70 per cent of children from the second poorest household quintile entered working life without completing primary education.

Overall, more young entrants into working life today have completed lower and higher secondary education than in the past. A fifth of these young entrants have completed at least lower secondary education and 13 per cent higher secondary education or more, compared with 14 and 7 per cent, respectively, among the working age population as a whole. Female completion rates for secondary education are only slightly lower than the rates for men and this minor gender gap appears to have changed little over time.

The gap in access to secondary education between children from poor and richer households, however, has widened considerably, as the rapid increase in secondary school completion rates has been almost entirely confined to the richest household quintile. The interpretation of these figures is not entirely straightforward as the causality may go in both directions for the adult population; that is, a high income and consumption level may have been a result of a higher level of education, just as the parents’ good economic status made it possible to obtain such an education. For the young recent and current entrants into working life, however, coming from a better-off household is essential for accessing and completing secondary education. This also reflects a huge difference in access to secondary education between rural and urban areas as the richest (fifth) household quintile is largely urban, while the other quintiles are largely rural. In 2016, some 58 per cent of urban youth (aged 15–24) had completed at least lower secondary education and 28 per cent (of those aged 20–29) had completed at least secondary education, compared with a mere 11 and 4 per cent, respectively, among rural youth.⁵⁸

⁵⁵ Here defined as those aged 15–24.

⁵⁶ Here defined as those aged 15–20 in 2016.

⁵⁷ Here defined as those aged 10 or above.

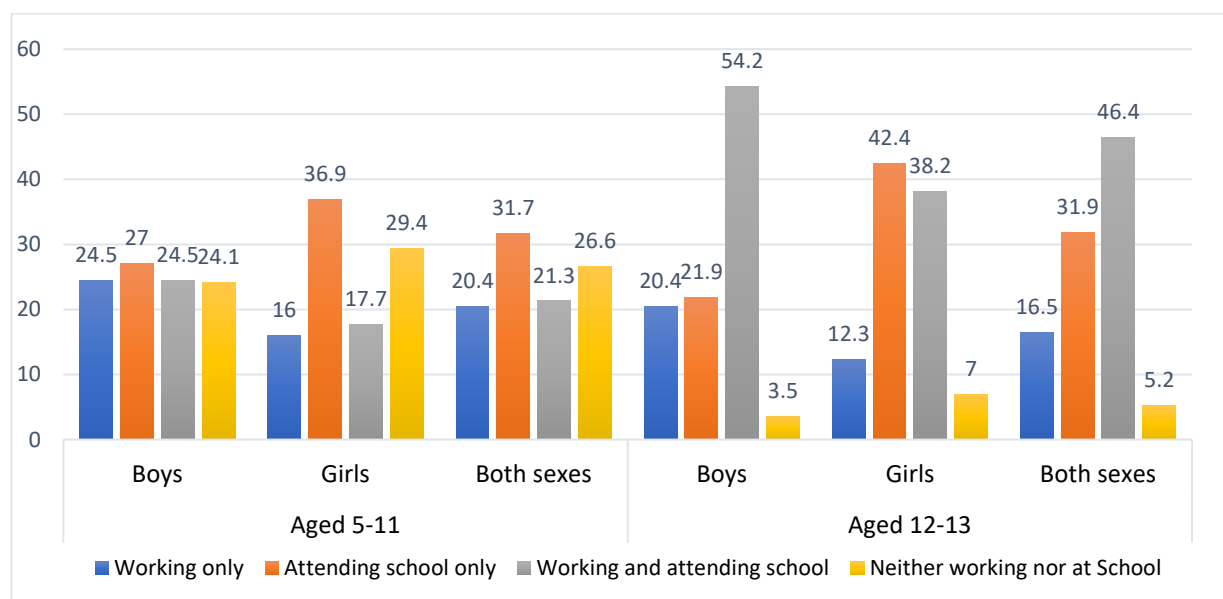
⁵⁸ Worldwide Inequality Data Base on Education, 2019.

These huge discrepancies in education between rural and urban areas and across household consumption quintiles are a major cause for concern. They can be expected to translate into increasing inequality of access to productive employment and, by extension, increasing income inequality in the years to come. In particular, large numbers of rural youth are at risk of being left behind as the country develops, lacking both sufficient land to make ends meet and the necessary education to access productive off-farm jobs. Because they constitute the vast majority of the country's young people, major efforts need to be made to sharply increase their access to both primary and secondary education. Otherwise, human capital is also likely to emerge as a major constraint on sustaining rapid productive transformation and economic growth in the coming years.

There are several reasons why children cannot access and devote themselves fully to education. Prohibitively long distances to school and high costs act as barriers. Furthermore, even though primary education (grades 1–8) is free of charge in Ethiopia, schools are often thinly spread in rural areas. Poverty and the need to contribute to the household income can be another major barrier.

In fact, the incidence of child labour remains very high in Ethiopia, including among the younger age groups, and typically involving long hours of work. More than two out of five children aged 5 to 11 are involved in child labour. About half of those involved in child labour combine work with school, while the other half has to forgo education altogether (Figure 5.1). The incidence of child labour is higher among boys than girls – 49 versus 34 per cent for the 5–11 age group – and more girls than boys can devote themselves fully to education. The incidence of child labour is higher among 12–13 year old children, but older children are more often able to combine work with school (Figure 5.1).

Figure 5.1. Child labour and school attendance by age groups and sex, 2015 (%)



Source: Child labour survey (2015), Table 5.13.

Child labour is much more common in rural than in urban areas and primarily involves work in agriculture. Almost 60 per cent of all rural children (aged 5–17) work, compared with 19 per cent of children in urban areas. Less than a fifth of rural children can attend school unfettered by any obligation to work, compared with almost 70 per cent of those in urban areas. The situation is particularly precarious for rural boys, among whom a mere 16 per cent “attend school only”, while 68 per cent are involved in child labour.

Most working children work very long hours: those aged 5 to 11 work an average of 32 hours per week. On average, boys work more than girls (34 compared with 29 hours per

week) and children in rural areas (34 hours per week) work more than those in urban areas (30 hours per week). Even those who combine work with school, work very long hours⁵⁹ – leaving them very little scope to attend school. Child workers who do not attend school (including those aged only 5–11), work almost full-time. The high incidence of child labour and the barriers to obtaining adequate formal education, especially among children from poorer and rural households, means that large numbers of children will face particular difficulties in accessing productive jobs as adults, with implications for poverty and inequality.

These are not the only challenges facing young people. In rural areas, in future they will be even more land constrained than their parents as each inter-generational transfer of land involves splitting it into smaller holdings shared between more hands. The average area under grain crops⁶⁰ among small-holder farms has fallen from 0.94 hectares in 2004–05 to 0.81 hectares in 2017–18⁶¹ and will continue to fall until the slowdown in population growth and increased exit opportunities combine to reverse the trend of a growing agricultural population. Today’s rural youth will be called upon to spearhead a continued transformation of agriculture from primitive subsistence farming into modern, efficient farms producing primarily for the market, while being severely land constrained. They will also have to rely on non-agricultural sources of employment and incomes to a much greater extent than their parents.

This will require comprehensive strategies to enable and actively foster rural economic development through a two-pronged approach focused on (i) continued agricultural transformation and (ii) economic diversification through the development of non-agricultural economic activities, not least in the form of SMEs, and the forging of strong links between the different players in an increasingly diverse economic setting. It will also require a change of perceptions. An education should not primarily be seen as a means to escape the drudgery of work in agriculture and what Marx called the “idiocy of rural life”. The opportunities being opened up by the “fourth industrial revolution” and advancements in ICT (which among other things greatly reduce the importance of location) might be exploited to the advantage of the transformation of agriculture. This could improve its image, turning it from employment by default into one of many areas of employment by choice.⁶² It is critical that the young generation in rural Ethiopia be equipped with the education, knowledge and skills needed to spearhead the transformation of agriculture and the rural economy in the years to come; investments in rural youth must become much more inclusive than at present.

Urban youth face great difficulties in accessing jobs at all, let alone productive and decent ones.⁶³ In 2018 open unemployment among urban youth (aged 15–24) stood at 29 per cent, twice as high as among the rest of the labour force (aged 25–64). Young women in the labour force were particularly severely affected, with well over a third of them being unemployed. The published results of the 2018 urban labour force survey do not allow a more detailed analysis of the characteristics and causes of urban youth unemployment, but a World Bank study, using somewhat older data, concluded that while “queuing” for attractive public sector or other high status jobs might explain some of the unemployment among those with tertiary education, the most important reason by far behind the high youth

⁵⁹ 28 hours per week on average among both 5–11 and 12–13 year olds.

⁶⁰ The areas under grain crops account for most the arable land.

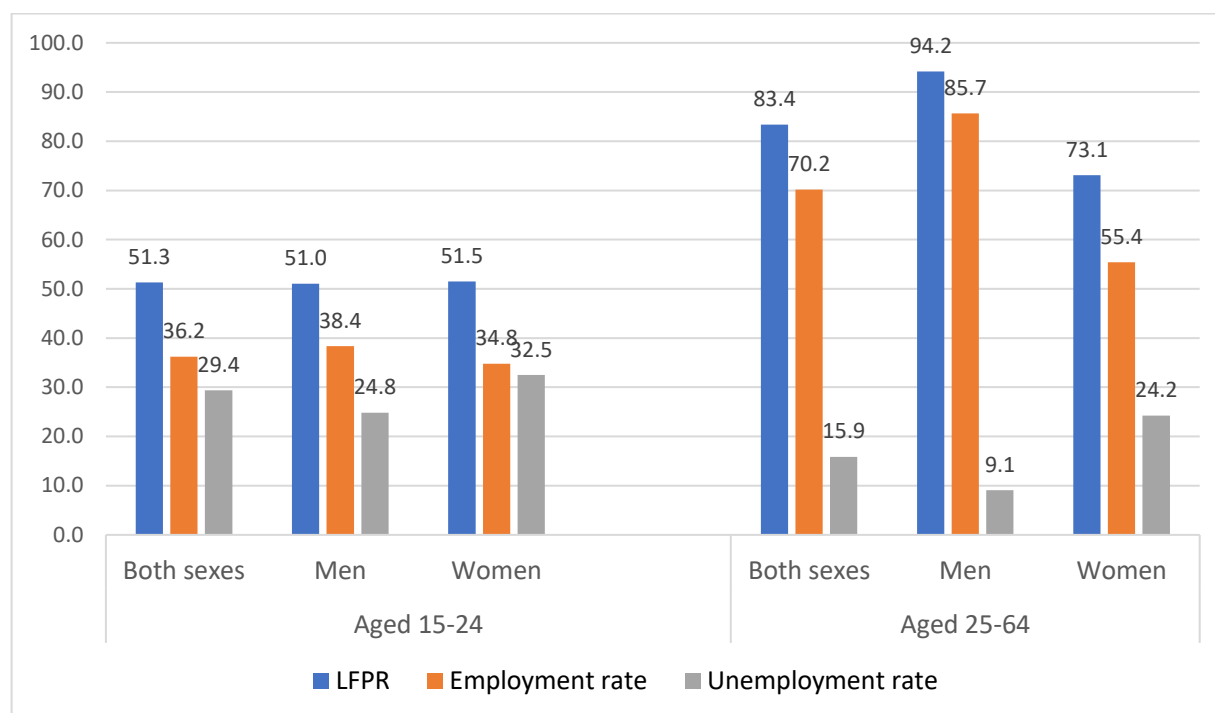
⁶¹ See Section 5.

⁶² For a comprehensive discussion of “The impact of the fourth industrial revolution in job creations and skills in Africa”, see Campbell, Egger, and Ronnås (2018).

⁶³ Information on NEET rates are, unfortunately, not available for urban youth. For the country as a whole ILOSTAT estimated them to be 10.5 per cent (5.7 per cent for men and 15.1 per cent for women) in 2013. However, these comparatively low rates reflect the heavy weight of rural youth, among whom NEET is hardly an issue, in the total youth population.

unemployment was a discrepancy between supply and demand: the number of job-seekers far exceeded the number of jobs on offer (World Bank, 2016).

Figure 5.2. Labour force participation, employment and unemployment rates in urban areas by sex and age groups, 2018 (%)



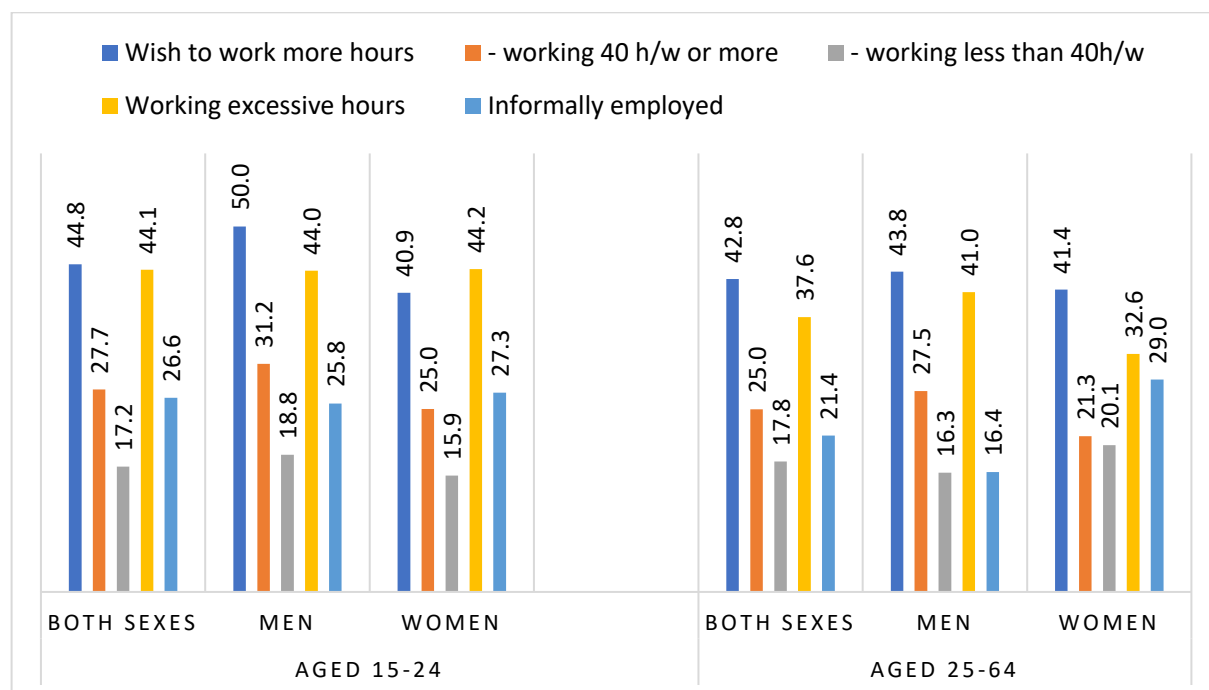
Note: Working age population defined as the 15–64 age group. Labour force participation and employment rates are calculated against the working age population. Unemployment rates are calculated against the labour force.

Source: UEUS (2018), Table 4.1.

Far from all employed young people have good working conditions. Some 45 per cent of them in 2018 wished to work more hours. While this suggests widespread underemployment in terms of hours worked, the vast majority of those wishing to work more hours had already worked 40 hours or more per week (Figure 5.3). Only 17.2 per cent were underemployed in the sense that they were working less than full-time and wished to work more. At the other end of the spectrum, 44 per cent worked excessive hours, that is more than 48 hours per week and often much more. The high share of employed urban youth working excessive hours, together with the high share who already work full-time or more but would still like to work more hours, strongly suggests that a large segment of employed young people in urban areas earn very little and are therefore forced to work excessive hours in order to make ends meet. The proportion of young men and young women who work long hours and still wish to work more is almost the same (Figure 5.3). Poor working conditions and earnings are typically associated with informal employment. It is clear, however, that very low earnings among urban youth are not confined to informal employment but also prevail extensively in formal employment (although it is difficult to draw firmer conclusions given the available data).

The large numbers of young people entering the labour market in urban areas every year need to be matched by a much higher rate of job creation. Given the very high rates of economic growth in recent years, more attention needs to be paid to the structure of growth, to make it more job-rich and geared towards making full and productive use of the extremely valuable human resources that urban youth constitutes. It is not just a question of creating more jobs, however. Dead-end and low-productivity jobs need to be replaced by decent and productive employment that also offers career paths.

Figure 5.3. Working hours and informal employment in urban areas, 2018 (%)



Source: UEUS (2018), Tables 5.27–5.30.

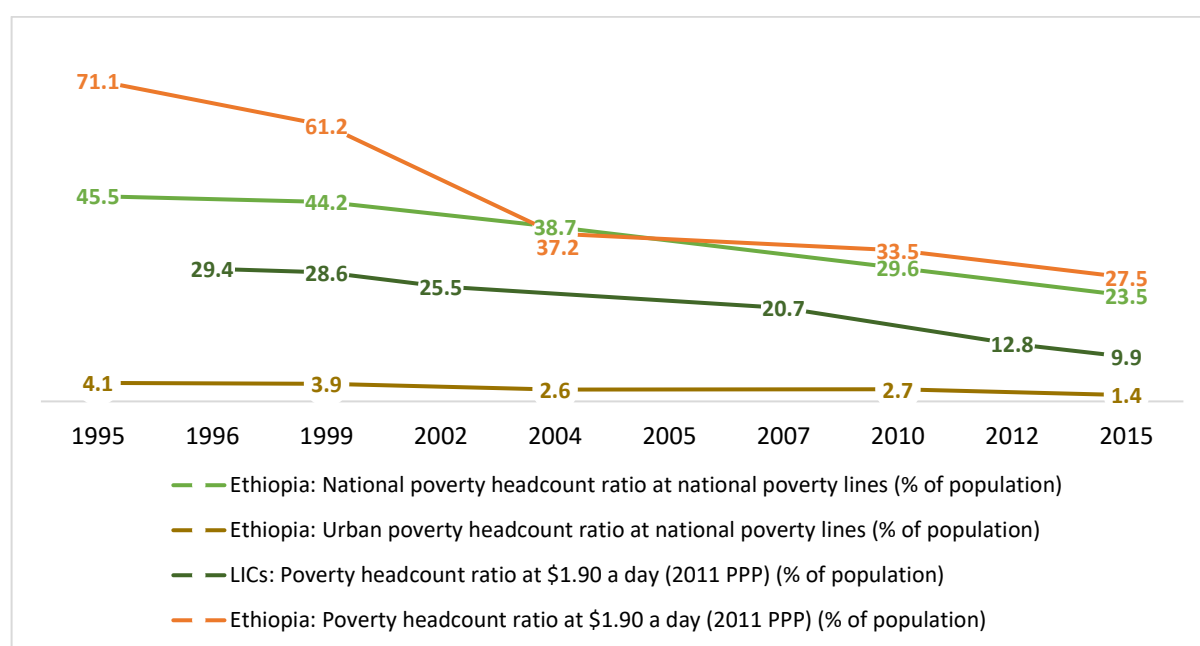
6. Structural transformation through the lens of inclusive, productive employment

The preceding sections in this chapter have described the broader demand- and supply-side conditions that affect the creation of employment and decent work in Ethiopia. This section shifts the lens of analysis and asks: What are main characteristics of the productive transformation of the Ethiopian economy? What are the main opportunities and challenges for making this transformation robust, inclusive and job-rich? It begins by examining poverty reduction trends in Ethiopia, and then examines, in turn, the principal pathways through which people can access productive employment through the main pillars of the economic transformation, the development of agriculture and economic diversification through the development of the non-agricultural sectors.

6.1 Poverty reduction in Ethiopia

Levels of poverty in Ethiopia have fallen over the past decade (see Figure 6.1). That said, although Ethiopia has a relatively low level of poverty for its income level, the extent to which per capita GDP has translated into poverty reduction has been low (World Bank, 2019a, p. 35).

Figure 6.1. Poverty in Ethiopia compared with low-income countries (LICs) (percentage of the population)



Sources: Ethiopian poverty data (at national poverty lines) extracted from Interim Report on 2015–16 Poverty Analysis Study (National Planning Commission, 2017), Table 10; poverty data at \$1.90 per day extracted from World Bank development indicators.

Poverty remains far more pronounced in rural than in urban areas. The percentage of the population living below the national poverty line of less than US\$ 0.6 per day⁶⁴ has declined far more sharply in urban areas, where it fell from 36.9 to 14.8 per cent between 1999–2000 and 2015–16, compared with rural areas, where it declined from 45.4 to 25.6 per cent in the same period. Unsurprisingly, national poverty rates in Ethiopia are determined

⁶⁴ The national poverty line amounts to ETB 3,781 per adult per year in December 2010 prices, or Br 7,184 per adult equivalent per year (in December 2015 prices); this is relatively low (JCC, 2019a and World Bank, 2019a).

largely by the incidence of poverty among the rural population, and poverty remains far more pronounced in rural areas.

Despite rapid agricultural growth, rural per capita consumption ostensibly increased by a mere 1 per cent per year on average between 2011 and 2016 and was tilted towards the richer quintiles (World Bank, 2019a, pp. 41–43). Over the same period, urban per capita consumption grew by 6 per cent per year. The national average was about 2 per cent per year. In fact, growth in rural consumption occurred only in Tigray, Gambella, and Harari, whereas it was negligible in the other regions. The World Bank also reported that the consumption of the bottom 15 percent in rural areas contracted between 2005 and 2016.

The national Gini coefficient increased from 0.29 in 1995–96 to 0.33 in 2015–16. This increase has been driven primarily by an increase in urban inequality to 0.38 in 2015–16, because levels of rural inequality have remained relatively stable at a low level around 0.28, reflecting relatively equal land distribution.⁶⁵ The sustained low rural Gini coefficient is both positive and somewhat unusual and suggests good scope for development of agriculture as a vehicle for broad-based income growth.

The data on economic growth and poverty reduction are somewhat contradictory. In particular, the anaemic growth in rural consumption is difficult to reconcile with the rapid increases in agricultural yields and production, also on a per capita basis, and the fall in headcount poverty. The continued low rural Gini is also difficult to reconcile with declining levels of consumption among the 15 per cent poorest households and other evidence of differentiation of rural households.

Furthermore, even though the Ethiopian government does not collect data on working poverty, the World Bank estimates that more than 13 per cent of workers aged between 30 and 64 are paid wages below the poverty line, with young workers likely to be particularly disadvantaged (Jobs Creation Commission Ethiopia, 2019a, p. 57). As with all other poverty markers – these figures differ across regions – the highest number of low-earning workers are concentrated in the Southern Nations, Nationalities, and People's Region (SNNPR), followed by the city of Dire Dawa and the Benishangul Gumuz region.

The reasons for the stubborn persistence of rural poverty, especially among the lowest consumption quintiles and among rural populations in Ethiopia, are complicated and, as we have noted, contradictory. They would need much more careful examination than is possible here. On one reading, it is likely that the initial levels of development in Ethiopia were so low that growth has increased incomes of the poor, but not yet to the level of pulling them above the poverty line. A lack of physical assets, education, and “remoteness” in terms of distance to towns or poor roads, especially among the poorest, has also had an impact on the persistence of poverty. For the lowest consumption quintiles, it is also likely that their initial development “handicap” was such that they have not been able to benefit from development interventions, such as better roads⁶⁶ or agricultural extension services, which have lifted the less worse-off out of poverty (Dercon, Hoddinott and Woldehanna, 2012). A second issue is likely to be the lack of diversification in the rural economy and spatially differentiated poverty outcomes. It seems that the most significant impacts on poverty have been confined to areas relatively close to urban centres (Hill and Tsehay, 2018). An additional complexity relates to patterns of social exclusion: a deep history of occupational segregation based on ethnicity, clans, and past slavery status limits the labour market opportunities for certain groups in Ethiopia; that is, it restricts their earnings, occupational mobility, and working conditions (Bundervoet and Tas, 2019). As a result, and by reinforcing poverty, social

⁶⁵ Data extracted from National Planning Commission (2017), Table 12.

⁶⁶ On the impact of roads on poverty in Ethiopia, see Nakamura, Bundervoet and Nuru (2019).

exclusion also has an impact on educational opportunities, as well as on access to and uptake of basic services for these groups.

One implication of the modest increases in rural consumption is likely to be increased internal rural–urban migration. The 2013 LFS found that 44 per cent of the urban population were migrants, and that recent migrants were moving predominantly to look for a job. It would appear that rural–urban migration is driven primarily by issues around land scarcity and degradation, lack of employment opportunities, and poverty rather than by employment opportunities in urban areas.⁶⁷ This may also be a major driver of recent spikes in urban unemployment, which increased from 16.9 per cent in 2016 to 19.1 per cent in 2018, with rates of female unemployment more than double the unemployment rates for men (Central Statistical Agency, 2018). Qualitative studies suggest that many of the newer migrants to urban areas work in the burgeoning informal service sector. In the city of Dire Dawa in Ethiopia, for example, which has had one of the fastest rates of urbanization in Ethiopia, most new migrants live in informal settlements (that is, slums) and earn their livelihoods as street vendors, domestic workers, commercial sex workers, and daily wage labourers (Feyissa, Midega and Wakjira, 2018).

To sum up, it appears that if these data on consumption are correct, then increases in rural income have not been sufficient to drive economic diversification based on domestic demand growth. As we point out later, this also has major implications for the growth of the manufacturing and service sectors and, by extension, for employment generation. In the absence of massive export growth, the relatively slow pace of diversification of the rural economy, and the slow manufacturing growth described above can also be explained by the slow growth in personal consumption.

6.2 Accessing productive employment

There are basically three avenues for new entrants into the labour force and for the working poor to access productive employment:

- improved returns to land and labour in agriculture;
- successful entrepreneurship in the non-agricultural sectors; or
- accessing (formal) wage employment in jobs for which the wage is sufficiently high to allow a consumption level above the poverty line.

Possibilities to obtain a productive job depend on a person's employability and opportunities of access through one of the three main avenues outlined above. Education and human resource development largely determine employability, as discussed in Section 3. The focus of this section is opportunities in the context of a structural transformation of the economy and of employment.

The creation of productive jobs through the three avenues mentioned above depends on a successful structural transformation, resting on two main pillars; (i) intensification and transformation of agriculture and (ii) economic diversification through the development of non-agricultural sectors of the economy, not least manufacturing. These two dimensions are highly interdependent. They are explored in some detail below.

⁶⁷ Some of our interviews suggested that the rates of rural–urban migration are being constrained by recent increases in ethnic strife across the country – as a result, migrants (and predominantly young people) may be seeking to move within their regional states.

6.2.1 Increasing returns to land and labour in agriculture

Agriculture remains the main source of livelihood and employment for the vast majority of Ethiopians. In 2016, over 30 million Ethiopians worked in agriculture, accounting for almost 75 per cent of total employment.⁶⁸ Agriculture also accounted for more than half of the total employment growth in Ethiopia between 2004 and 2016, as agricultural employment increased by 6.5 million, that is, by more than 2 per cent per year over the period. The continued rapid growth of agricultural employment was largely supply driven, resulting from a large discrepancy between labour force growth, on one hand, and the creation of productive non-farm jobs, on the other.

Even under the best of circumstances agriculture must continue to serve as an employment buffer for years to come. It will be some time before exit opportunities from agriculture, in the form of productive non-agricultural jobs, will exceed the demographically induced growth of the agricultural labour force and thus result in an absolute decline in agricultural employment. Meanwhile, agriculture will face the dual challenge of both accommodating an expanding work force and increasing productivity and returns to labour to reduce the large number of working poor in agriculture.

Agriculture in Ethiopia can be divided into three broad categories:

- (i) some 15 million private small-scale farms, which account for 95 per cent of the total area, as well as production of grain crops;
- (ii) large-scale commercial farms accounting for 4 per cent of the grain crop production and area;
- (iii) non-sedentary agriculture with a strong dependence on livestock, found mainly in the Afar and the Somali region.

In addition, quasi-industrial horticulture has developed rapidly in recent years in the proximity of Addis Ababa and a few other cities.

In 2017–18 there were an estimated 17.2 million agricultural households, 17.0 million of which were classified as small-scale private farms and 15.7 million cultivated at least some grain crops (Agricultural Survey, 2018c). The vast majority of farms are very small, averaging a mere 1.04 hectares. Eleven million households have less than one hectare of land (*ibid.*). Population growth has inevitably resulted in a diminishing size of holding and increasing land fragmentation, even though the land frontier has been expanded. The pace of this process can be gauged by the fact that the average area grain crop cultivation per farm fell from 0.94 hectares in 2004–05 to 0.81 hectares in 2017–18.⁶⁹

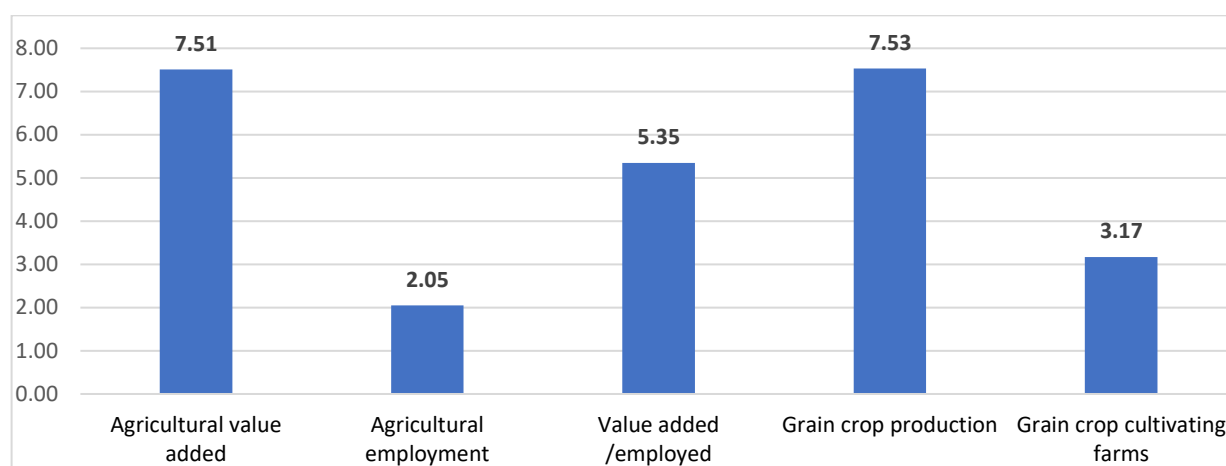
In the virtual absence of irrigation, rainfall determines the agricultural seasons. Ethiopia has one major agricultural season (Mehere) and a minor season (Belge). The Mehere season accounts for more than 90 per cent of the total grain crop production.⁷⁰ The analysis below focuses primarily on the private small-scale farm sector, in view of its overwhelming importance as a source of employment and income.

⁶⁸ HICE (2016a), Table 15.

⁶⁹ Authors' calculations based on the 2004–05 and 2017–18 agricultural surveys. The figures refer to the *Mehere* season and excludes large commercial farms.

⁷⁰ Agricultural Survey (2018c), Table 2.

Figure 6.2. Annual growth (CAGR) of agricultural production, employment and productivity, 2004–16 (%)



Note: Figures for agricultural employment, agricultural value added and value added per employed refer to the period 2004–2016. Grain crop production and grain crop cultivating farms refer to the period from 2004–05 to 2017–18.

Sources: UN National Accounts; HICE (2015–16), Table 15.1; Agricultural Survey (2018a). Authors' calculations.

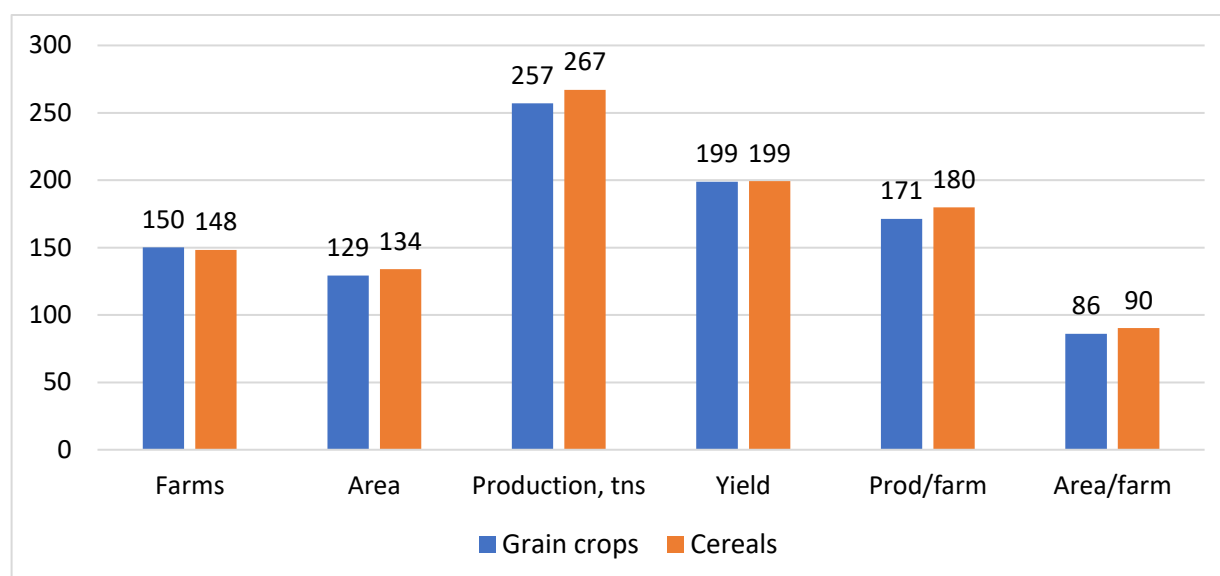
According to national accounts statistics the total value added of agricultural production increased by a staggering 7.5 per cent per year between 2004 and 2016.⁷¹ Agricultural employment increased by an average of 2.05 per cent per year over the same period, implying an annual productivity growth of 5.35 per cent (Figure 6.2). These aggregate figures tell us little about the sources of growth, however, or the extent to which productivity growth was translated into increased labour income. The development of an export-based horticulture industry and the leasing of mostly marginal land to large commercial agricultural enterprises can be expected to have contributed to the rapid growth in agricultural value added. But it would appear that small-holder grain crop production increased at the same pace as overall agricultural value added (Figure 6.3).⁷²

Figure 6.3 provides a bird's eye view of the dynamics of grain crop production, which is the mainstay of small-scale agriculture. The number of farms growing grain crops increased by 50 per cent between 2004–05 and 2017–18. Despite an increase in the total cultivated area by 29 per cent, the cultivated area per farm fell by 14 per cent. Total production of grain crops increased by more than 150 per cent between 2004–05 and 2017–18, mainly due to increases in yields, which doubled over the period, but the total cultivated area also increased by 29 per cent. The growth in yields more than offset the fall in the cultivated area per farm, and average production of grain crops per farm increased by an impressive 71 per cent. The development of cereals closely followed that of grain crops as a whole, but there was a slight shift in the cultivated area away from pulses and oil seeds to cereals, resulting in more rapid growth in cereal production. It is reasonable to assume that the sharp increases in production must have translated into increased returns to labour and household incomes, even though costs of production also increased as a consequence of increased use of inputs.

⁷¹ At constant 2010 prices in national currency. The figure also includes forestry and fishing.

⁷² The accuracy of the very high agricultural growth rates has been called into question. They appear to be at odds with statistics on rural consumption, and it is also not clear how reported changes in production methods and use of cash inputs could trigger such rapid growth (see, for instance, Dercon, and Vargas Hill, 2009, and Dercon, Vargas Hill, and Zeitlin, 2009).

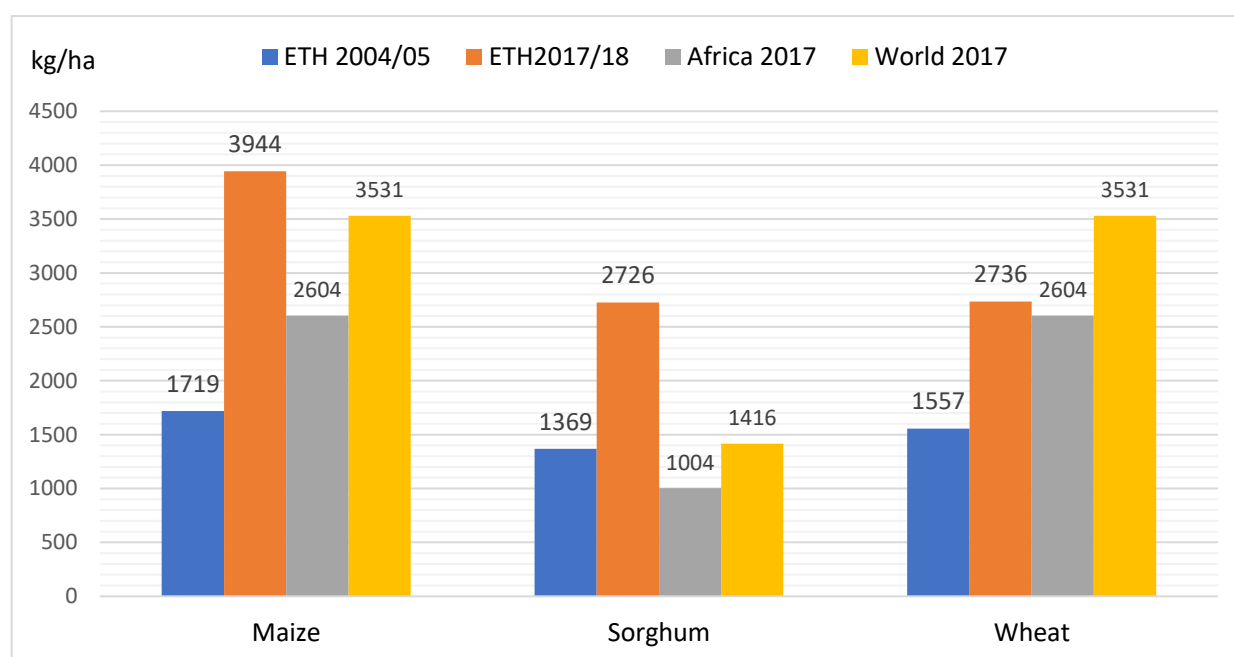
Figure 6.3. Development of production of grain crops and cereals, 2004–05 to 2017–18 (Index: 2004–05 = 100)



Note: Apart from cereals, grain crops also include pulses and oil seeds.

Sources: Agricultural Survey (2005a), Tables 1 and 3; Agricultural Survey (2018a), Vol. I, Table 2. Authors' calculations.

Figure 6.4. Yields of main grain crops in Ethiopia compared with averages for Africa and the World (Kg/ha)

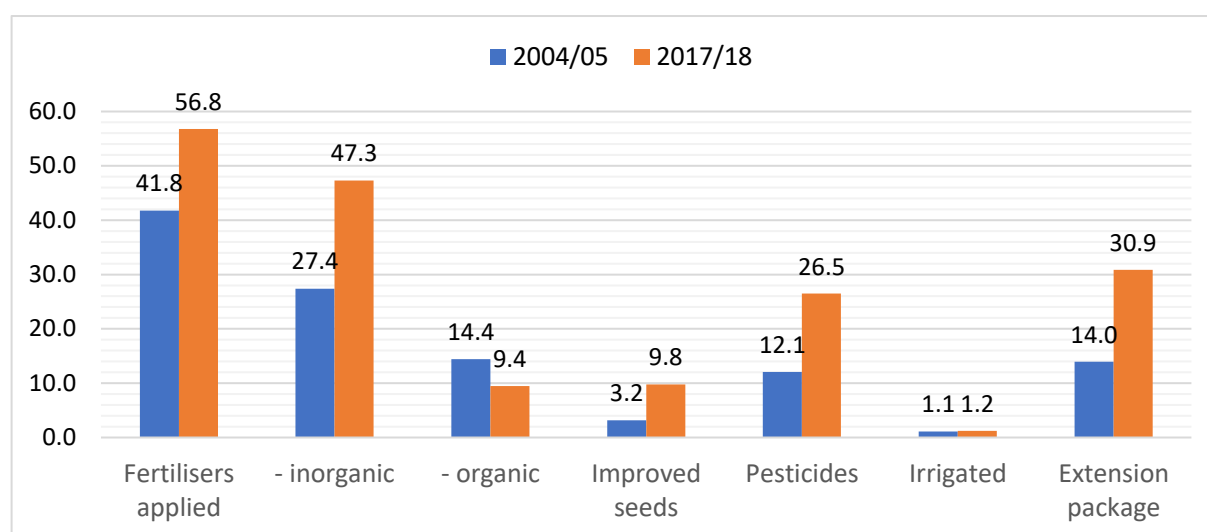


Note: Figures refer to the main Mehere season.

Sources: Agricultural Survey (2005a), Tables 1; Agricultural Survey (2018a), Table 2; FAOSTAT. Authors' calculations.

Average yields of maize almost doubled between 2004–05 and 2017–18, ostensibly reaching 3,944 kg/ha, well above not only the African, but also the global average (Figure 6.4). Yields of sorghum and wheat registered impressive increases as well. While wheat yields were still below the global average in 2017–18, yields of sorghum were reported to be almost twice the global average.

Figure 6.5: Use of yield enhancing cultivation practices in grain crop cultivation in 2004–05 and 2017–18 (Percentage of cultivated area)



Sources: Agricultural Survey (2005b), Table 1; Agricultural Survey (2018b), Table 1. Authors' calculations.

The use of yield-enhancing farm practices and inputs in grain crop cultivation among small-holders increased significantly, but unevenly between 2004–05 and 2017–18 (Figure 6.5). By the latter date fertilizers were applied on 57 per cent of the cultivated area, up from 42 per cent in 2004–05. There was a major shift from organic to inorganic fertilizers over the period.

The use of most other yield-enhancing practices and inputs increased as well, but remain much less widespread than fertilizers. Extension services are comparatively well developed and accessible in Ethiopia and their coverage more than doubled over the period to 31 per cent of the cultivated area. By contrast, the use of improved seeds remains very limited overall (Figure 6.5).

A more detailed analysis yields a more complex picture. By 2017 fertilizers were being applied to 88 per cent of the area under wheat and 78 per cent of the areas under maize and teff, but to only 24 per cent of the area under sorghum. The use of extension services was also much more common in maize and wheat cultivation than in cultivation of traditional crops such as teff and sorghum. Maize was the only crop where improved seeds were used on more than half the cultivated area (55 per cent), in stark contrast to teff, wheat and sorghum, where improved seeds accounted for less than 10 per cent. The lack of research and development into improved seeds suitable for Ethiopian conditions, with the important exception of maize, has been highlighted by others as a major constraint on the intensification and increasing returns to land and labour in Ethiopia (see, for instance, Dercon and Vargas Hill, 2009, and Bachewe et al., 2016). Hence, it appears that increased use of fertilizers was an important factor behind the rapidly increasing yields of major food crops over the past decade.⁷³ Only in the case of maize were yield increases achieved through a broad-based and balanced use of yield-enhancing practices.

⁷³ Increased use of labour, oxen and hoes has also been identified as contributing to increased yields (Dercon and Vargas Hill, 2009).

The irregular and uncertain supply of water remains a major constraint on the development of agriculture in Ethiopia as access to irrigation remains insignificant (as already mentioned):

It largely restricts cultivation to only one crop per year as cultivation is confined to periods with adequate rainfall. Constant regular access to water through irrigation might enable two or more harvests per year.

It reduces the efficacy of other yield-enhancing inputs, in particular the use of high yielding varieties (HYV) of seeds.

It exposes farmers to significant risks of crop failure. This is not only a major cause of impoverishment, but it also seriously limits the ability of small-scale farmers with small economic margins to invest in yield-enhancing cash inputs, obtained more often than not on credit, as this would magnify the consequences of a crop failure.

The effects of climate change are likely to affect Ethiopia more and more in the coming years. Recent studies have shown that the Horn of Africa is getting drier, especially in areas already affected. This will hurt both farmers and pastoralists. The most recent models of climate change seem to suggest that Ethiopia is becoming drier overall. This will probably lead to lower rainfall during the long rains. The eastern part of the region is expected to become significantly wetter, however, with increased rainfall and higher risks of floods (Tierney et al., 2015). These findings have dire implications for a region already grappling with decades of drought, extreme hunger, and rising political instability (Feyissa, forthcoming).

Educational levels among small-scale farmers remain dismally low, despite improvements over the past 10–15 years. By 2017–18 more than half of the holders were still illiterate (down from 69 per cent in 2004–05) and an additional 20.5 per cent had at most three years of formal education, if any. A mere 12 per cent had obtained more than six years of formal education.⁷⁴

Table 6.1. Use of yield-enhancing cultivation practices in grain crop cultivation by level of education among small-holders in 2017–18 (%)

	Educational level of holders, %	Percentage of each educational category using			
		Fertilizers	Improved seed	Pesticide	Irrigation
Illiterate	53.4	38.1	23.1	31.9	8.5
Literate (informal)	8.9	44.3	27.8	37.4	13.0
Grades 1–3	11.6	43.9	31.7	38.3	6.8
Grades 4–6	14.1	44.0	31.0	36.0	7.3
Grades 7–8	6.5	46.0	32.2	40.0	7.4
Grades 9–11	4.1	44.9	32.7	38.5	4.5
Grade 12 completed	0.4	48.6	39.8	42.2	..
Above grade 12	1.0	40.1	33.8	21.5	5.3
Total	100	41.0	26.8	34.4	8.3

Source: Agricultural Survey (2018b), Table 2.

⁷⁴ Agricultural Survey (2005b), Table 2; Agricultural Survey (2018b), Table 2.

As might be expected, level of education matters for the adoption of improved cultivation practices (Table 6.1). Illiterate farmers are less likely to adopt yield-enhancing cultivation practices than those who are literate. However, it would appear that the impact of further education on cultivation practices wanes once basic literacy has been obtained, at least with regard to the use of major cash inputs. Yet, it would be unwise to draw far-reaching conclusions from the figures in Table 6.1. While application of basic cash inputs may not require much formal education, a shift from subsistence-based to market-oriented production is nevertheless likely to require at the very least basic literacy and numeracy skills. Looking ahead, it is difficult to envisage a continued modernization of agriculture without a parallel increase in farmers' education and skill levels.⁷⁵

Information about the market-orientation of small-holder agriculture and challenges for increasing production for the market is largely based on ad hoc studies, most of which are based on dated data. Output markets seem to function reasonably well. A survey in 2007 found that the spreads between farmgate and retail prices of major crops in Addis Ababa were not very wide and were due to high transport costs rather than excessive intermediary margins.⁷⁶ Local facilities for agro-processing are often limited, however. The use of credit remains limited. According to the 2017–18 Agricultural Survey only 18 per cent of small-holder farmers had taken loans in the past year.⁷⁷

Female-headed households, which make up approximately a quarter of all farm households, are disadvantaged in several respects.⁷⁸ They have less access to land and other factors of production than male-headed households. They have less access to formal credit as they are less likely to own and control physical assets that can serve as collateral, which in turn reduces their access to yield-enhancing inputs, such as fertilizers and pesticides, which are typically sold in large quantities for cash up-front.⁷⁹ Demographic factors may play a role as female heads of farms tend to be older, more likely to be illiterate and less likely to be married.

Looking ahead it is reasonable to conclude that sustaining the recent very rapid growth in production and yields will require overcoming some major constraints.

The use of yield-enhancing inputs and practices needs to become more broad-based and balanced. The most acute need would seem to be the development and widespread application of improved seeds, beyond maize, that are adapted to local conditions. This is particularly important as high-yielding varieties of seeds tend to be much more responsive to fertilizers than indigenous seeds.

Climate change poses a threat to agriculture in Ethiopia. A major consequence will undoubtedly be an increased risk of crop failure. High risks of such failure inherent in rainfed agriculture are already a major impediment to sustained rapid development of agriculture. It can safely be concluded that risk mitigation will become increasingly important. Expansion of irrigation, development of resistant varieties of seeds, and innovative insurance schemes are some of the counter-measures that should be explored.

⁷⁵ Unfortunately the annual agricultural surveys do not include any information on the use of the production, e.g. own consumption or sale/barter.

⁷⁶ Dercon and Vargas Hill. 2016. P.43. The farmgate price as a percentage of the retail price in Addis Ababa was on average 67 % for teff, 69 % for wheat and 53 % for maize.

⁷⁷ Agricultural survey 2017/18c. Table 10.

⁷⁸ World Bank 2019c, p.18.

⁷⁹ Authors' interview with the Agricultural Extension Directorate, May 2019. World Bank 2019c, pp. 18 and 24.

A continued intensification of agriculture through the adoption of improved cultivation practices will be inexorably linked to an increased market-orientation. This will require development of an efficient and dense network of downstream linkages, including agro-processing. Empirical evidence from other countries shows that intensification of agriculture and a diversification of local economies through the development of non-farm economic activities, providing, among other things, upstream and downstream linkages to agriculture, are mutually reinforcing and interdependent. Ethiopia is unlikely to be an exception in this regard.

The continued very low levels of education and, indeed, literacy, among farm holders will, unless addressed, inevitably exert a growing constraint on the scope for transforming Ethiopian agriculture away from subsistence orientation into a modern, market-oriented and efficient economic sector.

6.2.2 Economic diversification through development of the non-agricultural sectors

The development of the non-agricultural sectors takes very diverse forms in terms of location, types of activities and size of firms. It ranges from proliferation of non-agricultural micro and small enterprises in rural areas to large-scale, often foreign-funded and export-oriented, manufacturing conglomerates. The shift from agricultural to non-agricultural employment is typically accompanied by urbanization. This link can vary greatly in strength, however. A high concentration of non-agricultural activities in major cities will result in high levels of rural–urban migration, while economic diversification of rural areas and small towns will significantly reduce the pressure to migrate. Such diversification is important, not only to stem rural–urban migration, but also to sustain agricultural development through improved market access and the creation of upstream and downstream value-added chains. When viewed from the perspective of the individual agricultural household the importance of non-farm employment opportunities becomes evident. It offers an alternative and complementary source of deployment and income for the household’s labour resources at little or no alternative cost, serves to even out the considerable seasonality in labour demand inherent in rainfed agriculture and makes it possible to increase household income security by putting “the eggs in more than one basket”.

A clear distinction must be made between opportunity-driven and distress-driven structural transformation. Opportunity-driven transformation can serve as a powerful mechanism for increasing overall economic growth and productive employment. A transfer of surplus labour from agriculture to non-agricultural sectors with much higher productivity results in important direct productivity gains, while also resulting in higher productivity for those who remain in agriculture.

By contrast, relentless population growth combined with stagnant subsistence-oriented agriculture or highly unequal access to land results in a vicious circle of falling returns to labour in agriculture, a pauperization of agricultural households and landlessness. Sheer necessity then pushes people out of agriculture, resulting in distress-migration and supply-driven growth of lower-end services, where entry thresholds are low. The latter, often labelled “premature” urbanization is hardly an example of productive transformation, but rather of a lack of it, combined with strong demographic pressure. In aggregate statistics the two types of transformation resemble each other. However, while the first is characterized by economic growth, increasing productivity at both source and destination, and falling numbers of working poor, the latter is associated with employment growth at the expense of productivity in low-end services, lacklustre economic growth and stagnant or increasing numbers of working poor.

Egalitarian land distribution and very high rates of agricultural growth over the past 10–15 years suggest ideal preconditions for an opportunity and demand-driven structural transformation in rural Ethiopia. Yet the two types of transformation may well exist in

parallel and they need to be distinguished as far as possible: one leads to productive jobs, while the other does not.

Lack of statistics precludes a detailed up-to-date analysis of the development of the non-agricultural sectors. The latest nationwide labour force survey was undertaken in 2013.⁸⁰ Statistics based on enterprise surveys are patchy and for the most part cover only manufacturing. Two sets of quasi-regular surveys undertaken by the Central Statistical Agency and covering small-scale and large and medium scale manufacturing, respectively, provide the main source of statistical information. Regular statistics on enterprises in the service sectors, which account for the majority of establishments and of non-agricultural employment, are not produced. The World Bank's enterprise surveys cover both manufacturing and services firms, but exclude firms with fewer than five employees and informal firms. The National Bank of Ethiopia publishes some information on micro- and small enterprises that have benefitted from credit. Finally, the Urban Job Creation and Food Agency collects data on micro- and small enterprises, which are neither publicly available nor disaggregated.

A snapshot of the main features of the structural transformation between 2005 and 2013 from an employment perspective is given in Figure 6.6. The share of agriculture in total employment fell from 80.2 to 72.7 per cent over the period. However, the growth in the share of non-agricultural employment by 7.5 percentage points was to a large extent due to apparently very rapid growth in employment in private households – that is, domestic servants and helpers – from 0.8 to 7.3 per cent.⁸¹ Growth of the shares of other non-agricultural sectors was very modest, for example, manufacturing rose from 4.9 to 5.1 per cent.

The growth of non-agricultural employment was to a large extent accompanied by urbanization and the share of urban employment in total employment increased from 11.0 to 15.6 per cent between 2005 and 2013. In rural areas, employment remained overwhelmingly agricultural. Apart from employment in private households, non-agricultural employment was confined largely to some employment in manufacturing (cottage industry) and in trade, none of which exceeded 3 per cent of total rural employment.⁸² More recent data from urban labour force surveys suggest that urban employment increased by 4.6 per cent per year between 2012 and 2018, well above the national rate, but less than between 2005 and 2013 (8.0 per cent).⁸³ At the same time, it would appear that the share of manufacturing in total urban employment fell from 14.4 per cent in 2013 to 12.3 per cent in 2018.

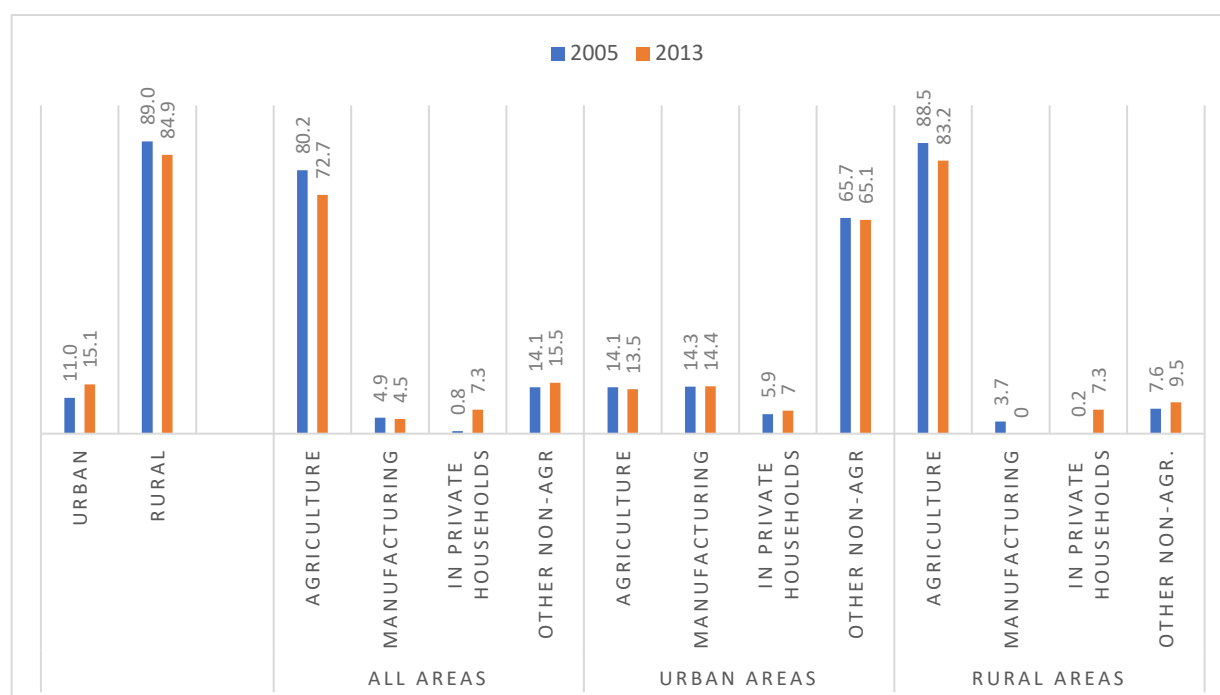
⁸⁰ Data from more recent household, income, consumption, and expenditure surveys are much less detailed and not comparable with data from the labour force surveys.

⁸¹ It seems likely that differences in enumeration practices would account for a major part of the increase in employment in domestic households.

⁸² The general picture of a rather modest growth of the non-agricultural sectors is confirmed by data from the household income, consumption, and expenditure surveys of 2004 and 2016, which using somewhat different definitions and methodology arrived at a share of agriculture in total employment of 82.5 per cent in 2004 and 73.6 per cent in 2016 (HICE, 2004; HICE, 2016).

⁸³ UEUS (2012), Table 4.1; UEUS (2018), Table 4.1.

Figure 6.6. Distribution of employment by rural and urban areas and by main economic sectors in 2005 and 2013 (%)



Sources: LFS (2005), Table 5.4; LFS (2013), Table 5.3.

Other studies confirm the picture of a still very low level of economic diversification in rural Ethiopia. A study based on a survey from 2011 on non-farm income and rural labour markets found that although a quarter of all the surveyed rural households derived some income from own (non-agricultural) enterprise activities and that more than a fifth were engaged in agricultural wage employment and 8 per cent in non-agricultural wage employment, these off-farm activities accounted for a mere 18 per cent of total household earnings, while on-farm agricultural activities made up 82 per cent of total household earnings (Table 6.2).

Table 0.1. Sources of income among rural households in 2011 (%)

	Households earning some income from	Contribution to total income
Crop cultivation	94.1	71.4
Livestock	60.2	10.7
Agricultural wage income	21.4	6.6
Non-agricultural wage income	8.1	3.1
Income from own enterprise	94.1	71.4

Source: Bachewe et al. (2016).

The reliance on off-farm economic activities was found to differ between older and younger heads of households, as well as by gender. Off-farm income made up 21 and 23 per cent of the total income for young male and young female headed households,⁸⁴ respectively, compared with 15 and 17 per cent, respectively, of the male and female heads of households aged above 35. This may reflect a stronger entrepreneurial drive and ability among young heads of households, but it may also be due to a necessity to supplement farm income as

⁸⁴ “Young” was defined as below the age of 35.

younger households often own less land (Bachewe et al., 2016. p. 8). Indeed, the survey found that reliance on off-farm economic activities was negatively correlated with both household income and land endowment. Non-farm income accounted for 28 per cent of total income among the poorest households, compared with about 16 per cent in the richest two quintiles (Bachewe et al., 2016. pp. 7–8). Non-agricultural employment, in the form of both wage employment and self-employment, was found to be positively correlated with education, while wage employment in agriculture seems to serve as an employment of last resort for those who cannot make ends meet on their own farm and who lack the education to take up non-agricultural employment.

Recent studies suggest that the job creation record of micro- and small enterprises in Ethiopia remains rather poor (Oqubay 2019a and Oqubay 2019b). For instance, a World Bank study estimated that firms with more than 100 employees accounted for 74 per cent of net manufacturing employment between 2011 and 2015 (World Bank, 2015b, p. 25). Furthermore, very few MSEs have managed to graduate to medium-sized enterprises – between 2011 and 2014 the share was less than 3 per cent in Addis Ababa (Tony Blair Institute of Global Change, 2018). Another source suggests that, despite increased allocation of credit, job creation in micro- and small enterprises has actually decreased in recent years.⁸⁵

Yet, small firms continue to provide by far the most important source of non-agricultural employment. A comparison of data from the 2016–17 small-scale manufacturing survey and the 2018 medium- and large-scale manufacturing survey revealed that firms with fewer than 10 employees accounted for over 90 per cent of total employment and more than 80 per cent of permanent wage employment in manufacturing (Table 6.3).

Table 6.3. Number of establishments and employment in the manufacturing sector

	Establishments with 0–9 employees	Establishments with 10 employees or above
Number of establishments	142 968	3 626
Number of persons engaged*	2 140 668	224 711
Number of permanent employees	831 577	181 246
Permanent employees as a proportion of persons engaged	38.9%	80.7%

Notes: Persons engaged includes: unpaid family workers, unpaid and paid apprentices, permanent and paid employees, as well as seasonal and temporary workers.

Source: Data for small-scale manufacturing industries extracted from Central Statistical Agency, Survey on Small-Scale Manufacturing Industries, 2016–17 (Summary Tables 3.1 and 3.2); Data for medium and large-scale manufacturing extracted from Central Statistical Agency, Survey on Large and Medium Scale Manufacturing and Electricity Industries, 2018 (Table 4.15).

Anaemic economic diversification in rural areas results in increased supply pressure on the urban labour markets through rural–urban migration in search of work. Despite rapid employment growth in urban areas, urban labour markets are ill-equipped to meet this challenge. Efforts to speed up industrialization by attracting FDI and promoting export-oriented manufacturing have so far yielded limited results in terms of both exports and employment. Indeed, urban manufacturing employment appears to have fallen as a share of total urban employment in recent years, while the construction boom, which never created much employment, is now past its peak. Indeed, an urban labour force survey carried out in 2018 revealed a rather grim picture (Table 6.4).

⁸⁵ According to the National Bank of Ethiopia job creation in MSEs fell from 2.8 million to a paltry 144,000 in 2017–18, while the number of start-ups declined by half, from 271,000 to 144,000. However, these figures appear too extreme to be taken at face value.

Table 6.4. Labour force participation and employment characteristics in urban areas in 2018 (15–64 age group; %)

	Sex			Age group	
	Both sexes	Men	Women	15–24	25–64
Labour force participation rate	72.0	80.6	64.7	51.3	83.4
Employment rate	58.1	70.7	47.3	36.2	70.2
Unemployment rate	19.3	12.2	26.8	29.4	15.9
<i>As % of employed</i>					
Would like to work more hours, total	43.3	44.9	41.2	44.8	42.8
working less than 40 h/w	17.7	16.7	18.9	17.2	17.8
working 40 h/w or more	25.6	28.1	22.4	27.7	25.0
Working excessive hours	39.1	41.5	35.9	44.1	37.6
Informal employment	22.4	17.9	28.6	26.6	21.4

Source: UEUS (2018), Tables 4.1, 5.27, 5.28 and 5.30.

Some 19 per cent of the urban labour force (aged 15–64) were unemployed in 2018. Unemployment was particularly high among women, at 27 per cent, and among young people, at 29 per cent. On top of this, there is likely to have been a large number working age people who would have been available and willing to work, but who had given up searching for work and retreated into inactivity.⁸⁶

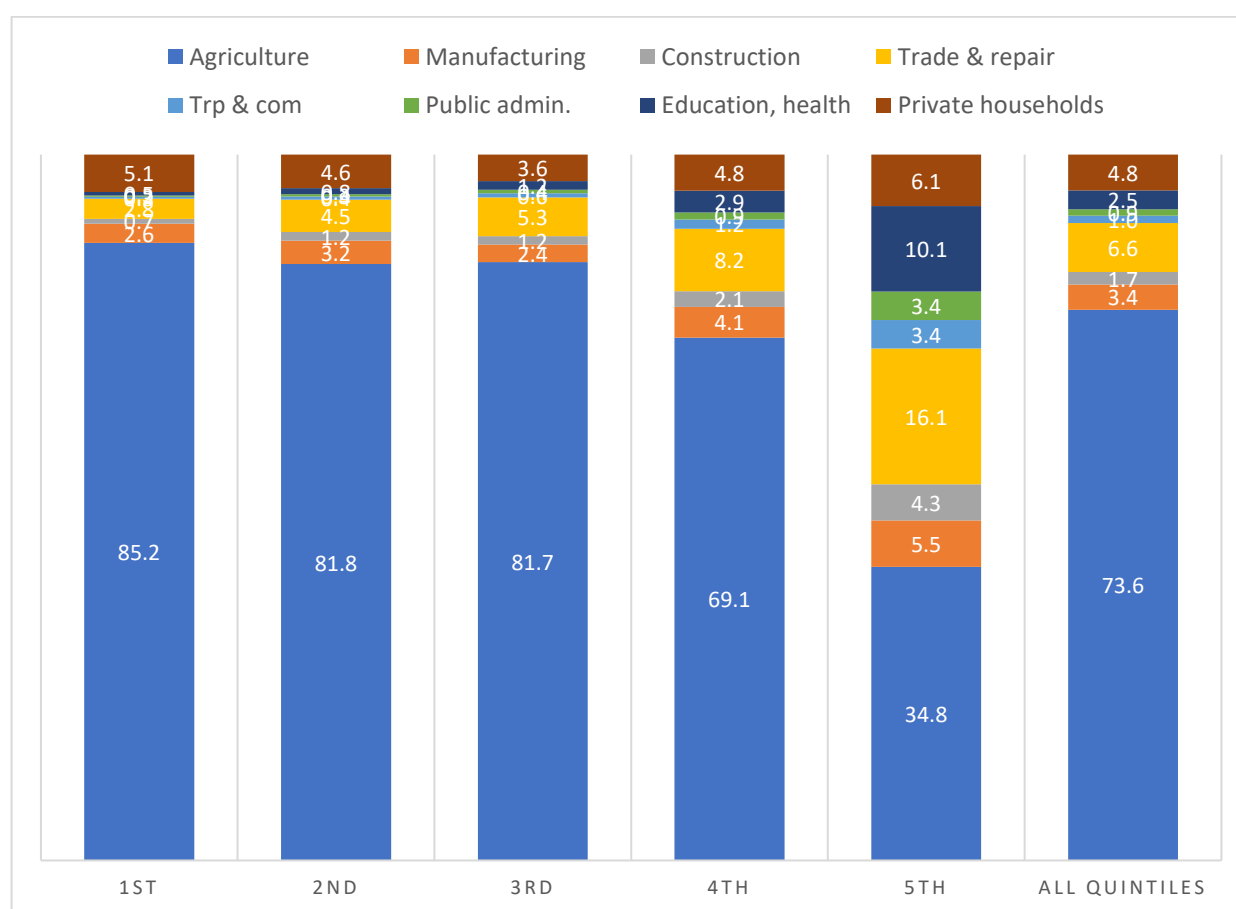
Far from all urban employment amounts to full and productive jobs. More than 40 per cent of employees stated that they would like to work more hours (Figure 6.4). However, far from all who wished to work more hours were underemployed in terms of hours worked. Indeed, more than a quarter of the employed – that is 59 per cent of those wishing to work more hours – already worked 40 hours or more per week. Working long hours and wishing to work even more hours suggests employment at very low levels of productivity and returns to labour per hour: in other words, jobs that are so poorly remunerated that working excessive hours becomes necessary in order to make ends meet. Indeed, 40 per cent of all employed had worked excessive hours – defined as more than 48 hours/week – in the week preceding the survey. The comparatively low headcount poverty rates in urban areas – about 10 per cent in 2016 – should be seen against the high proportion of the employed working excessive hours. At the other end of the spectrum, 18 per cent worked less than full time and would like to work more, in other words, were time-underemployed. Formal employment ostensibly accounted for more than three-quarters of all urban employment in 2018. Clearly, access to a formal urban job does not guarantee decent earnings and working conditions.

Despite often very low wages and returns to labour in the non-agricultural sectors, results from the 2006–17 HIES confirm the twin conclusions that, by and large, (i) access to wage employment (with the important exceptions of agriculture and private households) and (ii) access to employment in the non-agricultural sectors are important avenues for obtaining productive employment. In 2016–17 more than 85 per cent of all those employed in the poorest household quintile worked in agriculture, as against 35 per cent of the employed in the richest household quintile (Figure 6.7). The dominance of agriculture as a source of employment and the close correlation between employment in agriculture and low income is clear from the fact that agriculture accounted for more than 80 per cent of total employment among the bottom 60 per cent of households.

⁸⁶ Unfortunately the survey did not capture this group.

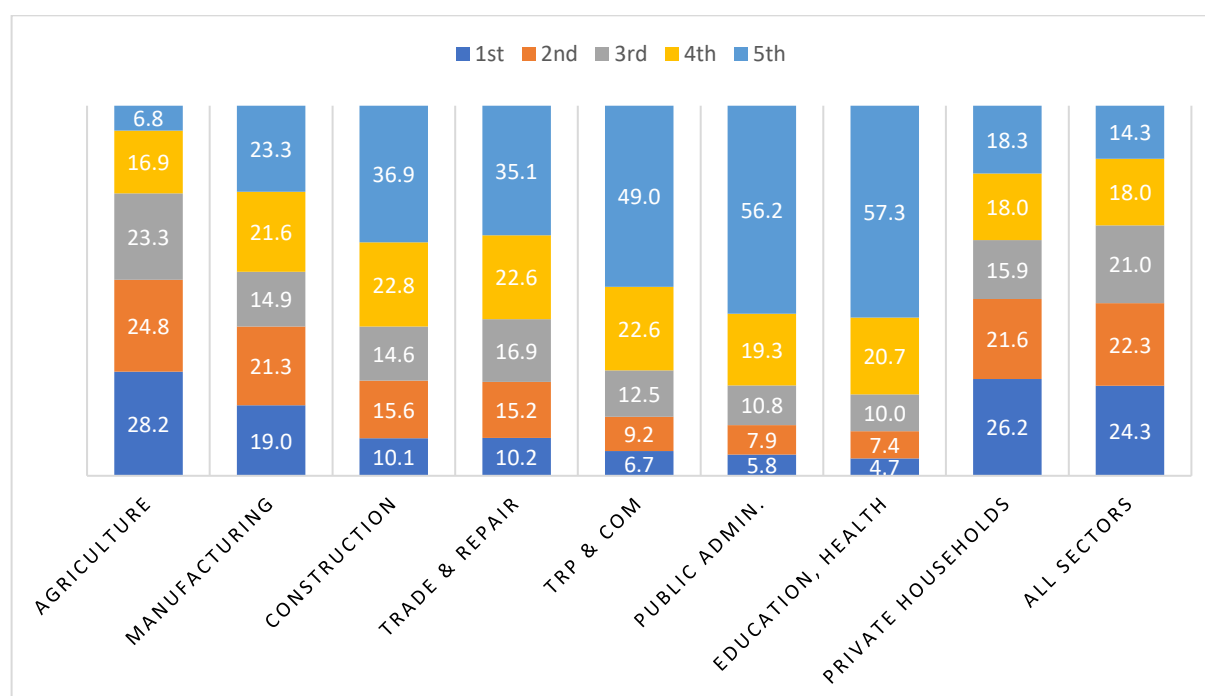
An examination of the distribution across household consumption quintiles of employees in different sectors casts additional light on the role of different economic sectors as avenues to greater prosperity (Figure 6.8). In 2016–17 well over half of all public sector employees in public administration, education, and health care belonged to the richest household quintile, compared with less than 7 per cent of those employed in agriculture. Those employed in transport and communication, trade and construction also generally came from the richest and second richest household quintiles. By contrast, those employed in manufacturing were distributed fairly equally across household quintiles. Indeed, 40 per cent of manufacturing employees came from the 40 per cent poorest households. Two reasons, which are not mutually exclusive, might explain why manufacturing employment seemingly does not bring greater prosperity. First, non-mechanized rural cottage industries still remain widespread, and second, the recent proliferation of labour-intensive large-scale manufacturing for export, competing with low-cost labour, might lock people in poverty rather than provide an escape from it.

Figure 6.7. Sector distribution of employment by household consumption quintiles (%)



Source: HICE (2016b). Authors' calculations.

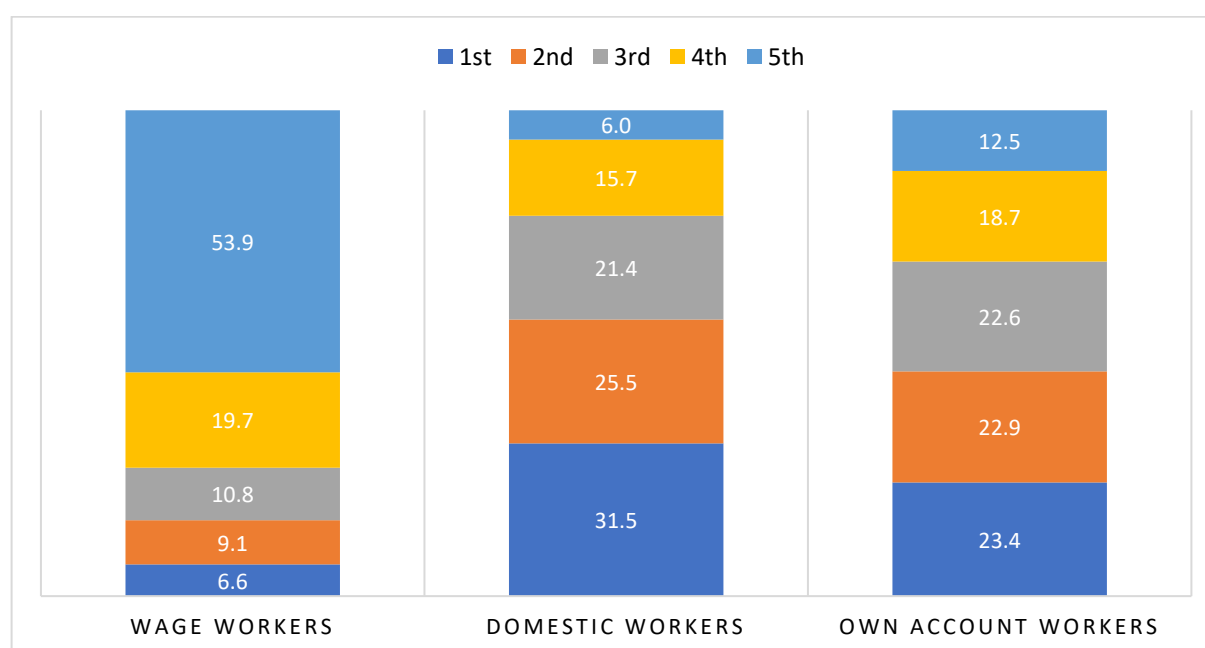
Figure 6.8. Share of household expenditure quintiles in total employment by economic sectors



Source: HICE (2016b). Authors' calculations.

Nevertheless, despite generally low wage levels, access to wage employment is by and large associated with greater household prosperity (Figure 6.9). Well over half of all wage employees (excluding workers in private households) belong to the richest household quintile, while less than 7 per cent come from the poorest quintile. By contrast, work in private households clearly pays poorly and is an option for poorer households. Own account employment presents a mixed picture and the figures do not really yield much insight, largely because the data source does not distinguish between agriculture and own account employment in the non-agricultural sectors.

Figure 6.9. Employed by household consumption quintiles and employment status in 2016–17 (%)



Source: HICE (2016b). Authors' calculations.

Poor education imposes a major constraint on access to non-agricultural employment. According to the 2016–17 HICE survey, only about half of all employed were literate. A mere 37 per cent had obtained at least four years of formal education, essential for basic literacy and numeracy skills, 18 per cent had completed eight years of primary education and 11 per cent had at least lower secondary education (Table 6.5). But access to jobs in most non-agricultural sectors requires at least some basic education. Upper secondary education is required for most public sector employment, not least in education and health care. Educational requirements for entry into trade, transport and communications, and construction are somewhat lower, but still beyond the reach of much of the labour force, while the low levels of education among those working in manufacturing probably reflect the continued high incidence of primitive cottage industry in this sector, but also the generally low level of technology in manufacturing. Access to wage employment generally requires at least eight years of primary education, but often more, thus excluding over 80 per cent of the labour force.

Table 6.5. Employment by highest level of education obtained and economic sectors in 2016–17 (%)

	Agriculture	Manufacturing	Construction	Trade	Transport & communications	Education & health care	All sectors	Wage employment
Literate	42.3	48.9	81.4	64.4	77.5	96.0	49.0	85.0
4 classes or more	28.4	43.8	73.5	56.8	68.9	94.3	37.2	81.1
6 classes or more	16.4	35.3	59.6	44.9	57.3	92.5	25.7	75.6
8 classes or more	7.8	26.2	47.3	32.6	41.9	89.0	16.7	68.7
Lower secondary or more	3.6	17.3	33.6	23.0	29.1	83.6	11.3	61.2
Upper secondary or more	1.0	9.3	18.3	11.2	15.6	75.2	6.7	46.3
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: HICE (2016b). Authors' calculations.

Not only do inadequate education and, indeed, literacy skills, impose a major and binding constraint on a large part of the labour force when it comes to accessing non-agricultural and wage employment, but insufficient education levels among the labour force are also likely to impose a major constraint on the scope for economic diversification, entrepreneurship and enterprise development and increased wage employment. The constraint on expanding wage employment is clear from Table 6.5. Although more difficult to substantiate statistically, low levels of education probably also impose a constraint on non-agricultural entrepreneurship and SME development and on self-employment as a vehicle to escape income poverty. Some ethnographic studies reaffirm this, but also point to the role played by social networks in providing support to entrepreneurs (especially young ones) in expanding and consolidating their businesses.⁸⁷

⁸⁷ See the discussion on education and entrepreneurship in di Nunzio (2017), p. 98; di Nunzio (2019). For a discussion on youth, education and unemployment see Mains (2012).

The seemingly lacklustre growth of employment in the non-agricultural sectors of the economy, in particular in SMEs and outside the large cities is somewhat astonishing considering that rapid agricultural growth would be expected to have created conducive conditions through a broad-based increase in domestic demand and, not least, in view of the fact that Ethiopia has pursued ambitious and pro-active industrial policies, focusing, for example, on SME development.

The primary policy governing MSMEs in Ethiopia is the Micro and Small Enterprise Development Policy and Strategy of 2010–11,⁸⁸ which sets out the terms on which support is to be provided to micro and small entrepreneurs in the areas of skill training, marketing, access to finance, production support, and work premises support. The policy is administered by the Urban Job Creation and Food Security Agency, while overall supervision is provided by a micro and small enterprise (MSE) council chaired by the deputy prime minister. More recently, a ten-billion-birr Youth Revolving Fund was created in the 2017 budget to address challenges of job creation. The stated objectives of this Fund were to “assist youth to employ their capabilities in creating job opportunities” and to “provide financial assistance for organized income generating activities conducted by youth”.

Several reasons can be put forward to explain the apparent lack of dynamic growth, and employment growth, in the non-agricultural sectors.

Discretionary schemes and support do not compensate for general weaknesses in the business environment. As detailed in Section 2, Ethiopia scores poorly in international surveys of the business environment; it took 159th place among 190 countries in 2019 (World Bank, 2019d). Red tape in connection with starting a business and obtaining building permits, as well as poor access to finance, irregular electricity supply and cumbersome trading across borders are among the most severe and frequently mentioned constraints (see also World Bank Enterprise Survey, 2015).

The weak development of small and medium sized enterprises (SMEs) is an Achilles’ heel. Not only are such firms crucial from an employment perspective, but they are fundamental for vertical economic integration, linking large and small firms through value chains and as channels for diffusion of technology and know-how.⁸⁹ Two constraints on SME development deserve particular attention:

- (i) Finance is geared mainly towards micro-enterprises and large enterprises, while lack of access to finance remains a key constraint for small and medium-sized enterprises. Small enterprises that grow are thereby disqualified for micro-finance, yet cannot access regular bank loans. In rural areas, which are plagued by issues of high collateral and poorly designed financial instruments, this has had particular implications for the diversification of the economy (Berhane and Abay, 2019).
- (ii) Entrepreneurship and business management capacity remain underdeveloped. Such skills, and low levels of education more generally, can be formidable constraints for setting up and running a business and for graduating from a micro-enterprise to an SME.

Schemes to promote MSEs are not always effective or well-targeted and defaults are common. The MSE sector is also politically contentious. As the Micro and Small Enterprise

⁸⁸ Available at:

<https://www.cmpethiopia.org/content/download/2366/10048/file/MoUDH%20MSE%20Development%20Policy%20&%20%20Strategy%20280416.pdf>.

⁸⁹ The below points are drawn from interviews conducted by one of the authors – for details please see Sarkar, Ronnas and Fedi (2019).

Development Policy and Strategy notes, there was also a political rationale for encouraging MSEs – it was intended to boost political support in urban areas.⁹⁰

Finally, some stakeholders reaffirmed the findings from previous ethnographic studies which had suggested that entrepreneurial networks are key in helping young entrepreneurs sustain and grow businesses; in the absence of mechanisms to develop those social networks, MSE development policies often come up short and are co-opted for other political purposes (see Mains, 2012; di Nunzio, 2015; di Nunzio, 2019).

6.2.3 Some are left behind

In tandem with the generally positive employment and poverty trends, driven by agricultural development and structural change, it would appear that there is a counter-current of perpetuated deprivation and that parts of the poor population are being left behind. An analysis based on the household income, consumption and expenditure surveys revealed that the consumption of the poorest 15 per cent of rural households declined between 2005 and 2016 (World Bank, 2019a, p. 63).

Rapid population growth increases the pressure on scarce land resources, resulting in land fragmentation, diminishing holding sizes, and, for some, near landlessness. High intra-household dependency ratios (many mouths to feed but few breadwinners), resulting from high fertility rates, significantly reduce the ability of impoverished agricultural households to save or to invest in their children's education and in tools and technology that would enhance the productivity of their labour and their land. Poverty forces children into child labour and makes it difficult for them to acquire adequate education and skills, which in turn severely reduces their prospects of accessing productive employment and escaping poverty as adults, which, together with high fertility associated with low education, perpetuates poverty, transmitting it from one generation to the next. This vicious circle is not new to Ethiopia or to Africa more generally. Over the past 10 to 15 years large and increasing numbers of Ethiopian households, albeit far from all, have managed to break out of this vicious circle. Strong, targeted measures will be needed to effectively address a remaining hard core of extreme poverty.

⁹⁰ The Policy states (p. 3): “There is also a political justification for providing policy and strategy related support to MSEs. Just as farmers are the basis for a developmental state (developmental administration) in rural areas that will fulfil the interests of rural residents whereby a crucial role is to be played by rich farmers, achieving this would give impetus (for the governing party) to achieve progress in terms of democracy and development and muster the support of the urban population.”

7. The road ahead: Challenges and responses

Ethiopia has made substantial progress towards achieving Sustainable Development Goal 8: “*achieving sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all*”. Between 2005 and 2015 the number of productive jobs⁹¹ is estimated to have increased from 19.6 to 32.6 million and the share of the labour force in productive employment increased from around 60 to almost 70 per cent. This achievement is all the more impressive as it took place in the context of very rapid labour force growth, in a period punctuated by climatic shocks and political instability in the broader Horn of Africa. Rapid growth in the yields of the main food crops helped to lift a large part of the rural population out of working poverty, at the same time as investment-led growth in urban areas increased the availability of productive non-agricultural jobs. Ethiopia scored well on other SDG 8 indicators as well. Since 2011–12 per capita GDP growth has averaged 7.4 per cent, well above the SDG benchmark of 7 per cent. Similarly, the annual growth rate in output per worker has been among the highest in sub-Saharan Africa, although, as this chapter argues, commensurate gains in material living standards have not always been observed. The unemployment rate is also comparatively low in Ethiopia, although the relevance of this indicator in a still predominately agrarian economy is limited as in rural areas and among poor households the deficit of productive jobs overwhelmingly takes the form of working poverty rather than open unemployment.

Ethiopia can look back on almost two decades of successful development. It has made major advances in human development, intensification of agriculture and, somewhat more unevenly, in economic diversification and creation of non-agricultural employment. Yet, the past is a deceptive guide to the future; the main drivers of growth over the past 10–15 years are unlikely to be able to sustain growth to the same extent in coming years. Substantial challenges still need to be overcome if the ambitious SDG goal of achieving productive employment and decent work for all by 2030 is to be achieved.

First, more productive jobs need to be created, and faster. A simple projection suggests that the number of productive jobs needs to increase by almost 2.8 million per year in the coming decade; that is, twice as many as were achieved annually in the period 2005–15. Approximately 2 million of these will need to be new jobs, mainly to provide work for the approximately 1.8 million new entrants into the labour force each year, but also to eliminate unemployment. In addition, some 820,000 working poor will need to access productive employment annually in order to eliminate poverty and working poverty. This can be achieved either by increasing productivity and returns to labour in their current jobs, which are mainly in agriculture, or by providing the working poor with access to new productive jobs created elsewhere in the economy.

Ethiopia will benefit from a strong demographic tailwind in the years to come, which will ease the task of productive job creation in two main ways. The labour force’s annual rate of growth will fall from 3.7 per cent per year in 2005–15 to an estimated 3.1 per cent per year, thus somewhat reducing the supply pressure on the labour market. At the same time, the dependency ratio is expected to fall from 0.77 in 2020, to an estimated 0.67 in 2030. With fewer mouths to feed, poverty will decline and the economic margins of poor households will increase. As a result, they will have a bit more money to invest in their children’s education or in on-farm or off-farm economic activities.

Second, the economic transformation faces mounting structural and macroeconomic challenges. Over the past decade, economic growth has to a large extent been driven by

⁹¹ Defined as jobs yielding an income sufficient for the worker and their dependents to maintain a consumption level above the poverty line.

publicly funded investment in physical infrastructure. This is not sustainable, and growth needs to become more broad-based. But the manufacturing sector has until recently remained sluggish. The initial easy gains in agriculture have been reaped and the fertilizer-driven increases in yields and expansion of the cultivated area have largely run their course. To sustain rapid growth in agriculture a more comprehensive approach is needed to support a transformation towards modern and intensive small-scale farming. Structural weaknesses have appeared in the form of a markedly dual character of the economy. On one hand, there are an increasing number of export-oriented and often foreign-funded firms (and farms) and on the other hand a horizontal growth of micro-enterprises. Small and medium enterprises, in particular, remain underdeveloped, and this constrains vertical, and to some extent horizontal, economic integration. Closely linked to this is the need for economic diversification and creation of non-farm productive jobs outside the big cities.

Third, advances in education have been impressive, but not inclusive. Illiteracy remains widespread among the adult population and the education system has a weak middle: that is, major gains have been achieved in primary education but secondary education and TVET have been neglected. There is also a strong bias towards urban areas and current policy continues to favour tertiary education at the expense of broad-based development of secondary education and the goal of universal primary education remains distant in rural areas. This is out of tune with Ethiopia's developmental ambitions, as inclusive access to adequate education and training is essential for access to productive employment and decent work. As it stands, large parts of the rural population, especially young people from poor households, are at risk of being left behind. Furthermore, even though the gender gap in education has been closed among young people, women continue to be distinctly disadvantaged in the labour market and at work.

Finally, young people who have started, or will start their working lives in the coming decade will make up over 60 per cent of the country's work force by 2030. Sustaining the present momentum of rapid productive transformation and achieving the SDG goals, including SDG 8, will depend on the successful integration of the young into the economy and the world of work and on making it possible for them to realize their full potential and move the country forward through access to productive and decent employment.

Each of these challenges is discussed in greater detail below, along with some policy recommendations.

7.1 The economic transformation needs to be put on a more secure footing

The exceptionally high rates of economic growth since 2002 have taken most observers by surprise. Although growth was fuelled by rapid agricultural growth and in later years by expansion of the non-agricultural sectors of the economy, Ethiopian growth has been lopsided and partial, and is relatively fragile. Major qualitative changes in the nature of the structural transformation are needed to maintain the momentum of rapid economic development in the years ahead.

7.1.1 The public investment led growth of the past decade is not sustainable and growth needs to be put on a different and more broad footing

Productivity growth in agriculture has been a main driver of economic growth since 2004. Since 2011 this role has diminished somewhat as construction, driven by massive public investments in infrastructure, has emerged as a major growth engine. Since 2017–18, however, public investments in construction have been substantially constrained, as part of the government's efforts at fiscal consolidation, and the recent slowdown in GDP growth is

largely a result of this. A second-order issue is that the growth in construction has had little direct impact on employment. Nor have efforts to create linkages between the construction industry and domestic suppliers, especially SMEs, been particularly successful due to capacity issues on the supply side.

Overall, the sectoral changes in output in the Ethiopian economy have not been accompanied by a change in employment patterns. Even as agriculture's share of total output declined by about half between 1991 and 2018, it continues to employ almost three-quarters of the workforce in Ethiopia. At the same time, the share of the population employed in manufacturing actually declined between 2005 and 2013. This indicates that the government's greater focus on export-oriented, labour-intensive manufacturing has not yet had the intended development effect.

From a macro-policy perspective, several other concerns militate against the government's chosen development path. An overvalued birr makes imports cheaper, but exports less competitive. More importantly, it has resulted in a debilitating shortage of foreign currency, which is a binding constraint on businesses reliant on imports. More generally, the business environment has not improved over time, with access to credit remaining a major concern. In this regard, too, agriculture has been neglected – its share of all outstanding loans in 2017–18 was a paltry 2.8 per cent. FDI, to the extent that it has been attracted, is concentrated in specific regions and industries: efforts to attract FDI to other sectors and industries have thus far failed. The total exports of goods and services do not exceed 10 per cent of GDP, and have stayed relatively static since 2010–11. In fact, one can safely conclude that international trade has so far played a relatively minor role in Ethiopia's economic development.

Most worryingly, perhaps, for a state with such developmental ambitions is that public revenues are low (at 13 per cent of GDP) and have been declining. Although the Ethiopian government has ring-fenced pro-poor spending in its budget during the current period of fiscal consolidation, this means that in the absence of increased revenues, there is little room for increased public investment in the economy and in development of human resources.

Looking forward, it is clear that current policies need to be reconsidered. The very strong focus on export-led industrial development to the relative detriment of agriculture appears unrealistic, especially in the short to medium term. Too little of the value added thus created is likely to remain in the country to have much impact on domestic demand and any pivoting role on domestic enterprise development has yet to materialize. Of course, it is not the importance attached to manufacturing and export-led growth per se that is the problem, but the singular focus on this as the potential growth engine.

This approach is also far from inclusive as it largely ignores the three-quarters of the population who live in rural areas and from agriculture. Indeed, the poorest among the rural population barely witnessed any consumption growth between 2011 and 2016. Spatial mobility of labour implies that the urban labour markets are closely linked to the rural economy. Full and productive employment of the urban labour force can be achieved only in tandem with a significant improvement of returns and employment opportunities in rural areas. Linked to this, of course, is the issue that manufacturing and associated services cannot generate sufficient jobs in the short to medium term to absorb more than a minor portion of the new entrants to the labour force, let alone provide jobs for an additional influx of rural labour to urban areas. To sum up, therefore, a balanced development policy for Ethiopia would need to focus on agriculture and economic diversification driven by domestic demand, as well as manufacturing and export-led growth.

A number of subsidiary policy actions may also be useful in this context:

The National Bank of Ethiopia does not pursue either economic growth or employment targets in the conduct of monetary policy. Moving beyond merely targeting inflation and adopting either an explicit growth and/or employment target would enhance the predictability and thus the effectiveness of monetary policy.

Maintaining a moderately undervalued exchange rate has proven effective in increasing competitiveness in many countries, not least in Asia, at early stages of development. Exchange rate flexibility, allowing depreciation to make the currency moderately undervalued and liberalization of the current account would help strengthen competitiveness, reduce foreign exchange shortages, and support reserve accumulation in the Ethiopian context.

Although the government is already examining ways of increasing revenue collection this needs to be prioritized.

Continued efforts should be made to improve the business environment, especially in terms of increasing access to credit.

7.1.2 A more comprehensive approach will be needed to sustain the momentum of agricultural development and support a transformation towards modern and intensive small scale farming

Employment in agriculture increased by 6.5 million, that is more than 2 per cent per year, between 2004 and 2016, accounting for more than half of the total employment growth in Ethiopia over the period. By the latter year agriculture still accounted for three-quarters of all employment in the country. It can safely be assumed that the rapid growth in agricultural employment has been largely supply driven, resulting from a large discrepancy between labour force growth, on one hand, and the creation of productive non-farm jobs on the other. Supply pressure will decline slightly in the years to come as the demographic pressure decreases somewhat and assuming that the capacity of the non-agricultural sectors to create jobs increases. Yet, even under the best of circumstances agriculture will have to continue to absorb much of the labour force growth for years to come. It will be some time before exit opportunities from agriculture, in the form of productive non-agricultural jobs, will exceed the demographically induced growth of the agricultural labour force and thus being about an absolute decline in agricultural employment.

Total agricultural production, as well as small-holder grain crop production, increased by a staggering 7.5 per cent per year between 2004 and 2016, implying annual productivity growth of more than 5 per cent.⁹² This growth was all the more impressive as it was achieved primarily by small-scale farmers⁹³ and resulted mainly from an increase in yields, which doubled over the period. Ethiopia has a history of equitable land distribution and some 15 million small-scale farms, holding on average a mere 1 hectare of land, have been the main actors behind the rapid intensification and growth of agriculture, as well as its main beneficiaries. It would appear that the rapid growth in yields was achieved largely through an increased use of inorganic fertilizers and an increased input of labour, and supported by an expansion of extension services. With the important exception of maize, improved seeds are rarely used and almost all cultivation remains rainfed.

⁹² At constant 2010 prices in national currency. The figure also includes forestry and fishing. It should be noted that the very high rates of growth have been questioned in the past. See, for instance, Dercon and Vargas Hill (2009) and Dercon, Vargas Hill and Zeitlin (2009).

⁹³ Private small-scale farms account for 95 per cent of the total production of grain crops, as well as 95 per cent of the area under grain crop cultivation.

Looking ahead it is clear that sustaining the momentum of rapid growth in production and agricultural yields will require a much more comprehensive approach than just relying on more inputs of fertilizers and labour:

The use of yield-enhancing inputs and practices needs to become more broad-based and balanced. The most acute need is arguably the development and widespread application of improved seeds, beyond maize, that are adapted to local conditions. This is particularly important as high-yielding varieties of seeds tend to be much more responsive to fertilizers than indigenous seeds. This will require urgent attention to the development and dissemination of locally adapted high-yielding varieties of crops such as teff, wheat and sorghum, to make up for past neglect in this field.⁹⁴

A continued intensification of agriculture through adoption of improved cultivation practices will be inexorably linked to an increased market-orientation. This will require development of an efficient network of downstream linkages, including agro-processing. Empirical evidence from other countries show that intensification of agriculture and a diversification of local economies through the development of non-farm economic activities, providing inter alia upstream and downstream linkages to agriculture, are mutually reinforcing and inter-dependent. Ethiopia is unlikely to be an exception in this regard.

Irregular and uncertain supply of water remains a major constraint on the development of agriculture in Ethiopia as access to irrigation remains insignificant. The dependence on unpredictable rainfall constrain the development of agriculture in three main ways.

It typically confines cultivation one crop per year as the cultivation depends on periods with adequate rainfall. With constant access to water through irrigation two or more harvests per year might be obtained.

It reduces the efficacy of other yield-enhancing inputs, in particular high yielding varieties (HYV) of seeds.

It exposes farmers to significant risks of crop failure. This is not only a major cause of impoverishment, but it also seriously limits the ability of farmers with small economic margins to invest in yield-enhancing cash inputs, obtained more often than not on credit, as this would magnify the consequences of a crop failure.

The impact of climate change in Ethiopia is likely to be significant, affecting the amount and pattern of rainfall in particular. This is a major concern in view of Ethiopia's history of drought, food insecurity and spatially concentrated patterns of poverty. The high risks inherent in rainfed agriculture already impose a constraint on agricultural development. Climate change will exacerbate these risks. Risk mitigation and measures to adapt agriculture to the effects of climate change must therefore increasingly become the focus of agricultural development efforts.

These severe constraints need to be addressed on several fronts. Irrigation should be expanded where possible. This will typically involve a combination of both large- and small-scale investments, where government must assume responsibility for the former and facilitate the latter. Special attention needs to be devoted to drought-resistance in the development of new seed varieties. Innovative schemes for risk mitigation, for example, the up-and-running rural public works programmes, but also crop insurance schemes, need to be developed, made affordable, and, if necessary, subsidized.

The very low levels of education and, indeed, literacy, among farmers will, unless addressed, inevitably impose a growing constraint on the scope for transforming

⁹⁴ For a criticism see, for instance, Dercon and Vargas Hill (2009).

Ethiopian agriculture away from subsistence orientation into a modern, market-oriented, and efficient economic sector.

There appears to be a discrepancy between the rapid growth in labour productivity in agriculture registered in the annual agricultural surveys, on one hand, and the comparatively more modest gains in incomes and consumption registered in the household income, consumption, and expenditure surveys, on the other hand. Disentangling this enigma is beyond the scope of the present study and would also require access to more and better statistics. Ethiopia has a laudable system of annual agricultural surveys to capture production and the use of cash inputs. However, as the transformation of agriculture moves beyond an initial phase and becomes more complex a broad range of other aspects of the agrarian transformation and development of the rural economy need to be captured as well, such as the use of production for sale, barter or own consumption, prices obtained for production and paid for inputs, use of labour time and the combination of agricultural and non-agricultural household activities and last, but not least, size of holdings (owned, rented, leased out) and a breakdown of production characteristics by size of holdings.

7.1.3 Weak economic diversification, weak SME development, and the need for horizontal and vertical economic integration across sectors

In Ethiopia, two forms of structural transformation of employment are occurring at the same time. On one hand, there is an incipient opportunity-driven shift of labour from agriculture to more productive, non-agricultural jobs. Considering the rapid agricultural growth, however, this positive trend still appears frustratingly slow. At the same time, some rural households have, for demographic or other reasons, become victims of a vicious circle of fragmentation of holdings and falling returns to labour in agriculture. When farm incomes are no longer enough to make ends meet, household members are forced to take up casual wage work in agriculture or to migrate to urban areas, where they become part of the informal economy, working for a pittance in lower-end services where entry thresholds are low. The picture that emerges, then, is of a dual-path structural transformation: one that is opportunity-driven with the potential to drive a dynamic economic development, and another that is distress-driven, perpetuating poverty and curbing productive transformation as people get stuck in low-productivity dead-end jobs.

Government development strategies have adopted two approaches to dealing with this. The first national development policies were premised on the logic that agricultural productivity growth would stimulate industrial demand by, among other things, increasing rural incomes and creating linkages between industries with the most production linkages to rural areas. This has since been modified, and the current Growth and Transformation Plan II focuses on industrialization, which is expected to be driven by export demand from international markets, while retaining a certain focus on creating backward linkages to agriculture.

A genuine productive transformation requires diversification of the rural economy. Yet, Ethiopia continues to suffer from a lack of diversification in the rural sector, and a lack of both horizontal and vertical linkages.

A number of studies confirm the very low level of economic diversification in rural areas in Ethiopia: for the vast majority of rural households off-farm economic activities still provide a minor source of employment and income. By 2011, for instance, survey data show that although a quarter of all rural households engage in some non-agricultural activities,

off-farm economic activities accounted for a mere 18 per cent of total household earnings.⁹⁵ A number of qualitative studies have argued that the efforts to create linkages between the agricultural and non-agricultural sectors have had mixed results (Oqubay, 2019a; Oqubay, 2019b). For instance, the leather industry and horticulture provide a study in contrasts: although centuries old, leather's contribution to merchandise exports declined by half between 2004 and 2016, and backward linkages with the livestock sector did not emerge despite the size of the latter. In floriculture and horticulture, exports reached 10 per cent of overall merchandise exports in 2015–16, up from 1 per cent in 2003–04. The factors that contributed to these varied outcomes include generic design of policy instruments without sectoral knowledge and consultation, including among financial institutions, which need to create tailored financial products for different sectors, and inadequate skills development, where a lack of effective links between universities, TVET institutions and industry associations/the private sector has created a shortage of skilled labour.⁹⁶

A major plank of Ethiopia's strategy in the field of industry has focused on the development of industrial parks, which are intended to attract FDI and spur export-oriented manufacturing. This strategy has not yet been completely successful, largely because it has been quite difficult to create linkages between domestic manufacturing and exporting firms. Sometimes the problem is simply geographical: exporting firms are often set up in industrial parks where there are few, if any, domestic firms (Zhang et al., 2008). In 2016, in fact, only 4.5 per cent of manufacturing firms were exporters (Oqubay, 2019a). At the same time, there has been a proliferation of micro-enterprises, which have (i) consumed a huge volume of funds provided under youth entrepreneurship promotion schemes, but (ii) generated little employment, and (iii) only graduated to becoming medium enterprises in very low numbers.

There are no easy solutions to these issues, but some re-orientation of policies should be considered.

A shift in focus from discretionary schemes to addressing the main general constraints on enterprise development, as identified in World Bank and other surveys. This would require, among other things:

- o improving entrepreneurship and business management capacity, especially among young people;
- o easing the availability of, and access to finance, in particular to SMEs. At present, finance flows to micro-enterprises and large enterprises dwarf the amounts being lent to SMEs. Recalibrating rules around micro-finance could also ease flow of funds;
- o a more carefully designed policy for micro, small, and medium enterprises, with particular focus on design, implementation, and targeting.
- o Economic development and diversification of rural areas and small towns, including:
- o Promotion of regional/local economic development strategies with broad-based local participation and ownership. In this context the importance of small and medium-sized towns as hubs for local development deserves particular attention.
- o Making the fostering of rural–urban economic linkages and vertical linkages between small, medium and large-scale firms a central objective of overall industrial policies.

⁹⁵ Recent data on rural economic diversification are largely lacking.

⁹⁶ It is worth noting that there are occupational hierarchies in leather-work in Ethiopia.

7.2 Educational levels remain low and inequality in educational

The past 10 to 15 years have seen major advances in education, albeit from very low levels, reflecting the high importance attached to education. Literacy rates increased from 27 to 40 per cent between 2004 and 2016, while the share of adults with at least four years of education increased from 14 to 27 per cent. By 2016, some 18 per cent had completed eight years of primary education and 11 per cent had at least lower secondary education, representing a doubling of the rates registered in 2004. Gender differences in educational attainment have, by and large, been eradicated. However, rural–urban disparities, as well as disparities between poor and better-off households, remain very wide. Indeed, the less than satisfactory overall situation is largely due to the fact that rural education trails far behind urban education and that the economic status of the household a child comes from matters hugely for their chances of acquiring an adequate education.

7.2.1 Bridging the rural-urban education gap has become a main challenge

Despite impressive advancements in education over the past 10 to 15 years, education levels in rural areas remain very low. Less than half of the rural adult population were literate in 2016 and a mere 6 per cent had more than eight years of primary education. These figures contrast sharply with the urban scene, where well over 80 per cent of the adults were literate and almost 40 per cent had more than eight years of primary education. The educational status of the younger age groups is better, but far from satisfactory.

Although eight years of primary education is now both compulsory and free, statistics from 2016 show that less than half of all children completed primary education, suggesting very high dropout rates and implying that at least half of the young entrants into working life lack an adequate education. Almost four out of five children do not pursue any education beyond the primary level.

The risk that a rural child will never be able to go to school is four times higher than for an urban child and four out of five urban children complete primary education, compared with only two out of five rural children. The rural–urban education disparities increase at higher levels of education. Almost six out of ten urban children complete lower secondary education compared with little more than one out of ten rural children and the chances that an urban child will complete higher secondary education is eight times higher than for a rural child.

The very high levels of literacy among the adult population in rural areas imply a need to further strengthen and expand existing schemes for basic adult education, with a particular emphasis on rural women. This is essential as basic literacy and numeracy skills are fundamental for personal empowerment and for escaping working poverty. It is also essential in order to release the full productive potential of these very large numbers, which is a prerequisite for a sustained and inclusive development of agriculture and of the rural economy as a whole.

7.2.2 Poverty and child labour deprive children of education and their prospects of productive employment and decent work as adults

Poverty is a major obstacle to accessing education. Four out of ten children from the poorest household quintile have never been to school compared with less than one out of ten

children from the richest quintile.⁹⁷ Only a quarter of the children from the poorest households complete primary education. Hence, there is a very high probability that poverty will be transmitted from one generation to the next as basic education is fundamental for accessing productive employment.⁹⁸ Access to secondary education is still largely a preserve of children from the richest households. More than half of the children from the richest household quintile complete lower secondary education, and more than a third also complete higher secondary education, compared with only a few per cent of the children from the poorest 60 per cent of the households. Indeed, the gap in access to secondary education between children from poorer and richer households has widened considerably as the increase in access to secondary education has been almost entirely confined to the richest household quintile.

Hence, children from poor households, and in rural areas more generally, fail to complete even basic education. Prohibitively long distances to school and high cost can serve as barriers to access. Although primary education, that is grades 1–8, is free of charge, schools are often thinly spread in rural areas, in particular in less densely populated regions. Poverty and the need to contribute to household income are another major barrier. The incidence of child labour remains very high, also among younger age groups, and typically involves long hours of work. More than two out of five children aged 5 to 11 are involved in child labour. About half of these children combine work with school, while the other half have to forgo education altogether.

Child labour is much more common in rural than in urban areas and primarily involves work in agriculture. Less than a fifth of rural children (aged 5–17) can attend school unfettered by any obligation to work, compared with almost 70 per cent of those in urban areas. Most working children work very long hours, 32 hours per week on average for those aged 5 to 11. The high prevalence of child labour and its strong association with poverty imply that increasing the availability of opportunities for primary and secondary education in rural areas may not suffice, but incentives, such as free school meals, must be created to reduce the opportunity cost of sending a child to school.

7.2.3 Strategies for human resource development and for economic development need to be harmonized at all levels

The educational attainment structure (EAS) – that is, the share of different educational categories (no education, primary, secondary, tertiary, TVET and so on) – in the labour force and the extent to which there is full and equal access to education, sets the limits for a country's technological and structural transformation and shapes its feasible patterns (Nübler, 2014). Hence, it largely defines the limits for broad-based, inclusive, and sustainable development and the scope for industrial and other policies to this end at any given time. A successful productive transformation requires that strategies for human resources development and education policies be closely coordinated with economic and industrial policies and that they be designed to work in tandem to foster a productive transformation that is both inclusive and sustainable.

Empirical evidence shows that countries with high shares of middle level education have the widest range of options for developing and diversifying manufacturing and for a broad-based and inclusive development, while countries with a narrow middle – that is, an educational attainment structure shaped like an hour-glass – have limited options for

⁹⁷ It should be noted that there is a correlation between disparities between rural and urban areas, on one hand, and between poorer and better-off households, on the other, as the better-off households (in particular it would appear the fifth quintile) are much more likely to be in urban areas than poorer households.

⁹⁸ This issue is explored further in Section 6.

developing a broad manufacturing base and for broad-based technological development. Instead, these countries tend to develop high-tech niches in the economy, with weak linkages to the rest of the economy (ibid.). That development pattern is neither robust nor, as a rule, inclusive. The current educational attainment structure in Ethiopia has a fairly broad base, a weak middle, and a comparatively strong top, resulting from an elitist education policy in the past and massive investments in broad-based primary education in recent years. Not only is there a narrow middle, but secondary education also continues to be dwarfed in terms of funding.

A structural and technological transformation of the economy requires large cadres of skilled labour. Yet technical and vocational education and training (TVET) remains poorly developed and suffers from several weaknesses. There are real or perceived problems of quality and relevance and linkages to the private sector remain weak. TVET is typically seen as a second-best option and thus attracts mainly less talented and motivated students. This perception is reinforced as employers tend to undervalue TVET graduates, resulting in difficulties in finding wage jobs and low pay.

The balance between general and technical, vocational and professional education at the secondary and post-secondary levels also needs to be revisited and revised as part of a policy to develop TVET into a good option endowing students with the skills and capabilities needed for accessing jobs as skilled professionals. There is also a need to develop TVET programmes at the post-primary level as an alternative path to pursuing general secondary education for the majority of young people, not least in rural areas, who otherwise drop out after completing primary education, with few employable skills.

7.2.4 Releasing the human development constraints on inclusive and sustainable development

Despite the expansion of primary education in recent years, Ethiopia's educational attainment structure and highly unequal coverage represent a serious obstacle to inclusive development and limit the scope for moving out of the low-technology, low-wage manufacturing segment and onto a path of sustained and broad-based technological upgrading of manufacturing and tradeable services. Major efforts are required to sharply increase access to both primary and, not least, secondary education for rural young people, who make up the vast majority of young people nationally, to prevent human capital from emerging as a major constraint on sustained rapid productive transformation and economic growth in the years to come.

To alleviate this constraint, investments in primary education need to be sustained and further expanded in rural areas, while much higher priority must be given to a broad-based development of secondary education, with the aim of making not only primary education, but also – over time – secondary education universally available to the young generation. Experience from elsewhere, as well as the results of recent household surveys in Ethiopia show that secondary education is essential for accessing formal wage employment or to become a successful entrepreneur in an increasingly modern and complex economy and labour market. Hence, greatly expanding the access and coverage of secondary education should become an urgent next step after achieving universal primary education. In addition, schemes for adult education need to be substantially scaled up in order to eliminate the backlog of illiteracy, in particular in rural areas and among women.

This will require not only a sustained rapid expansion of education facilities, in particular in rural areas, but also decisive measures to sharply reduce child labour and to eliminate it entirely in its worst forms.

7.2.5 The gender gap has been closed in education but remains in the labour market and at work

Overall, women have less education than men, but this is not true of younger cohorts entering the labour market. By 2016 the educational attainments of girls were at least at par with that of boys. Yet, significant gender differences persist in the labour market and at work. Women make up more than 40 per cent of the agricultural labour force and head approximately 25 per cent of all farming households, yet have less access to land and other factors of production than men (World Bank, 2019c, p. 18). Female-headed agricultural households yield lower returns from a given level of resource expenditure and, more specifically, receive fewer agricultural extension services, access less formal credit, manage less land, harvest a narrower range of crops, and have access to fewer production inputs (such as fertilizers, pesticides, herbicides, and fungicides) (ibid.). In business, women tend to have less access to resources to grow and formalize their businesses, leading to smaller firms with lower profitability compared with men.

Women face much greater difficulties than men in accessing jobs, as reflected in much higher unemployment rates. The gender wage gap also remains very large. In 2018, the average female wage in urban areas was a mere 62 per cent of the average male wage. To a certain extent this wide wage gap is due to occupational gender segregation and an overrepresentation of women in low-wage sectors, such as trade, hotels and restaurants. However, the gender wage gaps within sectors are also large. In manufacturing, women earned on average 65 per cent of the average male wage, in trade 64 per cent, in hotel and restaurants 66 per cent, in education 68 per cent, and in health and social services 62 per cent. These large gender-based wage gaps can have only two explanations: either higher positions in each sector remain a preserve of men and/or the principle of equal pay for equal work remains a distant goal.

Of course, the desirable scenario would be to change the broader social norms underpinning these gender gaps. Essential as this is, it is likely to take a great deal of time. In the interim, therefore, labour legislation needs to ensure equal and fair treatment of women at work. Career guidance at school is one of several measures that can contribute to reducing gender-based occupational segregation. The Ethiopian government could also design specific policies for women, in entrepreneurship, technical training, access to credit and business support services. As of now, most existing schemes do not specifically target women.

7.3 Engaging young people in the labour market

Young people⁹⁹ currently account for about 38 per cent of the working age population (aged 15–64). Some 33 per cent of the working age population in 2030 have yet to reach working age and together with the current youth cohort (aged 15–24) they will make up approximately 61 per cent of the working age population in 2030. They are, or will be, better educated and much better connected with and informed about the outside world than the older generation and, undoubtedly, have higher aspirations and new visions.

However, today's young people will arguably also face greater difficulties and challenges than previous generations. In particular, young people in rural areas will be more land constrained than their parents. Education and skills will be crucial as they are called upon to lead a transformation of agriculture from subsistence farming to “modern” commercial agriculture and they will increasingly need to seek productive employment and careers outside agriculture. This will require two interventions in particular. First, it

⁹⁹ Here defined as those aged 15–24.

underscores the paramount importance of eliminating the large inequalities in education between rural and urban areas and of making access not only to primary education, but also to secondary education independent of a child's economic background. Second, comprehensive strategies need to be developed that enable and actively encourage rural economic development through a two-pronged approach focused on continued agricultural transformation and economic diversification through the development of non-agricultural economic activities, not least in the form of SMEs, and the forging of strong links within the rural economy, and between the urban and rural economies.

In urban areas, young people face major difficulties in getting a foothold in the labour market. Very high youth unemployment rates – 25 per cent for young men and 33 per cent for young women aged 15–24 – speak for themselves. A strong preference for public sector employment and a willingness to queue for such jobs has been put forward as one explanation for the high youth unemployment. However, this is at most a minor explanation. The disadvantages of being newcomers on the labour market and lacking work experience, particularly in a situation in which the number of jobseekers far exceeds the number of vacancies, is likely to be the most important reason. Career counselling at school, better linking of curricula to today's and tomorrow's labour market demands, expanding possibilities for internships and apprenticeships are some ways of facilitating the transition from education to employment.

7.4 Catch those at risk of falling behind

Effective progress towards the eradication of poverty and achieving productive employment for all requires both enabling people to access productive jobs and escape poverty and preventing people from falling back into poverty. The gains in poverty reduction are the net result of flows in both directions. It is worrisome that the consumption of the bottom 15 per cent in rural areas contracted between 2005 and 2016 (World Bank, 2019, p. 48). This suggests, amidst the general trend of upward mobility, there has also been a counter-trend of impoverishment. There is also a segment of chronically poor households, mainly in rural areas, who have been bypassed by the past decade of rapid economic growth.¹⁰⁰ Despite the impressive increases in average per capita agricultural production it would appear that many rural households are still caught in a vicious downward spiral and causal chain where poverty tends to entail child labour, poor education, high fertility, high dependency ratios and increased population pressure on land, lack of means to invest in agriculture and in children's education, land fragmentation, and the perpetuation of poverty. Evidence of a distress-driven flight from agriculture to low productivity non-farm economic activities, which exist in tandem with opportunity-driven structural change, is an indication that a part of the rural population is caught in such a vicious circle and subject to impoverishment. An increase in the incidence of agricultural wage labour is another indicator.

Today's large inequalities in access to education are alarming as they will translate into inequalities in access to productive jobs and decent work tomorrow. They pose a major threat to Ethiopia's aspirations to achieve the SDGs and sustained inclusive development more generally. A large segment of rural young people are at risk of being left by the wayside of development. With too little land to make ends meet and with insufficient education and skills to access productive non-farm wage jobs or to become successful entrepreneurs they are at risk of getting stuck in perpetual poverty.

There also appears to be a centre-periphery dimension to the problem of lack of inclusion. Dynamic agricultural development has largely been confined to the densely

¹⁰⁰ A World Bank estimate suggests that 16 per cent of all households in rural areas and in small towns are chronically poor (World Bank, 2019, p. 49).

populated highlands and central parts of the country. Much less information is available on the lowlands, where non-sedentary agriculture and animal husbandry is prevalent. However, the results of both demographic and health surveys and the household income consumption and expenditure surveys show that the regions of Afar and of Somali consistently score worse on indicators such as education, fertility, and per capita consumption levels.

Among the multiple interventions that are possible and needed to catch and support those who are falling behind, three deserve to be singled out.

- (i) Access to adequate education stands out as particularly important. With insufficient or no land to fall back upon, education and skills become an absolute prerequisite for being able to access productive employment and to escape poverty.
- (ii) The value and effectiveness of rural public works programmes has been proven in Ethiopia, India, and elsewhere. As a source of employment and income of last resort these programmes mitigate risks, which is particularly important in rainfed agriculture, as well as providing a supplementary source of work and income to land-poor rural households. The Productive Safety Net Programme (PSNP), which currently reaches about 10 per cent of the population, is a laudable initiative with a proven record and provides a strong pillar in the gradual construction of a universal social protection floor.
- (iii) Affordable health care stands out as an arguably second most important pillar of social protection. A number of studies in Ethiopia and elsewhere have shown that unexpected medical expenditure, combined with the loss of labour resulting from illness are a main cause not only of temporary hardship, but also of loss of land, resulting in permanent impoverishment and destitution. Ethiopia aims to develop a system of universal affordable and accessible health care. Nevertheless, personal out-of-pocket expenditure on health care still accounts for 37 per cent of total current expenditure on health care in Ethiopia. Despite rapid improvements in recent years the number of professional health staff per thousand inhabitants, currently 1.3, still falls short of the WHO target of 2.3.

7.5 Inclusiveness is a precondition for a sustained rapid economic transformation

In closing, two points on the need for inclusive growth are worth reiterating. First, there is clearly a huge need for inclusive investments in education and skills in Ethiopia, given the shortcomings of educational outcomes in rural areas in particular, and the disparities between children from poorer and richer households. If current trends were to continue, it seems clear that shortcomings in education and skills will impose an absolute constraint on the country's developmental ambitions sooner rather than later.

Second, as already mentioned, the focus on export-led industrial development to the relative detriment of agriculture is far from an inclusive development policy. Export-led growth can, of course, have an important role to play as part of a more broad-based strategy, but hardly as the main focus in present-day Ethiopia. A highly equal land distribution and the momentum of rapid agricultural development ought to create good conditions for a robust and inclusive growth of domestic demand. The sluggish diversification of the rural economy and the weak development of SMEs more generally imply a failure to effectively tap into this demand. At the same time, slow growth of rural consumption suggests that agricultural growth has not translated into increased rural spending power as effectively as one would have wished.

Our review of the different policies in Ethiopia suggests that the demand side of the economy has been largely neglected. A good example is provided by the various policies for micro and small enterprise development. No matter how many well-thought-out incentive schemes are put in place to promote MSMEs, these cannot and will not prosper unless there is demand for their production.

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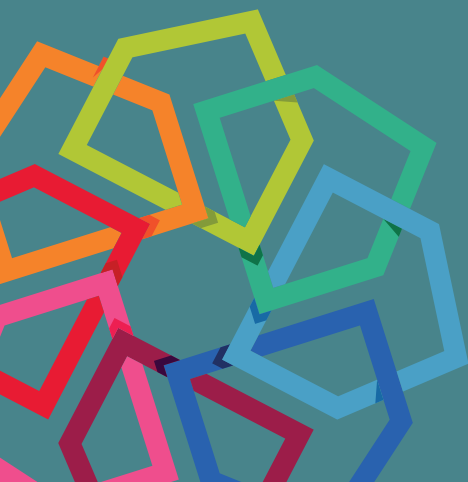
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