

Promoting Structural Transformation for High Productivity Jobs in Kenya

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Introduction

Structural transformation refers to the transition of an economy from low productivity and labour intensive economic activities to higher productivity and skills-intensive activities. The key driver of structural transformation is the need to shift from reliance on low productive sectors such as the agricultural and subsistence sectors towards the modern sector which is dominated by services and manufacturing. Such a phenomenon opens opportunities for more productive jobs and promotes a country's economic growth as it ensures resources are redistributed and used more efficiently.

Generally, structural transformation is defined by four essential and interrelated processes: a declining share of agriculture in national output and employment; rural-to-urban migration underpinned by rural and urban development; the rise of a modern industrial and service economy; and a demographic transition from high rates of births and deaths to low rates of births and deaths associated with better health standards in developed and urban areas.

Structural Transformation in Kenya

The promulgation of the 2010 Constitution of Kenya heralded transformation of

government structures into a devolved system of governance. The Kenya Vision 2030 advocates for accelerated transformation of the country into a rapidly industrializing upper middle-income nation that offers high quality living standards to its citizenry and avails decent and high-productivity jobs on a continuous basis, which are vital to tackling poverty in the country. In addition, policy direction has recently focused on structural transformation as evident from continuous dedication on manufacturing and even its inclusion among the 'Big Four' agenda. Structural transformation is underpinned in large part by institutions and policies that promote the development, adoption and use of technologies to change what an economy produces and how it does it.

Structural transformation in Kenya, as in most African countries has retrogressed, as evidenced in poor overall productivity performance, increased employment in low value activities, and low investment levels. Moreover, in terms of accumulation of technological capabilities, Kenya still exports mainly raw materials and commodities that do not require any advanced technology. This is attributed to Kenya's continued over-reliance on agriculture and light industries. In the past 16 years, agriculture contributed an average 26% to national income and approximately 60% of the country's foreign exchange earnings. Kenya's manufacturing share of GDP remained virtually constant,

averaging 10% annually in the past two decades.

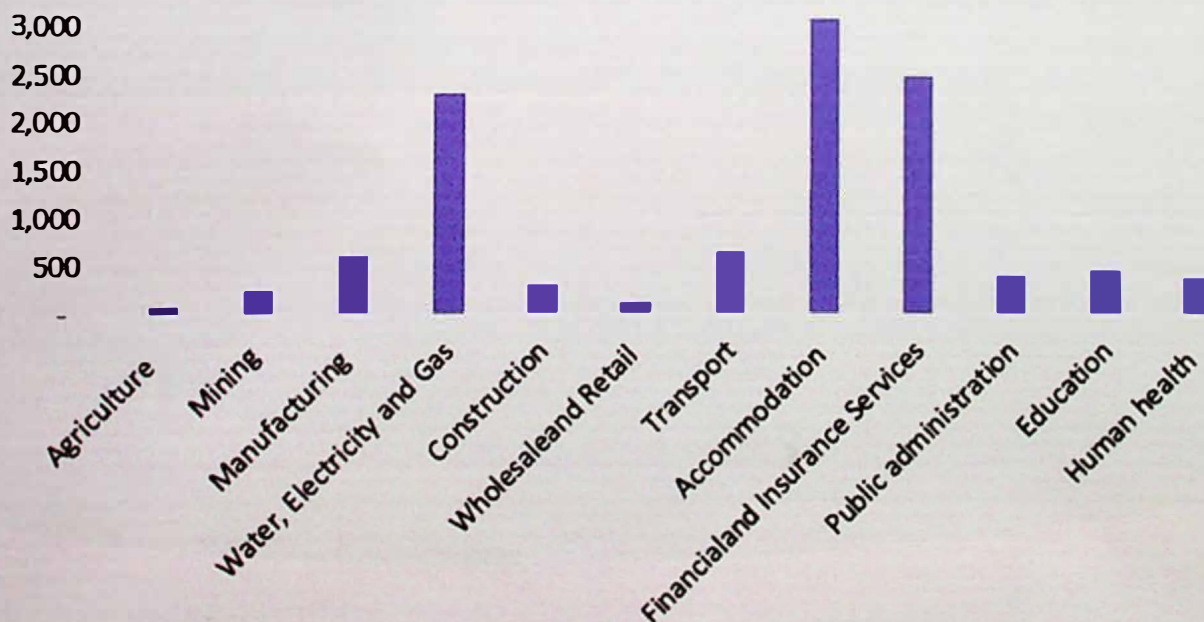
A study on productivity and its determinants in Kenya conducted in May 2018 confirmed that the country is still reliant on low productivity and labour-intensive economic activities. The labour productivity at the sectors is presented in the chart below.

The low productivity and labour intensive economic activity is dominated by agriculture, which employed about 60% of the total population. Second is the wholesale and retail sector which employed on average 15% of total employment between 2000 and 2016. The high productivity and skills-intensive sectors include real estate, and financial and insurance services that employed 0.1% and 0.5% of total labour force in the same period. A worker in the real estate sector produced, on average, output worth Ksh 21,110,000 annually between 2000 and 2016. Although the chart below suggests that the services sector in Kenya has a higher productivity, mainly driven by

modern and productive jobs in finance, communication and real estate sectors, most jobs in services are concentrated in low-productivity areas such as in the wholesale and retail sector.

The factors that affect labour productivity in Kenya are education, technology, wages, capital intensity, macroeconomic stability, openness, government expenditure and labour market participation rate. A one year increase in education increases labour productivity by 10% while a one per cent increase in openness reduces labour productivity by 0.01%, suggesting that liberalization may not be benefiting Kenya due to competition from cheap imports, owing to cheap labour and low domestic value addition. Similarly, an increase in the labour participation rate by one unit reduces labour productivity by 0.03%, suggesting that greater labour market participation brings in the less productive persons. In addition, the share of labour has been falling while that of manufacturing has been rising, further lending support to structural transformation.

Value of annual output per person in Kenyan shillings: Average for 2000-2016



Data Source: Kenya National Bureau of Statistics

Sustaining Structural Transformation to High productive Jobs in Kenya

The process of structural transformation is a path-dependent one, in which countries shift more easily to products characterized by the knowledge that are similar to those embedded in their current productive structure. Further, the wealth of a nation is determined by the level the country has attained while accumulating and mobilizing these productive capabilities. Kenya needs to diversify its products and shift from trading in traditional products to more complex ones. Countries that have been able to diversify into unique and complex products that only a few countries export have increased their productivity tremendously.

A clear focus on the quality of education to achieve the Vision 2030 is important. There is need to continue allocating more resources to the education sector to increase outreach and ensure quality across the system. It is prudent to tailor the market needs to the learning curriculum and embrace talents in schools or learning institutions. To this end, strengthening technical and vocational education and training (TVET) is essential. To avoid brain-drain, the education system and job market require an efficient reward scheme for levels of education attained. A better quality of workforce will shorten the learning curve and gestation period associated with acquisition of new technology.

Formalization of the informal economy can be encouraged by reducing the cost of doing business in the country. Decreasing

regulatory cost of formalization by lowering costs of trade licenses and eliminating unnecessary trade fees and charges while imposing fewer paperwork requirements will go a long way in facilitating formal trade. Further, informal traders need to be linked to incentives schemes such as assistance in accessing finance and basic compliance labour and environmental regulations. Additionally, as most informal firms are small, the broad policy could aim to assist these firms develop and graduate into formal economy enterprises. This requires concerted effort in addressing constraints such as limited access to credit and inadequate management skills. A policy effort that seeks to formalize employment relationships, offer training, expand social security benefits and enable transferability of qualifications and skills between the formal and informal sectors would help facilitate integration in the formal economy.

Kenya needs to harness its natural resources to build skills for its youthful population. Developing skills can lead to utilization of untapped entrepreneurship potential, creating opportunities for increased job and wealth creation. Finally, agriculture cannot be neglected given its contribution to GDP, employment, foreign exchange and the forward linkages it provides other sectors such as manufacturing and services. Boosting this sector could lead to spillover effects on the entire economy, which can indeed provide momentum for long term economic development and create decent employment.

About KIPPRA Policy Briefs

KIPPRA Policy Briefs are aimed at a wide dissemination of the Institute's policy research findings. The findings are expected to stimulate discussion and also build capacity in the public policy making process in Kenya.

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