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Guidelines for an Employment and Labour Market Analysis (ELMA)

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Abbreviations

ADB	Asian Development Bank	PES	Public Employment Services
AfDB	African Development Bank	PLMP	Passive Labour Market Policies
ALMP	Active Labour Market Policies	MSME	Micro, Small, and Medium Enterprises
ELMA	Employment and Labour Market Analysis	NGO	Non-Governmental Organisation
EURASEC	Eurasian Economic Community	SIDA	Swedish International Development Agency
FDI	Foreign Direct Investment	TVET	Technical and Vocational Education and Training
GDP	Gross Domestic Product	UIB	Unemployment Insurance Benefit(s)
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) GmbH (merger of former DED, GTZ and InWEnt)	UISA	Unemployment Insurance Savings Account
ILO	International Labour Organisation	UNESCO	United Nations Educational, Scientific and Cultural Organization
IMF	International Monetary Fund		
KR	Kyrgyz Republic		
NEET	Not in Employment, Education and Training		
ODA	Official Development Assistance		
OECD	Organisation for Economic Cooperation and Development		

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PART 1: INTRODUCING THE GUIDELINES

I Introduction

Promoting productive and decent employment is a complex task. To tackle the various facets of this challenge - namely unemployment, underemployment, vulnerable employment and working poor - German development cooperation pursues an interdisciplinary approach towards more and better employment (see Box 1). However, before implementing this integrated, three-dimensional approach to promoting employment, all stakeholders should have a common understanding of the nature of the various factors defining challenges and opportunities for increasing productive employment in a given country. The purpose of the present guidelines for “Employment and Labour Market Analysis” (ELMA) is to address this need for a deeper understanding of country specific challenges to employment generation.

ELMA provides a methodological tool for a comprehensive analysis of the labour market and employment situation and its respective underlying causes. It is based on the logic of the integrated approach for employment promotion of German development cooperation. Hence, possible factors are structured and analysed according to their impact on labour demand, labour supply and the matching process of the labour market. The time perspective of

the analysis is medium- (2-6 years) to long-term (up to 10 years). The structure of ELMA is flexible enough to deal with very different employment conditions in developing countries. Thus, it can be used for analysing labour markets in low-income countries, transformation countries, as well as in middle income countries.

ELMA might be useful for a broad range of stakeholders in development cooperation: it may help decision makers in operational departments and sector experts in technical departments at headquarters of German implementing agencies as well as project managers and their partner institutions in partner countries to deepen their understanding of the main constraints and challenges for country specific employment generation. Generally, there is a great deal of flexibility in the mode of implementation of ELMA. But in order to incorporate as much national expertise as possible and to facilitate an intensive dialogue on reform options we basically recommend a participatory, partner-driven process of conducting ELMA (see also further information regarding the process in Section III of Part 1, Figure 4 and in Annex A of these guidelines).

BOX 1

The perspective of the integrated, multi-dimensional approach of German development cooperation to promoting employment

The German approach rests on the assumption that the causes of employment problems do not only stem from deficits in the **labour market** itself, for example poor matching because of information problems. In addition, conditions for labour supply and demand impact likewise on employment generation. On the **labour demand side**, for example, an unfavourable business environment or a poorly developed private sector might constrain expansion of businesses, thus limiting in its course the demand for labour. Regarding the **supply side of labour** we often observe low employability of a major part of the labour force leading to un- or underemployment, and at the same time job vacancies. Deficits in the education system and low productivity of the workers because of illness, poor nutrition, etc., usually play a major role in preventing a better match of labour supply and demand.

Consequently, tackling employment problems within such an integrated approach needs not only to address conditions in the labour market itself, but also to strengthen labour supply and to boost demand for labour.

Source: see e.g. Federal Ministry of Economic Cooperation and Development (2007); GTZ (2010).

Like other tools for labour market and employment analysis¹ ELMA has been influenced by the highly structured and step-wise approach of Growth Diagnostics developed by Hausmann/Rodrik/Velasco (2004), which focusses on identifying binding constraints and not just listing observable hindrances. Consequently, there are many similarities to other tools, especially to the ILO tool “Employment Diagnostic Analysis”. Still, the structure of ELMA differs due to the underlying logic of the integrated employment promotion approach of German development cooperation. The analysis of labour market and employment conditions takes all three dimensions, labour demand, labour supply and matching likewise into account. By contrast, in the ILO approach human resources are seen as “creators of growth” and, subsequently, as the “point of departure for understanding and addressing the constraints, challenges and opportunities for inclusive and sustainable job-rich growth” (ILO (2012a), p. 3). From a normative point of view the human resource base is unarguably the ultimate target for improvements. But this should not dominate a positive analysis of labour markets and employment because it neglects the logic of market outcomes. As it is not reasonable to dispute whether it is the upper or under blade of a pair of scissors that cuts a piece of paper, it is not reasonable to ex ante give more weight to factors influencing the quality of human resources (labour supply) than to factors guiding growth (labour demand) or vice versa.

The main method of inquiry in ELMA is qualitative research. Still, we recommend complementing the argumentation with available information based on quantitative analysis of past and future trends. However, the comprehensive analysis needs to be managed: in order to optimize time and resource constraints ELMA is principally based on existing data and literature (e.g. studies, reports, research papers). Analyses of these data sources should be complemented by field interviews in order to validate and deepen information. To facilitate implementation of ELMA and ease planning and calculating of time and resources, we will inform you about possible indicators and data sources throughout the guidelines (see Part 2).

ELMA has been produced by the Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) GmbH on behalf of the German Ministry for Economic Cooperation and Development (BMZ).

1 e.g. the “MILES” approach of the World Bank (see World Bank (2008)); SIDA’s “Integrated Economic Analysis for Pro-Poor-Growth” (see SIDA (2006)) and the “Employment Diagnostic Analysis” developed by ILO (see ILO (2012a)) in cooperation with SIDA.

II Dimensions of employment problems in developing countries

Before giving an overview of the structure of ELMA (see next section), we need to narrow down the dimensions of employment problems which developing countries often face. These employment problems differ decisively from those in developed countries (see e.g. OECD (2012), p. 101). Whereas in developed countries measures to reduce unemployment are at the centre of any labour market analysis, similar measures in the context of developing countries do not cover the prevailing dimensions of employment problems adequately. In low- and middle-income countries the problems of underemployment, vulnerable employment and working poor are much more pronounced as unemployment as such. This is due to the fact that poor people in developing countries simply cannot afford to be unemployed. Therefore, an assessment of employment problems has not only to take into account the number and characteristics of unemployed, but should scrutinize in more detail dimensions of employment which are associated with poverty and vulnerability (see also e.g. ILO (2012a), p. 21).

Looking at the literature on employment we observe a confusing range of indicators and concepts used to analyse employment. So we encourage you to use Figure 1 as a translation tool in order to differentiate between

the various facets of employment problems. This so called “Rosetta stone” for labour markets has been developed by OECD, AfDB and others in order to be able to compare the various definitions used in labour market analysis with one another. In the glossary (see annex) these guidelines provide for additional definitions of all indicators used in ELMA.

As can be seen in Figure 1 the working age population of a given country can be characterised using different aspects as being in or out of the labour force, time use, employment status, working status, job quality and degree of formality of the employment.²

On the basis of these different dimensions of working age population we can highlight the following employment problems (see also glossary in the annex): As mentioned above, the discussion of employment problems in high- and middle-income countries is usually focussed on the problem of **unemployment**. However, without functioning social security systems poor people in developing countries need to work irrespective of what the working situation might be. Consequently, among the labour force of developing countries we find employment problems with respect to **underemployed** (non-voluntary part-time) and **vulnerably employed**. The latter category is a

Figure 1: The “Rosetta stone” for labour markets

1. Labour Force Status	2. Time Use	3. Employment Status		4. Working?	5. Job Quality	6. Formality
In the labour force	Full-time worker	Wage employed		Employed	Wage employment	Formal
		Self-employed			Vulnerable employment*	
		Contributing family worker / unpaid worker				
	Part-time worker	Voluntary part-time employed				Informal
	omvpöimtarý = Underemployed					
Out of the labour force	Job seeker	Unemployed	Broad Un-employment	NEET**		
	Inactivity or housework	Discouraged				
		Inactive				
In education		Student		Student		

* Adapted from ILO; **NEET: Not in Employment, Education, or Training.

Source: OECD (2012), p. 102.

² Please note that each pillar of characterization of the working-age population stands alone. Thus, within Figure 1 no indications of relations between subgroups of different pillars are given.

measure of people who are employed under relatively precarious circumstances (e.g. contributing family workers or own-account workers with no formal work arrangements, no access to benefits or social protection programmes, and more at risk to being affected by economic cycles).

As informal employment relations are often carried out under precarious conditions strong connections between vulnerable and **informal employment** exist. Also, vulnerably employed people usually make up an important part of the **working poor**. These are defined as employed persons, either for wages, on their own account or as unpaid family helpers, whose income is insufficient to bring them and their dependents over a defined poverty threshold (e.g. World Bank international poverty lines of US\$1.25 and US\$2 per person per day) (see ILO (2012a), p. 22).

Further dimensions of employment problems can be found by looking closer at the characteristics of **people out of the labour force**. Especially young people aged between 15 and 24 (henceforth considered as youth) and women are often discouraged from finding work (**discouraged workers**). Because their status of inactivity or housework is the result of having given up the search for employment rather than of a voluntary decision, the **NEET rate** (people not in employment, education or training in relation to the entire category), differentiated by youth and gender, needs to be taken into account, too.

III About the structure of the Employment and Labour Market Analysis (ELMA) and process of implementation

In view of these labour market challenges, the question comes up of how to identify and assess their possible causes. The structure of ELMA is based on the assumption that these employment problems are – at first sight – the result of inadequacies of the labour market itself. But labour supply and demand are, in turn, influenced by other market outcomes and institutions. Consequently, searching for reasons beyond employment problems on the labour market alone does not enable a broad-based charting and understanding of the specific constraints, challenges and opportunities regarding employment development in a given country. Whereas especially the market and institutions for training and education influences the quality of labour supply, labour demand depends mainly on the dynamics of markets for goods and services. Hence, if we aim at increasing labour demand, improving labour supply, and strengthening the matching process of the labour market with the goal of full and productive employment,

we have to consider the dominating forces influencing these important markets and institutions as well (see also Figure 2).

This integrated view applies also to the treatment of the public sector: in addition to an analysis of the forces within the three “core” markets for employment (market for training and education, markets for goods and services and the labour market itself with a possible migration out- or inflow) the public sector is seen as an important player, too. First of all, the public administration is demanding labour on the labour market. Employment opportunities created in the public sector can influence the outcome of the (formal) labour market (e.g. regarding wages) depending on the size and capacities of the public sector. However, the public sector is not only a “player in the field”. The government influences market outcomes by (a) setting the institutional framework of economic activities through laws and regulations and (b) further intervening in market

Figure 2: Important factors influencing employment

Labour Supply	Matching / Mediation	Labour Demand
Supply of Skills and qualifications Malnutrition / Health status Degree of social protection Labour migration Demographic development	System of coordination - Wages - Labour law and regulations - Collective bargaining Active and passive labour market policies and institutions	Employment in the private sector: Economic framework conditions with special focus on degree and intensity of international market integration General Business Environment, with focus on - Infrastructure - Regulatory framework - Financial markets Public sector as employer
Economic policies and governance of the public sector		

Source: author's own compilation

processes with economic policy decisions. In the context of developing countries with often limited capacities of the public sector to employ this second function usually exerts higher impact on employment than the function as a player in the field.

Like a doctor who can only observe the symptoms of a patient's illness we can only observe the different employment problems in a country. To find out what has led to these problems is the task of ELMA. However, broad-based labour market and employment assessments usually run the risk of ending up with a long list of constraints and challenges to productive and decent employment. This lack of focus might create a laundry list of reforms, which are impractical for discussions, decision making and implementation.

Of course, due to all markets being interrelated, it is far from trivial to isolate important factors leading to employment problems and opportunities from less important ones. The role of ELMA is to present a structured, step-wise approach (see also Figure 3) concentrating only on an assessment of those factors, which - based on economic theory and empirical evidence - are likely to be of special relevance to employment problems in developing countries. In other words, ELMA is a kind of instrument used in order to do diagnostics of employment problems.

The method of ELMA is to check step-by-step whether and to what extent all those factors stated in Figure 2 are relevant in the country's context. Before we present an **overview of the structure of ELMA** (see Figure 3 and Annex B). We would like to stress that the order of checking the relevance of different factors proposed in ELMA does not give indications about their relative importance. For employment problems to occur we need to address all three dimensions equally: labour demand, labour supply, and matching in the labour market. So we have structured ELMA according to efficiency, trying to avoid duplications in analysing as much as possible.

To understand the stepwise approach of ELMA it is useful to **distinguish between different constellations of labour demand, labour supply, and of the matching process** in the labour market which might have led to employment problems. In this regard, we apply the same method as a doctor who - in checking the condition of different organs of his patient - tries to pin down the most binding constraints to health. Of course, we all know that a healthy condition is always the result of all organs working together. This means also, that the illness might have been created simultaneously by deficiencies of different organs. Their functions are closely intertwined.

The same holds for ELMA: In an economy all markets are interrelated. So changes in one market affect all other markets by a chain of reactions. Hence, in reality the observable employment problems are the result of different constellations working together. For example, whether the number of people offering their labour on the market is too high or their skills are too low can only be decided in view of the quantitative and qualitative aspects of labour demand. Hence, factors influencing labour demand and labour supply instantly work together. Also the matching process on the labour market is affected by labour demand and supply. But in order to diagnose as thorough as possible and, based upon that, discuss on options of "therapy" it is helpful to (notionally) distinguish between constellations of labour demand, labour supply and the matching process in the labour market. This stepwise approach is used in ELMA (see also Figure 3). The analysis tool consists of 5 stages, each of them being divided in different analytic steps.

Principally, ELMA consists of five stages A to E (see Figure 3 on the next page):

- 1) **stage A:** basic analysis and definition of employment problems in the country's context,
- 2) **stage B:** analysis of labour demand,
- 3) **stage C:** analysis of labour supply,
- 4) **stage D:** analysis of the matching process in the labour market,
- 5) **stage E:** summary and conclusions.

Figure 3: The main stages of ELMA

ELMA in five stages	
A (1-6)	<p>What is the basic potential for employment in the country?</p> <p>Objectives of steps 1 to 6:</p> <ul style="list-style-type: none"> ■ Familiarising with basic factors influencing labour demand and labour supply ■ Getting to know degree and intensity of employment problems
B (7-11)	<p>What prevents firms from demanding more labour?</p> <p>Objectives of steps 7 to 11:</p> <ul style="list-style-type: none"> ■ Getting to know the conditions of business environment in general as well as in more detail for specific sectors ■ Identifying the most relevant constraints for business expansion, which subsequently impedes labour demand and employment generation
C (12-14)	<p>What prevents the labour force from offering (in sufficient quantities) the skills in need?</p> <p>Objectives of steps 12 to 14:</p> <ul style="list-style-type: none"> ■ Assessing the problem of skill mismatch ■ Getting to know the extent and quality of the provision of educational services ■ Identifying major challenges in the education system to provide adequately skilled labour supply
D (15-17)	<p>In which way do labour market institutions, regulations and policies impact on the matching process?</p> <p>Objectives of steps 15 to 17:</p> <ul style="list-style-type: none"> ■ Understanding wage formation as the central coordination mechanism in the labour market by connecting wage/productivity development with major factors influencing wage formation, e.g. labour law and regulations, wage policy, collective bargaining system ■ Assessing the effectiveness and efficiency of labour market and social protection policies: To what extent can active labour market policy address inefficiencies in the matching process? To what extent can passive labour market and – more general – social protection policies safeguard people from poverty and loss of income due to unemployment?
E (18-20)	<p>What are the main challenges to employment creation?</p> <p>What kind of consequences can be drawn regarding reform efforts of the respective country in general and in particular of German development cooperation programmes, supporting employment promotion?</p> <p>Objectives of steps 18 to 20:</p> <ul style="list-style-type: none"> ■ Getting to know the relative importance of the main constraints to employment generation identified before ■ Based on a participative process defining possible areas and options for government action ■ Proposing options for German development cooperation programmes of how to incorporate the findings of ELMA

ELMA has been developed on the ground of practical experience: In the framework of the implementation of the GIZ programme “Vocational Education & Training and Employment Promotion” in Kyrgyzstan a study was produced in 2012 tackling the labour market and employment policy situation in the Kyrgyz Republic.³ The aim of the study was to identify obstacles in labour market development and employment growth, and to elaborate recommendations for future interventions in the framework of German-Kyrgyz development cooperation as well

as general guidelines presented here as ELMA. Because of the closely related development process of both, study and guidelines, the main arguments and findings of the study for the Kyrgyz Republic can be presented within the structure of ELMA (see Annex A).

Based on these experiences (see also Box 2 in Annex A) and some general considerations we recommend the following **process of implementing ELMA** (see also ILO (2012a), p. 13):

Figure 4: Process of implementing ELMA



³ Wolfgang Schwegler-Rohmeis; Annette Mummert; Klaus Jarck (2013): Study “Labour Market and Employment Policy in the Kyrgyz Republic”, Identifying constraints and options for employment development, A Study by GIZ Program Vocational Education and Employment Promotion in Kyrgyzstan in cooperation with GIZ Sector Project Employment-oriented Development Strategies and Projects, Bishkek, February 2013. For further information contact: employment@giz.de



PART 2: ANALYSING CONSTRAINTS FOR EMPLOYMENT GROWTH – THE EMPLOYMENT AND LABOUR MARKET ANALYSIS (ELMA)

Stage A: Economic, demographic and political framework conditions for employment generation

We start with an analysis of the economic, demographic and political framework conditions for employment generation. Though all factors presented in Figure 2 are likely to influence prospects of productive employment in every economy, you will only be able to derive their relative importance by looking at the specific country's context. The first step, therefore, is a mapping of the economy and the labour market and an analysis of basic factors and forces that provide the parameters for the economic development and policy making.

For better orientation, we provide an overview for conducting each stage of ELMA (see Figure 5 regarding stage A) before we explain it in more detail. In the overview all different steps are listed and explained (“*orientation*”). In addition, we highlight in the overviews where the different factors can be located with respect to labour supply, labour demand or the matching process in the labour market (see the colouring of the lines of each step).

Step 1: Geographical situation

Because the **geographical situation** of a given country cannot be changed, it represents one of the basic parameters for a country's economic development. A favourable geographical situation offers many opportunities for the country's development, whereas a problematic geography reduces the potential scope of economic action. However, there is no automatism between the geographical situation and productive employment. Geographical hindrances to economic development, employment and income generation can be overcome by technical means and good institutions. This makes it even more relevant for the government to support market processes in order to compensate for unfavourable conditions (e.g. with infrastructure policy, good market institutions, but also social protection policies, etc.).

The geographical situation influences growth and subsequently employment in several ways. The most important ones are how locational factors influence the division of labour in domestic and international markets. Locational factors within the country shape **domestic market integration** which in turn influences the size of job creation in the private sector. Economic integration of provinces for instance might be negatively affected by mountain ranges or other natural barriers parting the regions in the country. Strong and integrated domestic markets are not only relevant for local production but also for export diversification, as many successfully exporting firms gained their competitiveness by meeting an increasing domestic demand. As can be learned from the “Asian Miracle”, export-led growth can contribute to economic development and poverty reduction. One important transmission mechanism between the growth of exports and poverty reduction is employment in the export industries and in local production within the value chain of exported goods. Hence, **integration in regional/global economic structures** is another important aspect of employment generation which is likewise shaped by locational factors. For example, landlocked countries or small island-states at considerable distance from main global centres usually face relatively high burdens to economic integration. Similar problems occur if one or several neighbouring countries suffer from conflict or other severe governance problems (see ILO (2012a), p. 57).

Figure 5: Guide through stage A

Steps	Labour Supply	Matching in the Labour Market	Labour Demand
A (1-6)	<p>What is the basic potential for employment in the country?</p> <p>Objectives of steps 1 to 6:</p> <ul style="list-style-type: none"> ■ Familiarising with basic factors influencing labour demand and labour supply ■ Getting to know degree and intensity of employment problems 		
<p>Orientation: We start ELMA with checking for the basic conditions for growth, because a growth potential is a necessary precondition for labour demand and subsequently employment.</p>			
1			Geographical situation
2			Patterns of economic development in the past
<p>Orientation: In order to realize as much employment as possible the demand for labour should correspond in terms of numbers, but also in terms of skills and qualifications to the supply of labour. The identified growth patterns can be used as a first rough indicator for quantitative aspects of labour demand. We will focus on quantitative aspects of employment also in the following steps 3 and 4 by looking into demographic structure and labour migration. Both factors shape labour supply: demographic structure indicates an increase or decrease of the working age population in need of jobs; the extent of labour migration represents an indicator for excess labour supply generally reducing (or increasing) the labour force.</p>			
3	Demographic structure		
4	Labour migration		
<p>Orientation: After having identified possible basic constraints to productive employment on the demand and supply side of the labour market we turn to the performance of the labour market in general, pinning down (among others) the dimensions of employment problems.</p>			
5			Labour market trends
<p>Orientation: Many developing countries face development constraints (e.g. locational, geographical, resource endowments, climate change) which more or less have to be taken as given. But this does not necessarily mean that the country is doomed to fail in generating employment and income. In this case special responsibility is borne by the public sector and the way the government carries out its function. The quality of public actions might compensate for unfavourable initial conditions for employment creation. Therefore, we complement our first round of diagnostic with analysing the basic situation regarding this role of the public sector.</p>			
6	Public Sector as a cross-cutting issue:		Political situation and economic policy orientation

Step 2: Patterns of economic development in the past

In view of this very basic economic classification of your country in question we move to an analysis of its economic development. The purpose of this exercise is to learn more about the **overall performance of the economy in the past** (about 20 years) and, by this, to pin down the linkages between economic growth, employment (employment intensity of growth) and poverty reduction. In principle, high growth-rates of GDP do not necessarily transform to better income prospects and reduced poverty. It is the purpose of ELMA to help to identify those factors which in some way hinder positive growth rates to result in better employment and income possibilities. So by analysing the growth performance in the past we are able to form very rough assumptions about the likely direction of structural transformation of the economy in the future and identify important sectors for employment and income generation.

The following indicators help you to analyse **growth patterns** and also to benchmark with neighbouring countries and/or countries of similar broad-based classification:

- GDP growth pattern
- Employment elasticity
- Poverty indicators (nation-wide and regarding subnational units) linking growth and poverty reduction
- Sectorial contribution to GDP
- Sectorial contribution to employment
- Sector productivity (comparing sectorial share of value added and of employment)

Data of national accounts, usually provided by national statistics offices, are essential for describing and analysing economic development. Many multilateral institutions supply world-wide economic data, as well. These data sources are especially helpful for benchmarking and describing long-term economic patterns:

- www.unstats.un.org/unsd/snaama/ (for national accounts)
- www.data.worldbank.org (World Development Indicators)

- www.comtrade.un.org (Trade data base)
- www.wto.org (Country trade reviews)
- www.imf.org/external/data.htm (overview over different data and statistics)

The time-horizon in the present analysis is medium- to long-term, thus concentrated on growth trends. However, short-term **business cycles matter**, too. The more severe a recession the higher are the risks within the economy of not being able to return to the long-term growth path. With respect to employment, experiences with past recessions point to the fact that they leave “scars” on the labour market (s. IMF (2010), p. 15), meaning that at least for some part of the population the human costs of recessions (e.g. loss of earnings, impact on health, on children, on youth and long-term unemployment) will not be compensated in the upswing of the economy. Therefore, very frequent and harsh ups and downs of the economy do not only bear problems for businesses to long-term investment but also risks to people’s employability, thus adding to structural unemployment, underemployment and poverty.

Thus, an analysis of main factors being responsible for economic crises in the past is likely to reveal typical vulnerabilities of the economy to external shocks. A good starting point is to closely analyse the degree of the country’s integration in global economic structures (e.g. trade structures, terms of trade changes over time, balance of payments analysis (incl. remittances of external migrants)). Based on this, you should specify the **macroeconomic conditions for long-term economic development**.

Having a rough idea about the performance of the economy and major interacting factors we likewise need to gather the basic facts and figures on the labour market patterns in the respective country. However, before doing so you should have a closer look on demographic development and migration patterns (external and internal). Both are closely linked to labour market trends because they are basic factors impacting on labour supply.

Step 3: Demographic development

Demographic structure and its dynamics are external forces that serve as major parameters for the quantitative supply of labour (see for details e.g. ILO (2012a), pp. 18-21). For example, high rates of reproduction increase pressures on the economy to generate (in numerical terms) enough

employment opportunities and likewise pressures on the education system to endow the work force with adequate skills.

Useful indicators are e.g.:

- Growth rate of total population and working-age population
- Current age structure (visualized e.g. by a population pyramid)
- Age-based dependency ratio
This ratio informs you about the number of people each working age person has to support. A high dependency ratio (many children and/or elderly in need for support by the working-age population) entails a low per capita income. The difference between the age-based dependency ratio and the actual dependency ratio (i.e. ratio between the non-labour force part of the population and the labour force) gives an indication of the scope for improving (here: reducing) the dependency ratio by increasing labour force participation (see ILO (2012a), p. 18).

Respective data sources are provided e.g. by

- the World Bank (<http://data.worldbank.org/indicator?display=graph>)
- the United Nations Statistics Division (<http://unstats.un.org/unsd/demographic/>)

Step 4: Labour migration

Labour migration alters the labour force structure and dynamics, thus impacting on the economic situation of both – sending and receiving country or region. Depending on the magnitude of in- and outward-labour migration you should try to assess the most relevant effects of migration on the labour market situation (if necessary differentiating between internal and external migration).

Migration projections for the future would be interesting, as well. An important aspect here is the fact that OECD countries undergo demographic changes which indicate a growing demand for labour migrants. Hence, you might take into account an assessment of the international labour market for the citizens of the respective country (bilateral labour agreements etc.).

You may find the following sources for migration data useful:

- <http://www.iom.int/cms/en/sites/iom/home/about-migration/facts--figures-1.html> (migration data)
- <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/0,,contentMDK:21924020~pagePK:5105988~piPK:360975~theSitePK:214971,00.html> (migration and remittances data)
- <http://laborsta.ilo.org/STP/guest> (ILO portal for international migration statistics)

Thanks to improved data availability, describing basic patterns of labour migration may not be problematic. However, assessing the relevance of labour migration for productive employment and income generation is more challenging. In the context of these guidelines we can only offer you some important arguments concerning the evaluation of migration on employment generation. Your task is to decide whether they apply to your country.

Labour migration is an individual strategy to adapt to differences in job offers and/or wages between different regions (or countries). The household decision to migrate oftentimes answers the purpose of stabilising total income of households by spreading employment risks and to overcome problems of domestic markets like e.g. access to credit. Based on that, its effects on the labour market and the income position of the population are heterogeneous in nature with positive and negative aspects.

Regarding possible positive effects it can be stated: If a country is a sending country with excess labour supply, external migration is likely to reduce pressures on the domestic economy to generate productive employment in two ways (see ILO (2012b), p. 6): (i) by reducing the number of productive jobs needed in the economy as part of the labour force is diverted abroad, and (ii) by reducing the threshold level of income needed by a worker to bring him/herself and his/her dependents out of poverty as part of the household income is derived from remittances. So, remittances can be a driving force for poverty reduction despite high employment problems in the country. For much the same reason overseas labour migration is also likely to reduce the number of working poor, provided that poor households have access to opportunities to

migrate to work abroad. If a country is a receiving country (excess labour demand) incoming migrants help to improve production possibilities with subsequent positive impacts for the economy.

However, you should try to evaluate whether the following negative aspects apply to your country, as well: Migration might intensify labour market mismatches and segmentation (e.g. rural-urban), and might put a strain to social cohesion. Also, the majority of low-skilled external labour migrants usually face informal and consequently often poor employment conditions in the receiving country. This is not only a problem for migrants regarding working conditions and income generation. Due to the integration of part of the domestic work force in foreign labour markets the sending country is more dependent on the economic conditions of the receiving country. Vulnerable employment and, more generally, the working poor part of the labour force in the receiving country are the first to be affected by external shocks by getting released, wages cut back or sales reduced if the economy is hit by a crisis. Thus, in case of macroeconomic instabilities in the receiving countries temporary benefits of migration for the sending country (providing additional income for households and reducing pressure on the labour market) can quite suddenly decline, thus reinforcing existing economic and employment problems in the sending country. In the long-run, the constant loss in human resources and talents due to external migration might further intensify problems in the supply of a qualified and skilled work force (see also ILO (2012a), pp. 19-20). Thus, “in cases where migration is permanent, a continued outflow of human resources will sooner or later gradually erode the capacity of the country and the domestic economy to develop. It may also be argued, that overseas migration is no substitute for a national commitment to achieving full and productive employment in the domestic economy” (ILO (2012b), p. 6). In this perspective, migration can be seen as indicating underlying problems in the labour market or political system of the country.

Step 5: Labour market trends

Now we would like you to present the available information and data on characteristics and trends in the labour market. An initial understanding of the main challenges in the labour market can be derived by analysing the dynamics and patterns of the following indicators of labour force

characteristics (to assess gender disparities, the indicators should be grouped by sex):

- Working age population
- Labour force
- Employed/Employment rate
- Unemployed/Unemployment rate

In addition, indications for employment challenges like, for example, working poor, vulnerable employment, informal employment, youth unemployment, reasons for inactivity, etc., should be presented (you should refer to the indicators of labour force and employment status that we discussed in Part I, Section II, Figure 1).

In general, national data sources on the micro level provide you with important information. The most important sources are **household surveys** and specialized surveys of households or individuals often referred to as **labour force surveys**, as well as **population censuses**.⁴ The labour force participation rates obtained from population censuses, however, tend to be lower, as the vastness of the census operation inhibits the recruitment of trained interviewers and do not allow detailed probing on the labour market activities of the respondents. **Administrative records** such as employment office records and social insurance statistics are also sources of unemployment statistics; however, their coverage is limited to “registered unemployed” only. At the same time, administrative records can overstate registered unemployment because of double-counting, failure to remove people from the registers when they are no longer looking for a job, or because it allows inclusion of persons who have some work. Due to such measurement limitations, national unemployment data based on registered unemployed should be treated with care; registered unemployment data can serve as a useful proxy for persons without work in countries where data on total unemployment are not available and time-series of registered unemployment data by country can serve as a good indication of labour market performance over time, but due to the limitation in comparability to “total unemployment” the two measures should not be used interchangeably.

⁴ See in the following ILO information on Key Indicators of the Labour Market (KILM), <http://kilm.ilo.org/2011/download/GuidEN.pdf>.

Overall, ILO database and labour market assessments (e.g. global reports, research paper series, etc.) together with data provided by national offices of statistics are the most important sources of information. For more details on finding data see the resource guide by ILO “How to find labour statistics” (<http://www.ilo.org/public/english/sup-port/lib/resource/subject/labourstat.htm>) and in general the overview of ILO database LABORSTA (http://laborsta.ilo.org/data_topic_E.html).

In addition, ILO has developed a guide to estimate current and past deficits in productive employment (see ILO (2012b)). This methodology can be used optionally in order to transfer the qualitative analysis done so far into quantitative information. Based on standard labour market indicators (e.g. labour force participation rate, unemployment rate, etc.) and poverty measures (e.g. headcount poverty rate) you can estimate past and present deficits of productive employment and project the need for productive employment creation to meet established targets for the reduction of poverty and unemployment. However, these estimations and projections take place on a highly aggregated level, meaning that the figures used for calculation might not represent the underlying economic situation adequately. Therefore, they should only be used as providing additional information (which, however, might be easier to communicate in discussions than qualitative argumentations).

Step 6: Political situation and economic policy orientation

We are still trying to get an overview of basic framework conditions for decent employment in your country. In the framework of growth theories, factor accumulation (capital and labour accumulation) and production efficiency determined by technological progress are considered to be the standard growth factors. Therefore, we had a closer look on the geographical situation, demographic development and migration. But empirical analysis points to another very important factor: it seems that both factor accumulation and production efficiency are driven by a common third variable: the quality of a nation’s institutions, including the government’s policymaking process (see Acemoglu (2008) Chapter 22 and 23 or Mankiw (2010). “When government screw up, they screw up big time” (Mankiw (2010), p. 228). Hence, the political situation and economic policy orientation are forces, which – like geographical situation and demographic development – set further basic parameters for a country’s economic development.

Because employment policy is a cross-cutting issue, it would by far not suffice just to check whether the country has e.g. a national employment strategy or important references to employment policies in other policy documents. On the contrary, we need to look deeper into the general economic policy orientation and see how much room is provided for private sector activities (e.g. property rights, private property vs. state owned property). The underlying assumption here is that sustainable employment generation presupposes adequate and sufficiently stable framework conditions for market activities of private actors. In this respect you should discuss the “social contract”, meaning the role of the state vis-à-vis private economic activities in your country. Indicators like e.g. degree of government interventions and regulations of the economy, degree of rule of law and protection of property rights, as well as public expenditure patterns (e.g. regarding social protection) might help you to clarify this aspect.

However, it is important to distinguish in your analysis between *de jure* economic policy orientation and *de facto*. Despite elaborate national development strategies and other strategic documents (also directly addressing employment promotion), the reality of economic policy making often deviates decisively from political intentions.

These “enforcement” and/or “implementation” problems are caused by scarcity of resources. Another important cause is lack of leadership and willingness which, in turn, stems from problems in the political sphere.

In this respect, one important question you should address is whether the political decision making process entails enough checks and balances with e.g. freedom of press, active consultation of private sector representatives and/or civil society, etc. Again, you should concentrate on real patterns in political decision making rather than on an assessment of the de jure situation.

Finally, a further important factor for the implementation of policies of employment promotion, national development and poverty reduction is considered to be the public finance system.⁵ Thus, in your analysis you should comment also on the overall quality of the public finance system. In addition, with respect to possible problems of macroeconomic instability of the country, stated in step 2, you tackle the question to what extent the existing patterns of macroeconomic policies in the country are able to mitigate these problems (see also ILO (2012a), pp. 60-61).

In addition to national data provided by ministries with respect to economic policy orientation and reform strategies (PRSPs, implementation of national development strategies, etc.) the following data sources may be useful:

- IMF reports and publications arranged by country, <http://www.imf.org/external/country/index.htm>;
- World Bank reports and publications, <https://openknowledge.worldbank.org/search-filter?field=country>
- The World Factbook provided by the Central Intelligence Agency (CIA) of the USA, <https://www.cia.gov/library/publications/the-world-factbook/>
- Economist Intelligence Unit (EIU) (free registering obligatory), <http://www.eiu.com/>

- The assessment reports conducted by the multi-donor partnership Public Expenditure and Financial Accountability (PEFA) Program, <http://www.pefa.org/en/content/pefa-publically-available-assessments>

Using of different (global) indices might complement your analysis (see also Hausmann/Klinger/Wagner (2008), p. 12):

- Global Competitiveness Report of the World Economic Forum; www.weforum.org/issues/global-competitiveness
- Index of Economic Freedom of the Heritage Foundation, <http://www.heritage.org/index/>
- Global Corruption Barometer provided by Transparency International; www.transparency.org/research/gcb/overview

5 The quality of public financial management (or synonymously good financial governance) can be linked to three core elements: (1) poverty-oriented and transparent budget and fiscal policies, (2) an efficient collection of tax revenues in order to create greater scope for private and public investment, and (3) effective control systems as a basis for the government’s accountability and responsibility vis-à-vis its citizens.

Stage B: The labour demand-side: the impact of business and sector development on employment generation

Taking into account the results of the first stage A (steps 1 to 6) we already have a general idea about the main challenges to employment creation in the country. In the next three stages of ELMA we will add more details to this rough picture. We will continue with stage B in which we scrutinize in more detail factors influencing labour demand (see Figure 6).

Step 7: General factors influencing the business environment

A favorable environment for private enterprises is a necessary condition for employment and income generation. Therefore, you should analyse general factors influencing the business environment in your specific country.

In addition to the already mentioned data sources you might find the following sources useful as well:

- IMF World economic data base (<http://www.imf.org/external/data.htm#data>), regarding projections for the future e.g. IMF world economic outlook with selected macroeconomic data series (<http://www.imf.org/external/ns/cs.aspx?id=28>)
- Doing Business data provided by the World Bank, <http://www.doingbusiness.org/data>
- Sector specific national data provided e.g. by the Central Bank, the respective Ministries, etc. as well as local informants like e.g. employers' organisations, chambers of commerce, trade unions, NGOs, etc.

Infrastructure conditions and policy

Infrastructure provision with respect to **energy (notably electricity) and water, transportation and telecommunication** are important aspects of the business environment. Business climate assessments like e.g. World Bank's Doing Business Report, Enterprise Surveys, etc., usually cover the regulatory dimension of infrastructure provision, but not necessarily the on-going conditions for example of electricity consumption (power shortages, energy tariffs, frequency of black-outs, etc.). In addition to respective statements regarding the actual quality of infrastructure

provision your analysis should refer more broadly to possibilities and limitations of policies regarding the energy, water, transportation and telecommunication sector. This assessment is important in order to be able to comment on future developments.

Regulatory framework for businesses

Rules and regulations of a government define and underpin the range of activities a business can legally choose. By this, they impact also on the ease of doing business. Hence, the **regulatory framework is an important factor for investment**, and subsequent employment and income generation. Activities of businesses are regulated in many ways, starting with e.g. business registration procedures, permits (e.g. for construction of business premises) and licences. The tax regime and regulations, labour market regulations, etc., are important regulation areas, as well. Contrary to e.g. regulations for business registration these latter categories of regulations impact recurrently on the business throughout its entire life-cycle.

A large number of methods have been developed to measure the quality of the regulatory framework for business activities. Using the data generated by these different methods is certainly helpful, but coverage and implicit limitations of these methods should be kept in mind (see also appendix). The following **dimensions of regulatory framework conditions** help to structure the analysis of the regulatory framework for businesses and the usage of different information sources. Generally, regulations impact on businesses in two ways. First, the content of regulations, their consistency with respect to other laws and regulations, define - from a legal perspective - the range of activities businesses can choose. But experience in many developing countries shows that de jure regulations may not be adequately enforced or administered, leading to scope for rent extraction/corruption, ineffectiveness and inefficiency. Consequently, this second dimension - the administrative perspective - has to be considered, as well. Other aspects like e.g. the frequency of changes in the regulatory framework (frequent reforms undermine the credibility of regulations and increase implementation

Figure 6: Guide through stage B

Steps	Labour Supply	Matching in the Labour Market	Labour Demand
B (7-11)	What prevents firms from demanding more labour? Objectives of steps 7 to 11: <ul style="list-style-type: none"> ■ Getting to know the conditions of business environment in general as well as in more detail for specific sectors ■ Identifying the most relevant constraints for business expansion, which subsequently impedes labour demand and employment generation 		
7			Business environment in general Infrastructure conditions and policy Regulatory framework for businesses Financial market conditions and policy
			<p>Orientation: Based on this first inventory of challenges to business expansion and subsequently employment generation we look at the business environment and the respective sectorial policies in specific sectors.</p> <p>The first step of this specific sector analysis is to explain your choice of sectors by referring to their relevance for employment generation (step 8).</p>
8			Explaining the choice of sectors, which need to be analysed in more detail regarding their business environment
			<p>Orientation: After checking for challenges in the business environment in the selected sectors, the conditions for MSMEs (including informal economy) and in the public sectors should be scrutinized. This step is advisable because labour demand in both sectors usually exerts influence on the formal and informal labour market. Therefore, you should state to what extent and in what way this is the case in the actual country.</p>
9			Sector specific analysis of labour demand conditions
10			Employment prospects in MSMEs (including informal economy)
11			Employment in the public sector

costs for public administrations) or the general capacities of the public sector for administering and enforcing the regulatory framework need to be taken into account.

Your assessment regarding the impact of labour market regulation and wage levels on the business climate should deal with the **ambivalent nature of labour market regulations**. On the one hand, labour market regulations are an important factor impacting on labour costs for businesses. On the other hand, the objective of many labour market regulations is to protect employees from market failures (e.g. asymmetric negotiation power). Therefore, you should analyse the allocative and distributive effects of labour market regulations with both sides in view. In order to present an integrated analysis of this topic, the evaluation of labour market regulations will be covered within the ELMA structure in step 15 (Step 15: Wages, labour law and regulations, collective bargaining system). In the present context, we recommend only to present the results of the analysis with further reference to the analysis of labour market institutions in the following steps.

Financial market conditions and policies

One common feature of all aspects of the business environment discussed so far is that they impact on the decision of enterprises to invest. In the case of favourable business environment conditions the returns to private investments are higher, thus making investments more attractive.⁶ This again can lead to a higher demand for labour. Put differently, up to now we argued that a lack of labour-demand by the private sector might be caused by low attractiveness of private investments. But lack of labour-demand can also stem from high **costs of financing investments**. Therefore, you should analyse whether and to what extent the current conditions offered by financial markets and influenced by respective policies create hindrances to investment decisions.

Principally, high financing costs in the country under analysis can be the result of (1) problems in capital mobilization and/or (2) poor financial mediation by the financial institutions (see also Hausmann/Rodrik/Velasco (2004), p. 18). You discuss the extent to which both aspects apply in your country:

(1) Aspects of capital mobilisation

Capital mobilisation is an important factor for financing. Financial institutions like banks can only lend as much money to businesses as they are able to receive from depositors beforehand. So if there is just not enough capital supply in the country we observe higher prices for capital (higher interest rates). The development of the **gross capital formation**⁷ rate (in per cent of GDP) vs. the **domestic savings** rate (in per cent of GDP) can give you first insights into the magnitude and directions regarding capital mobilization problems. If a low capital formation is accompanied by a high savings rate, there might be no problem of insufficient capital supply.

Savings basically can be invested in the country (e.g. money, real investments increasing the capital stock, financial assets) but also be transferred to other countries. In case of significant net capital outflows the main problem may not be capital mobilisation per se, but distortions that prevent its channelling into domestic investments. One reason for such a scenario might be a rather poor financial mediation (see also Marktanner/Nasr (2008)). Hence, by working on improving financial mediation in the country a higher proportion of savings could be used for capital formation in the economy.

Unfortunately, many poor developing countries face the situation of a combination of all negative aspects stated above: low capital formation, low domestic savings and only limited attraction of external capital inflows such as official development assistance (ODA), foreign borrowing and foreign direct investment (FDI)⁸ (see e.g. United Nations (2009)). A low level of FDI usually correlates with poor business environment conditions as well as poor financial mediation. In this situation, low domestic savings rates might initiate a vicious circle, further deepening the problems of financing.⁹

7 Formerly: gross domestic investment.

8 The impact of FDI in financing gross capital formation is not clear-cut (see Krkoska (2001)). The positive effects of FDI are generally related to improving the overall economic situation, e.g. creating jobs, transferring technology, upgrading skills, fostering competition, and contributing to the fiscal standing of the economy (see in general World Bank (2010), p. 2). Thus FDI development is rather an indicator for challenges and opportunities in the business environment than for capital mobilization.

9 Low domestic savings translate into little investments, little investments into little output, little output into little income, and little income again into little savings, thus perpetuating problems of capital mobilization into the future.

6 See also the argumentation by Hausmann/Rodrik/Velasco (2004), p. 18.

In many poor developing countries capital formation is highly dependent on ODA and foreign borrowing to compensate for little domestic savings. Though these capital injections might ease the pressures on the capital market they increase debt risks and often raise issues of higher risks in the financial sector. If applicable, you might comment on these aspects, as well.

(2) *Aspects of financial mediation*

Despite low domestic savings rates many countries still have substantial potential for domestic resource mobilization through e.g. **remittances or non-recorded savings** (see United Nations (2009)). As both sources are often transferred and deposited outside the formal financial sector, they are indicators for problems in financial mediation. In general, the size of the formal financial sector and banking sector depth are major indicators of the ability of the economy to provide and coordinate financial resources for economic activities.

Financial institutions (e.g. banks, non-bank institutions like credit unions, microfinance institutions, etc.) allocate financial resources, thus impacting on credit provision and conditions. The following indicators are useful in order to analyse the degree of efficient allocation of financial resources by these institutions:

- Real lending rate
- Interest rate spread
- Domestic credit to private sector
- Share of long-term financing
- Overall outstanding loans
- Non-performing loans

Problems in these areas often point to **governance problems** in the sector (e.g. inconsistent laws and regulations, inadequate supervisory function of central bank, etc.). Unaddressed governance problems lead to higher risks, instabilities and declining trust in the financial sector, thus reinforcing domestic resource mobilization problems.

Useful data sources can be found e.g.:

- Financial sector indicators of the World Bank, <http://data.worldbank.org/topic/financial-sector>

- Financial Development Report with Financial Development Index provided by the World Economic Forum, http://www3.weforum.org/docs/WEF_FinancialDevelopmentReport_2011.pdf

- Data provided by national central banks

Step 8 to 11: Analysis of specific sector conditions and policies

The overall picture of the business environment gained so far is useful for a first inventory of possible challenges. However, it will very likely fail to **address the diversity of business conditions in the observed country**. For example, enterprises are affected differently by regulations because e.g. they produce their goods and services in different economic sectors for which different regulations apply. Or they differ in legal status, turnover, number of employees, etc., leading to different treatments regarding the tax regime, labour laws and regulations, etc. One important function of sectorial policies is to promote the development in the respective sector by altering the business environment conditions. In order to deal with this kind of diversity we need to complement the analysis of general factors influencing the business environment with an analysis of selected specific sector conditions and policies.

Step 8: Identifying important sectors for employment generation

The purpose of step 8 is to explain your choice of sectors for the **specific sectorial policy analysis**. One important selection criterion is the relative importance of the sector to employment generation using the findings of step 2 (Step 2: Patterns of economic development in the past). If available, analyses with quantitative forecasting regarding sectorial economic development and employment trends¹⁰ might help guiding your selection.

Despite a great diversity in sector composition and development patterns of different developing countries, your specified sector analysis should at least address the following two segments of the economy: **MSMEs** (including informal economy) and **public sector**. The high proportion of mainly informally operating micro, small and medium

¹⁰ See for example ILO employment trends methods, discussed e.g. by ILO (2010).

enterprises (MSMEs) is a decisive factor for employment generation in all developing countries. Based on your analysis of specific sectors you might be able to highlight in more depth the cross-cutting issue of MSMEs in these sectors. With shares in total employment of 5-10% employment in the public sector may not be decisive from a quantitative perspective, but it may exert influence regarding wage settings, formal employment, etc.

Step 9: Sector specific analysis of labour demand conditions

In step 9 you discuss as many sectors as you find appropriate (see argumentation in step 8). In general, your sector specific analysis should also deal with the questions to what extent barriers to entry or exit the sector are in place and whether you can identify sector-specific hindrances to investments. However, the linkage to employment and income generation should be made clear (e.g. special role of agriculture due to high labour-intensity).

Step 10: Employment prospects in MSMEs (including informal economy)

High shares of self-employment in MSMEs are a distinctive feature of developing countries. In order to assess employment prospects in MSMEs (including informal economy) you should describe **central features of MSMEs** (e.g. overall number of MSME development, size distribution, sectorial and regional composition, ratio between formal and informal enterprises, etc.) **and employment in MSMEs**. Furthermore, you may scrutinize in more detail whether the overall business environment, described in previous steps, holds also for different types of MSMEs (especially for those with high employment shares and/or dynamics).

In a second step you tackle MSME policies. In your description and evaluation of MSME policies (e.g. with respect to addressing important business constraints and governance issues, like quality in coordination, implementation, monitoring, etc.) you should have the following considerations in mind:

In general, MSMEs are viewed as central for dynamics of economic development and job creation, thus making **MSME policy** an important instrument for productive employment. Though a recent literature review concluded that with respect to employment generation “small is still beautiful” (see de Kok et al. (2013), pp. 5-6), finding empirical evidence for a more detailed impact analysis of SME on employment is difficult. Standard arguments in favour of MSME support (and therefore discrimination against large enterprises) are based on the assumption that MSMEs are believed to (1) be more labour-intensive than larger firms resulting in more general employment growth if the share of SMEs rises, (2) enhance competition and entrepreneurship with subsequent positive spill-overs to the economy, and (3) be just as productive as larger firms, but credit constraints and other institutional failures impinges on them (see ADB (2009), p. 40). To overcome especially the last aspect, special assistance represents a useful second-best approach.

However, the same study points to the problem that the vast majority of micro-entrepreneurs would gladly switch to stable wage employment if only the opportunity would occur (see ADB (2009), p. 26). Thus their ability to expand and become employers might be rather limited. As a consequence, a rapid growth of new businesses is often accompanied by a high number of idle and loss-making enterprises leading to significant job destruction in its course. But still, some fast growing MSMEs, the so called “gazelles”, might compensate for these insufficient employment effects of many MSMEs. For example, according to a study of gazelles in Brazil high employment growth gazelles constituted 8.3% of Brazilian private businesses and created 57.4% of net new jobs between 2005 and 2008 (see Gibson/Stevenson (2011), p. 5). These empirical results regarding employment effects of MSMEs clearly stress the need of MSME policies to be well targeted to high employment growth MSMEs. Though this point is accepted in the employment promotion literature, understanding the “production process” of gazelles and, based upon that, identifying “latent” gazelles is not easy. Also, gearing public support to these businesses might contradict more broad-based MSME policy objectives like, for example, poverty reduction.

Step 11: Employment in the public sector

In developing countries the public sector exerts important influence on the outcome of the labour market by setting respective regulations. But also its function as formal employer should not be neglected. Though average wages in the public sector might be lower compared to average wages of the (formal) private sector, especially in uncertain times wage and social security conditions in the public sector can be quite attractive, reducing the availability of skilled personnel in the private sector. Thus, the bigger the share of employment in the public sector in relation to private employment is, the higher is the probability that the public sector “crowds out” employment creation in the private sector (see e.g. Bradley/Postel-Vinay/Turon (2011)).

The size of the public sector in terms of both its number of employees and its share in GDP in relation to the private sector allows you to assess the role of the public sector as an employer. If this quick-check indicates a substantial role of the public sector in employing part of the (formally employed) labour force, you might want to go further into detail by describing in what way **central features of public employment** deviate from (formal) employment conditions in the private sector.

Depending on the country, a discussion of the **following indicators** applied to the public sector might highlight possible structural problems:

- Wage levels and wage development (also in relation to the quality of public sector operations and services)
- Trade union membership rate and collective bargaining process
- Degree of employment protection
- Degree of social insurance (e.g. share of expenditures for pension liabilities of the public sector in social protection expenditures)
- Pay schemes and their transparency, quality of human resource management system



Stage C: The labour supply-side: the qualitative dimension of labour force development

In the second stage B we added more details to our diagnostic regarding possible challenges on the demand-side of labour. As both sides – labour demand and supply – are likewise important for employment, correspondingly we

turn to the supply-side of labour. Here we look deeper into the qualitative dimension of labour force development (see Figure 7).

Figure 7: Guide through stage C

Steps	Labour Supply	Matching in the Labour Market	Labour Demand
C	What prevents the labour force from offering (in sufficient quantities) the skills in need?		
(12-14)	Objectives of steps 12 to 14:		
	<ul style="list-style-type: none"> ■ Assessing the problem of skill mismatch ■ Getting to know the extent and quality of the provision of educational services ■ Identifying major challenges in the education system to provide adequately skilled labour supply 		
	<i>Orientation: The first step of stage C (supply-side analysis of labour) is to try to assess to what extent skill mismatch is indeed an issue in the actual country.</i>		
12	Qualification of the labour force		
	<i>Orientation: Principally, a mismatch of skills can be the result of problems (a) in the education system, and/or (b) inefficiencies of the matching process in the labour market. The latter refers, for example, to the role of Public Employment Services in providing job counselling services which might not be very effective. We will deal with such possible constraints in the matching process of the labour market in stage D. For the remainder of this stage we focus on the outcomes and conditions of the education system.</i>		
13	Describing the education system		
14	Challenges in education and training with special focus on TVET		

Step 12: Qualification of the labour force

The first step of your analysis of the labour supply-side consists of an **examination of the qualitative attributes of the labour force/working age population** in the country. At the core are aspects of education and skills, disaggregated by sex and age in order to cover also gender and youth issues (see also ILO (2012a), pp. 27; 52-53).

Useful indicators are e.g. (see education section of the World Development Indicators database, <http://data.worldbank.org/topic/education>):

- Literacy rates
- Education attainment rates
- Labour market participation by the education attainment level¹¹

If applicable and available, you can provide information regarding the **qualitative dimension of labour migration**, as well.

¹¹ However, because of usually limited quality of education in developing countries, these attainment rates might not be very informative about the true skills of the working-age population.

Especially in the context of low income countries we have to recognize that the quality of labour depends not only on the education and skills, but – on a very basic level – on **health and nutrition status**, as well. Therefore, you should complement your analysis with analysing the health situation of the population, using basic health indicators such as mortality rates, stunting and wasting among children and HIV/AIDS prevalence e.g. provided by the following sources:

- World Bank, <http://data.worldbank.org/topic/health>
- World Health Organisation (WHO) <http://www.who.int/gho/countries/en/index.html>, and
- other initiatives like e.g. <http://www.countdown2015mnch.org/country-profiles>.

In order to better classify the current situation of the human resource base in the country, we recommend to benchmarking with other countries as well as observance of past developments (continuous decline/increase of educational attainments of adult population). If available and applicable, comparing data regarding the qualitative attributes of unemployed/underemployed with those of job vacancies could indicate the extent and nature of problems of skills mismatch.

Step 13: The education system in the country

Examining the qualitative attributes of the labour force in the previous step 12 means nothing else than to assess the output of investments in human resource development in the country. Now in the remaining part of stage C we have a closer look into the education system, being a major input factor for human resource development. Therefore, in step 13 you provide a basic snapshot of the education system by explaining the main features of the education system briefly. This basic understanding is needed in order to locate the challenges of education and training analysed in more detail in the next step 14 more easily.

Your description of the system of skills development starts with an **overview regarding the structure and legislative basis of the system** (see e.g. Kuruvilla/Erickson/Hwang (2001), p. 4; UNESCO (2011)). Legislation provides a framework for education policy and outlines the role and responsibilities of the state as well as the strategies to achieve the policy goals. With respect to the structure you

should name key actors for national strategic planning, coordination and implementation, and their respective relations/responsibilities regarding different subsystems. Also you describe the institutions of the education sub-sectors (basic, secondary, tertiary, and Technical and Vocational Education and Training (TVET)¹²) briefly. If applicable, the share of private relative to public institutions in the respective sub-sectors might guide subsequent questions regarding allocation mechanisms and financing issues.

Inadequate provision of services is a visible sign of either lack of resources and/or improper management of the functioning of the education system. Therefore, you should focus on analysing financing and human resource aspects as well as the management of the system.

(1) Financing aspects

Financing aspects concern the way financial resources are mobilised, allocated and used toward production and provision of education services (see UNESCO (2011), pp. 29-30). **Key issues** are among others sufficiency of resources (e.g. education expenditures as per cent of GDP or government budget) and quality of resource allocation (e.g. share of the education budget for different education sub-sectors and existence of policies to address possible imbalances, predictability and sustainability of financial resource provision¹³ (see also UNESCO (2006), p. 11)).

Benchmarking with other countries might help you to assess the extent of financing problems, especially of underfinancing, in your country (see e.g. information by the UNESCO Institute for Statistics, <http://www.uis.unesco.org/Education/Pages/education-finance.aspx>). High levels of corruption indicate problems in resource allocation, as well (see Transparency International (2010), p. 14). It is also important to check whether mechanisms are in place to ensure that skilled migrants and/or countries of destination and/or employers abroad are contributing to education cost incurred in the country of origin which might otherwise be lost to the public budget.

12 TVET is the overall term for initial vocational education and training as well continuing vocational education and training.

13 Guiding aspects in this context are beside others: Fees or no fees for the courses? Credit options or not for the direct costs (course fees) and indirect costs (livelihood) of the courses? Public funding of the transition system or not?

(2) Human resource aspects

Furthermore, the quality of the system decisively depends on the number¹⁴ and capacities of teachers in educating and training. Also, the training of trainers efforts need to be adequately complemented by educational facilities (school space and equipment) (see e.g. UNESCO (2006), p. 14). However, as teacher salaries typically account for more than 80% of education budgets, financing issues are closely linked to the quality of instruction.

You should try to give a very basic assessment to the overall situation using e.g. data provided by the UNESCO Institute for Statistics (<http://www.uis.unesco.org/Education/Pages/teachers-statistics.aspx>).

(3) Management aspects

The management of the education system is the other major factor influencing skills development in the country. Management aspects cover capacity issues, as well. That means the capacities to lead and to manage the system of skills development and the processes of interactions are assessed. In addition, performance management is scrutinized, looking at the extent of systematic, integrated result oriented monitoring, evaluation and quality control.

Step 14: Challenges in education and training

On the basis of this snapshot of the system of education, you turn to highlighting challenges in general education (covering primary, secondary and tertiary level) as well as in TVET.

Challenges in general education

Access, participation, quality (including the relevance of the curriculum for labour market needs, e.g. what kind of qualifications are needed in order to fulfil education requirements for the majority of jobs) and efficiency in general education are leading topics for this assessment.

Admission, enrolment or attendance rates are indicators used to determine the **extent of access to elementary school and secondary level**. Because access to one level of education usually presupposes the mastering of the previ-

ous level, failures in early stages of education magnify their negative effect on skills development.

Although many countries improved access to elementary school in recent years, continuous participation in the education system up to a level which meets labour demand and job opportunities remains a challenge. Thus, depending on the availability of data you should try to assess the magnitude of **problems of retention**, looking e.g. at the share of drop-out of elementary and secondary levels, and, more general, the pattern of school age cohorts over the past two decades (cohort survival rate, completion rate) going through the different levels of education. The analysis should be informative regarding marginalized groups (e.g. poor, women) being excluded from education. Among the possible causes for low enrolment and high drop-out rates are formal barriers as e.g. school fees, but also further hidden costs (such as transportation or uniform costs), violence in school, socio-cultural-economic biases (e.g. with respect to gender), and incidences of child labour among lower socio-economic groups. As access and quality in rural areas usually lack behind urban areas, the analysis is complemented by disaggregated data informing about possible challenges in this regard.

Bridging of primary education to higher levels of education is also a critical issue in many developing countries. Again, recent focus on improving universal access to primary education might have led to neglecting subsequent pressures to improve education beyond the primary level. Therefore, existence and quality of measures that provide sufficient support and encouragement to students to continue their studies to secondary and higher education are analysed. In addition, you should discuss possible limitations to entry of secondary education (e.g. too little supply, not free of charge).

However, not only the duration in education matters, but also **the quality of education**. One important quality aspect is to adequately address diverse learning needs. Information on the national achievement in universally accepted learning competencies (literacy, numeracy, language skills, proficiency in science) and regarding the adequacy of teaching content (labour demand oriented) illustrates the performance.¹⁵ Because many attendants

14 This is relevant for the teacher-student-ratio which have an important impact on the quality of education.

15 The responsiveness of higher education to market needs can be assessed by e.g. looking at labour market feedback on job opportunities of graduates by field, admission of university graduates to graduate studies abroad, and graduate tracer studies.

leave the education system with secondary education, you should scrutinize in more detail the curriculum orientation using an integrated perspective which reconciles academic needs (geared towards higher education) with practical needs (matching needed life skills and labour market skills) (see also UNESCO (2011), pp. 39-40).

Challenges in technical and vocational education and training (TVET)

Technical and vocational education and training (TVET) has the function to facilitate the transition into the labour market. This is done by providing learners with practical knowledge and skills which are focussed on the labour market needs (qualification function). “TVET policies are generally designed to guide the effective provision of practical labour market skills through specialized education services (often delivered in formal settings) and training programmes (often provided in non-formal settings)” (UNESCO (2011), p. 43). Thus, the system of **TVET is like a hinge between general education and the labour market**. In order to make it effective central features and outcomes of both areas have to be integrated in TVET. The fundament of skills, knowledge, and career orientation provided by the pre-levels of education needs to be matched with the skills and knowledge demand of employers and their career plans for the potential employee.

Apart from this basic function of TVET systems “the quality of TVET is increasingly associated with having a broader scope including personal and general skills which can contribute to lifelong learning, participation and community building, through **entrepreneurial skills¹⁶ as well as a broad set of skills** regarding sustainable development [socialisation function]. These broad skill sets tend to have a bearing on an individual’s employability, active civic participation, and health, and to community building and economic development at the regional and local level” (UNESCO (2010), p. 5).

Taking these two interlinked central functions of TVET together, the TVET system can be seen as a key system for addressing learning needs: it needs to offer all those (lifelong) learning needs which cannot be provided by pre-levels of education and working experience. Obviously, because of the path-dependency mentioned above

the burden for TVET systems to provide adequate learning increases with low quality of education systems and absence of salaried employment and, subsequently, private sector initiatives. Hence, these conditions - typically given in developing countries - undermine successful TVET systems. In order to keep your feet on the ground regarding the potential of TVET systems in improving employability and sustainable development we recommend you to discuss the relation of these framework conditions to the TVET system in your country.

Historically, countries provide quite **different forms of technical vocational education and training**, making cross-country comparison as well as general policy advice hard to produce (see e.g. UNESCO UIS (2006)). TVET systems usually differ e.g. regarding using different

- places for learning: schools, training centres, colleges that have been created for the purpose of vocational learning or – with respect to trainings facilities workplace or in-enterprise workshops primarily established to produce goods and services
- forms of acquiring skills: formal, non-formal education; informal learning
- forms of regulation/provision: (1) government regulated systems with general and vocational education closely associated; (2) market regulated systems with TVET largely left to the market, meaning limited governmental interference and training is being delivered by private training providers, companies, employers on the job or by learning and working; (3) systems regulated by traditions (e.g. craftsmen, guilds); and (4) mixed systems like e.g. the dual systems (Germany, Switzerland, Austria, Netherlands, Denmark), “Formation en alternance” (France), and National Training Services (Brazil and other Latin American countries).

In view of the abovementioned functions of the TVET system an integrated approach is needed combining different forms of TVET provision effectively. How this optimal approach should look like can only be assessed having the specific needs of the labour force, the capacities of the public and private sector to manage (together) TVET and the historically developed system of TVET in view. In your analysis of the TVET system you should use available **data on access, participation and quality provision** in order to evaluate to what extent the TVET system fulfils

¹⁶ With entrepreneurial skills we refer to skills like e.g. analytical problem solving, planning & organizing, self-management, leadership, personal accountability, goal orientation etc.

its stated objectives. Furthermore, due to its interconnecting nature, you should evaluate the **extent and quality of the linkages to labour market institutions** (e.g. public employment services with career guidance and counselling, job placements), and **in more general to private sector participation** (e.g. employer engagement for TVET policy development and implementation, quality of co-ordination and cooperation of governmental institutions, training providers and the private sector).

Because of the high variety of TVET systems and needs, we can only point to **key issues** which are usually relevant in developing countries. Your task is to assess, whether and to what extent these issues apply to your country context (see Federal Ministry for Economic Cooperation and Development (2006), p. 9; BMZ (2012), p. 11). Key issues – with special respect to the initial vocational education and training – are among others:

- Weak legal framework
- Chronically poor funding
- Enormous demand because of increased age cohorts and enrolment rates
- Low commitment of firms to provide and finance training places
- Highly fragmented institutions with overlapping, inconsistent competencies of different ministries to regulate/implement TVET policies
- No national multi-stakeholder agency which is a driving force for (consistent) implementation of TVET policies
- Low reputation (acceptance) of formal degrees of the TVET system ('white collar syndrome', meaning low reputation of TVET in relation to academic education, e.g. university degrees)
- Low orientation to actual needs (including e.g. informal sector, gender mainstreaming) and working practices
- Focus on formal, post-secondary education impedes transition from general to vocational education, insufficient acceptance of non-formal or informally acquired competencies
- Lack of modernisation of curricula
- Lack of (adequate) systems of testing and certification
- Missing of extra preparation course for drop outs and low skilled workers for Integration
- Lack of a second chance to achieve the minimum standard of qualifications/competences.
- Missing attractive career pathways for high skilled professional workers with a competency-based access to universities
- Lack of a transition management

Stage D: Matching demand and supply of labour: the impact of labour market institutions and policies on employment generation

As explained in the beginning, employment problems can finally be caused by constraints to the matching process in the labour market. Thus, in the final steps of our diagnos-

tic of constraints to employment we tackle the matching process of the labour market (see Figure 8).

Figure 8: Guide through stage D

Steps	Labour Supply	Matching in the Labour Market	Labour Demand
D (15-17)	<p>To what extent do labour market institutions, regulations and policies impact positively on the matching process?</p> <p>Objectives of steps 15 to 17:</p> <ul style="list-style-type: none"> ■ Understanding wage formation as the central coordination mechanism in the labour market by connecting wage/productivity development with major factors influencing wage formation, e.g. labour law and regulations, wage policy, collective bargaining system ■ Assessing the effectiveness and efficiency of labour market and social protection policies: To what extent can active labour market policy address inefficiencies in the matching process? To what extent can passive labour market and – more general – social protection policies safeguard people from poverty and loss of income due to unemployment? 		
15		Wages, labour law and regulations, collective bargaining system	
16		The role of active labour market policies and institutions	
17		The role of passive labour market and social protection policies and institutions	

Here again, the public sector is theoretically in the position to mitigate some of the problems in the market. With respect to improving the matching process in the labour market, **intermediation services** play a crucial role. Such services, like Public Employment Services (PES), “interpose themselves between workers and firms to facilitate, inform, or regulate how workers are matched to firms, how work is accomplished, and how conflicts are resolved” (see Autor (2008), p. 1).

Step 15: Wages, labour law and regulations, collective bargaining system

Wage settings and, more general, contract agreements represent **the coordination mechanisms in the labour market**. A rise or fall of wages reflect scarcities (demand of labour is higher than supply) or – in the latter case – surpluses of labour (supply of labour is higher than demand). Thus, wages and working conditions demonstrate to employer and employees where resources are required. To get a rough understanding of important features of wage

formation in the country, you should scrutinize in a first step wage development in relation to economic development (e.g. changes in real wage vs. productivity development, disaggregated by sectors) and the extent of wage inequality.

However, wage formation is not only the result of supply and demand of labour. The functioning of this price mechanism is further influenced by labour laws and regulations as well as by the extent and functioning of collective bargaining systems (see also overview by World Bank (2012), p. 263). Thus, as a second step you briefly explain the **main features of these framework conditions** and identify possible challenges.

As argued before, assessing these framework conditions regarding their impact on the matching process of the labour market requires that you are aware of the **ambivalent nature of labour market regulations** (see also Coudouel/Paci (2006), p. 112). Therefore, you should scan existing labour regulations and the collective bargaining process in order to evaluate the respective effectiveness and efficiency in protecting the population from market failures regarding wage formation and working conditions. But at the same time you should also assess their impact on labour costs for businesses. Rigid and costly labour regulations tend to lower the incentives for long-term investment for businesses or for more labour-intensive production processes, thus negatively impacting on labour demand. As minimum wages and income policies are – in addition to collective bargaining – further core areas of wage policies, you should include these measures in your analysis.

Because generally developing countries face important deviations of de jure labour legislation from de facto practice¹⁷, explanations and comments regarding issues of enforcement, implementation and possible causes are an important part of your analysis of labour market framework conditions. In effect, poor coverage of wage policies and weak enforcement of labour regulations are possibly the major reason why empirical research only finds an

insignificant to only modest impact of wage policies and labour market regulations on employment levels (see e.g. World Bank (2012), p. 262). So instead of arguing in detail about pros and cons of specific labour market regulations and/or characteristics of collective bargaining processes for employment generation, you should concentrate on the big picture, especially regarding identification of starting points for improving implementation of essential labour market regulations and policies.

Step 16: Active labour market policies and institutions

In addition to regulatory measures defining the range of activities in the labour market, the matching process and labour market outcomes are further addressed by process-oriented labour market policies. For analytical and policy purposes labour market policies are usually split in “active” and “passive” subcategories. **Active labour market policies (ALMP) address inefficiencies in the matching process** with the objective of reintegrating the unemployed into the labour market. Inefficiencies in labour markets are manifold, e.g. regional frictions between vacancies and jobseekers, mismatch between labour demand and supply owing to discrepancies between competencies of job seekers and required skills, unemployment due to business cycle movements, etc. (see e.g. de Koning (2005) and also World Bank (2012), p. 267).

ALMP usually include the core activities of PES, namely information instruments and job mediation as well as specific reintegration measures such as training and subsidized labour (e.g. placement subsidies and wage subsidies for regular jobs, public work schemes, etc. (see e.g. de Koning (2005), p. 1). In case of high incidence of external labour migration, bilateral labour migration agreements supplement the portfolio of ALMP in some countries.

But in general the set of ALMP instruments is very heterogeneous with many deviations from country to country. Therefore, you should explain the different **elements of ALMP in your country's context** by describing the main characteristics of the most important measures and instruments and their governance and implementation structures (e.g. key actors in the labour market administration at macro, meso and micro level, coordination mechanisms of policies, etc.). ALMP often go hand in hand with activities of the private sector (possibly supported

¹⁷ In principle, labour market regulations and policies apply de facto only to the formal sector, meaning that the size and structure of the informal sector is a major factor defining the coverage of laws and extent of implementation. “In addition, in countries with weak implementation capacity, large pockets of unprotected employment persist even in the formal sector” (see Coudouel/Paci (2006), p. 114).

by donors), especially in the area of training measures. Therefore, we recommend that you undertake an analysis of these activities, where appropriate disaggregated into regions/sectors.

To get a first impression of the relevance of ALMP in general and with respect to specific instruments, it is useful to check for the “**spending effort**” which your country in question devotes to labour market policies: the share of public spending on labour market programmes as a percentage of GDP as well as its relative weight in total public expenditure are computed and benchmarked with other countries, if possible disaggregated also for different ALMP instruments (Martin (2000), p. 81).¹⁸ Expenditures on ALMP in developed countries range from up to 2.5% of GDP in northern EU countries to around on average 1% of GDP in non-EU countries such as USA, Canada, Australia, etc. (see OECD (2009), p. 71 and Grubb/Puymoyen (2008), p. 113). The corresponding figures of public spending for developing countries are much smaller (in the case of LIC especially in Sub-Sahara Africa close to negligibility). Therefore, if applicable, you should include externally financed programmes in your calculations.

Because heterogeneity is strong, **assessing the effectiveness and efficiencies** of these instruments very likely might not be an easy task for you.¹⁹ Consequently, within the framework of our guidelines of ELMA we find it also hard to provide you with suggestions on key issues. However, problems with respect to the **core activities of PES** are usually very dominant in developing countries. Due to a high share of micro and small firms and the predominance of informal contractual arrangements and information spreading of job openings, firms offering good labour conditions, good quality of educational degrees, skills certificates, etc. are less effective in developing countries. This, in turn, makes it more difficult for PES to address information gaps and asymmetries than in developed

economies. In addition, the core activities of PES, information instruments and job mediation practices, are based on registration systems for vacancies and jobseekers, which usually do not work well in developing countries. The low coverage of unemployment insurance benefits – if the instrument exists at all (see next step) – does not work in favour of using PES in developing countries. Also, the majority of businesses limits contact to public officials to an absolute minimum. This low participation of jobseekers and businesses alike reinforces a poor service quality of PES.

In view of profound problems of PES in improving the matching process of the labour market, the **focus of ALMP in developing countries is often more on training and on (direct) job creation schemes**, namely Public Works Programmes (PWP) and business start-up programs.²⁰ Key issues with respect to the effectiveness and efficiency of PWP are that the effects on long-term integration into the labour market are marginal, whereas the income support function of PWP seems to work (see e.g. Subbarao (2003), Betcherman et al. (2004), and World Bank (2009), (2012)). Thus, often PWP rather meet objectives of passive labour market and social protection policies than those of active labour market instruments.

18 Further indicators for the spending effort might be e.g. spending on active measures per person unemployed relative to average earnings and the number of participants on active programmes relative to the size of the labour force (taken from Martin (2000), p. 81). However, these indicators are used for an assessment of ALMP in OECD-countries and probably need to be adapted to the respective context of a developing economy.

19 Rigorous evaluations exist mostly in the context of developed economies. Thus, only limited information regarding effectiveness and efficiency of ALMP in developing countries is available (see e.g. Betcherman et al. (1999), (2004), Islam (2003); Vandenberg (2008); IDB (2009)).

20 Especially middle income countries, which have the means to finance such programmes, rely relatively more on PWP than advanced countries (see Cazes/Verick/Heuer (2009), p. 10).

Step 17: Passive labour market and social protection policies and institutions

Passive labour market policies (PLMP) have been introduced to safeguard people from poverty and loss of income due to unemployment. Thus, instead of addressing inefficiencies in the matching process, PLMP aim at compensating for socially unacceptable labour market outcomes. Unemployment insurance, minimum wages, and social protection measures provide a floor for income protection which is related to meeting minimum needs (in the case of unemployment insurance benefits (UIB) the benefits might be higher due to specified eligibility criteria). In analogy to the assessment of ALMP, you should explain **the measures and instruments of PLMP**, referring to spending efforts, characteristics of instruments and implementation structures.

In developed countries expenditures on PLMP are usually higher than public spending on ALMP. One important reason for this spending pattern is that **UIB-schemes** were installed in order to function as automatic stabilizers in times of economic crisis. However, with a persistent unemployment rate in advanced economies this important stabilisation function for the labour market faded into the background of PLMP assessments. But experiences with the global financial and economic crisis brought the initial purpose of PLMP - to ease adjustment to external shocks and ensure employability through times of crisis especially for vulnerably employed (see de Koning (2005), p. 3) – back into the frontline of international discussion.

Therefore, within the analysis of PLMP you should pay special attention to **existing measures aiming at protecting the incomes in case of unemployment**. However, due to the typical labour market situation in developing countries (high share of informal working relations, underemployment, and vulnerable employment) unemployment compensation schemes based on the (formal) employment status, popular in OECD countries, usually play only a minor role (for further discussion see Vodopivec (2009)). Even in transformation economies the coverage of UIB varies much and is considerably lower than in advanced economies (see World Bank (2009)).

Stage E: Summary and conclusions

We are now in the same position as a medical expert who has put his patient through all the tests and checks needed for a sound diagnostic and is expected to present his conclusions and recommendations for therapy. But this analogy also has its limits: contrary to the diagnostic undertaken by a single medical expert, ELMA is part of a process with many different stakeholders involved. In addition, the object of our diagnostic – employment problems – is complex. Also, the quality of diagnostic

depends on the availability of sound data and information, which in case of developing countries is oftentimes not available. Thus, we should not expect to come up with clear cut conclusions. Instead, in the following last stage of ELMA you should try to summarize the main findings in a “user-friendly” manner and prepare the ground for the follow-up process, e.g. for discussions and further research on the basis of your findings (see Figure 9).

Figure 9: Guide through stage E

Steps	Labour Supply	Matching in the Labour Market	Labour Demand
E (18-20)	<p>What are the main challenges to employment creation?</p> <p>What kind of consequences can be drawn regarding reform efforts of the respective country in general and in particular of German development cooperation programmes, supporting employment promotion?</p> <p>Objectives of steps 18 to 20:</p> <ul style="list-style-type: none"> ■ Getting to know the relative importance of the main constraints to employment generation ■ Based on a participative process defining possible areas and options for government action ■ Proposing options for of German development cooperation programmes of how to incorporate the findings of ELMA 		
18	Summary of challenges and their relative importance to employment generation		
19	Possible options and approaches for reforms to take up the challenges		
20	Conclusions and consequences for German development cooperation		

Step 18: Summary of challenges and their relative importance to employment generation

In the present analysis we tackled the employment and labour market situation in a developing country with central features like poverty, pervasive informal employment relations, high income inequality, etc. In view of these circumstances, it may not be very complicated to come up with a long list of challenges regarding decent employment. Following the integrated and systematic structure of ELMA is one important step to prevent simply creating a “laundry list” of problems, constraints, challenges at the end. Therefore, in a first step you should **name the key**

challenges (that is the most binding constraints to employment creation) which you have identified throughout your analysis using the structure of ELMA.

In order to prepare the ground for sound discussions on possible conclusions and recommendations, you should try to **prioritise your findings** in a second step as much as possible. In practice, you should go over the different factors identified in Figure 2 and checked in the various steps (see overviews) and try to answer the following questions for each factor:

- 1) What is the relative importance of each factor for the central forces of employment in your country specific analysis? For example how important is demographic

development for labour supply? How much impact has the system of coordination in the labour market on stated problems of matching?

To give you an example: Labour market policies are important. Thus, respective challenges e.g. in carrying out active labour market policies are consequently likewise important to address. However labour market policies might - even if carried out in the best of all ways - not be in the position of fundamentally altering labour market outcomes. This is because the fundamental forces of demand and supply working in the labour market exert higher impact on wages, contract agreements and working conditions than regulatory framework conditions and active, passive labour market and social protection policies. This is especially true in the context of developing countries with a high share of informal market and non-market employment relations (subsistence production) and very little scope for public finance.

In general, the bigger the gap between labour supply and labour demand is, the less effective are labour market policies in reducing overall employment problems even if they are implemented efficiently. This does not mean that releasing constraints to labour market policies would not be positive for employment generation. But reform efforts in that area should definitely be accompanied by complementary reforms in other areas.

In case of high mismatch between labour supply and labour demand you should give factors negatively influencing labour demand and supply a high priority: One major cause for excess labour supply is usually insufficient labour demand due to a poorly developed economy (business environment). Mismatch of skills and qualifications creates additional unemployment or underemployment (education system). Excess labour supply often leads to external migration (if labour markets in neighbouring countries are receptive to migrants). Consequently, smoothing negative impacts of migration by better migration management is an option, too.

- 2) What kind of identified challenges can be changed in short- to medium-term time horizon? For example some factors, like demographic development or geographical situation, are given, others not. However, changing them quickly might prove to be unrealistic.

This is especially true for fundamental problems in economic policy making and governance of the public sector, e.g. implementation gaps. Hence, you should try to focus on those constraints where the chances for successful reforms within a medium-term period (2-6 years) are highest.

- 3) With respect to economic policy making and governance of the public sector, other linkages to different challenges might exist, too. Can you identify some? Informal economic activities, for example, are important for employment generation. However their informal nature challenges economic policy instruments in a very broad way: For example, collective bargaining processes do not work efficiently, informal economic activities make it hard for a poor country with very limited capacities to install social protection/ insurance measures or even to use PES effectively. So, if you recognise such tendencies of one factor challenging different interconnected areas of public action, try to explain their relevance as specific as possible by e.g. referring to sector specific situation.

Depending on the country's context and initial interests in conducting ELMA, **the findings should be mainstreamed with respect to cross-cutting issues** (e.g. gender, youth, inequality, and sustainability).

Step 19: Possible options and approaches for the country to take up the challenges

The main purpose of ELMA is to enhance a thorough understanding of the nature of the various factors defining challenges and, based upon that, starting points for increasing productive and decent employment in a given country. This thorough understanding can be used by the different stakeholders in the country to discuss options and approaches to take up the challenges: For example the results of ELMA might present a good starting point for discussing the issue of mainstreaming existing national development policies to the need of employment generation or to develop national employment strategies.²¹ In order to prepare the grounds for such a follow-up process we would like you to propose most **important areas of**

²¹ For how the instrument of national employment strategies can be used in the context of developing countries, see e.g. Boldemann et al. (2009).

government intervention supplemented with information regarding possible reform approaches.

In order to achieve this it is important that you transfer the integrated perspective of causes of employment problems, gained through ELMA, into the recommendations for possible options and approaches for reforms in the country. What do we mean by that? For example, though lack of finance is usually one major reason for ineffectiveness of different policies (e.g. TVET system, labour market institutions) to recommend more financial resources for each policy area might not be a very effective recommendation. If we add all these individually reasonable pledges for higher sector budgets together it becomes apparent, that the partner in view of budget deficits, low domestic resource mobilization and high debt rates will not be able to take up this recommendation. Instead, differentiation in reform options is needed. Such a differentiation should mirror the different weighing of constraints to employment generation identified by ELMA in a plausible way.

In addition, your recommendations should be in line with the political commitment and should reflect the institutional, organisational, technical and financial capacities on the partner side. This is necessary because the only way to reduce constraints is by government action, probably supported by donors. In this respect, the knowledge of governance issues gained through ELMA helps to critically assess the framework conditions of policy implementation. The question should be discussed of whether government action could realistically work on binding constraints in short- to medium-term horizon. This includes also critically assessing the current effectiveness of donor support. If this is not the case, you could address the question of what (complimentary) changes in governance are needed in order to improve the implementation of proposed reforms.

Step 20: Conclusions and consequences for German development cooperation

In step 19 we summarized our insights into major bottlenecks of employment generation in general. Our final step is to address the question, where and in what way the German development cooperation could support its partner's effort to take up the challenges. Much of the conclusions and consequences for German development cooperation depend on the initial purpose for carrying out ELMA. But generally one important benefit of using ELMA is that such a broad-based analysis tool widens the perspective. Different programmes, being technical cooperation or financial cooperation programmes, but also the cooperation with other donor and implementing agencies might benefit because possible new options of realizing synergies between different projects (and subsequently intervention areas) can be identified.²²

So finally, you should evaluate in what ways the **present findings alter framework conditions for the operations of the various development cooperation programmes in the country**. Again, we would like to remind you that it is not the purpose of ELMA to come up with final and specific recommendations for interventions, but to guide and facilitate further research and discussions of employment related aspects of German development cooperation programmes.

22 With respect to gearing private sector development interventions closer to employment generation an overview is given by Rösler (2013).



Annex A:

A practical example for conducting ELMA

In the framework of the implementation of the GIZ programme “Vocational Education & Training and Employment Promotion” in Kyrgyzstan a study²³ was produced in 2012 tackling the labour market and employment policy situation in the Kyrgyz Republic by identifying constraints

and options for employment development (regarding more details on the process see Box 2).

The objective of this study was twofold:

- First, the study identifies relevant areas of intervention for future GIZ programmes and shall support a mission assessing the progress of the GIZ programme “Vocational Education & Training and Employment Promotion” which was implemented in spring 2013. In addition, in the short- and medium-term it can serve as a reference for policy and decision makers in the Kyrgyz Republic.
- Second, the present study has contributed to developing the methodological guidelines ELMA.

²³ Wolfgang Schwegler-Rohmeis; Annette Mummert; Klaus Jarck (2013): “Labour Market and Employment Policy in the Kyrgyz Republic”, Identifying constraints and options for employment development, a Study by GIZ Programme Vocational Education and Employment Promotion in Kyrgyzstan in cooperation with GIZ Sector Project Employment-oriented Development Strategies and Projects, Bishkek, February 2013. For further information contact: employment@giz.de

BOX 2

From research to practice – process of involving stakeholders for a broad-based employment and labour market analysis

In early 2012 the Ministry of Youth, Labour and Employment of the Kyrgyz Republic, the GIZ programme “Vocational Education and Employment Promotion” and the GIZ sector project “Employment oriented development strategies” decided to conduct an employment and labour market analysis. The aim of the research was to identify obstacles in labour market development and employment growth, and to elaborate guidelines for future interventions and German-Kyrgyz development cooperation.

The research consisted of background papers analysing employment constraints in the field of macroeconomics and business environment, labour market and social policy and vocational education in Kyrgyzstan. During missions to Bishkek and in several interviews with key stakeholders and experts, the authors gained insights into labour market trends and constraints for employment growth in Kyrgyzstan.

In order to validate these research findings, the Ministry of Youth, Labour and Employment of Kyrgyz Republic together with the GIZ programme “Vocational Education & Training and Employment Promotion” organized a Public Forum to discuss the draft study: „Labour Market and Employment Policy in the Kyrgyz Republic - Research of Labour Market Policy and Employment Promotion in Kyrgyz Republic”.

During the one-day workshop, approximately 50 participants from lead ministries, the National Statistic Committee, the Chamber of Commerce, NGOs, trade unions, entrepreneurs, academia and representatives from international organizations such as ILO, IOM and EU discussed in three working groups key constraints for employment creation, which had been identified by the authors: Working Group 1 Macro-economic conditions, business environment and sectorial growth; Working Group 2 Labour market trends, structures and employment opportunities; Working Group 3 Vocational education and skills.

The working groups, moderated by Kyrgyz and international experts, discussed in depth the presented outcomes, referred to contradicting facts and missing information and made recommendations regarding future areas of intervention for German-Kyrgyz development cooperation. The final report represents the results of the workshop. Hence, the study is the result of a joint effort and is likely to be widely acknowledged by experts and policy makers.

Because of the closely related development process of both, study and guidelines, the main arguments and findings of the study for the Kyrgyz Republic can be presented by applying the structure of ELMA. By doing so in the following, we hope to give a more specific example of how ELMA could look like.

Employment and Labour Market Analysis (ELMA) for the Kyrgyz Republic: main arguments

Stage A: Economic, demographic and political framework conditions for employment generation

A (1-6)	<p>What is the basic potential for employment in the country?</p> <p>Objectives of steps 1 to 6:</p> <ul style="list-style-type: none"> ■ Familiarising with basic factors influencing labour demand and labour supply ■ Getting to know degree and intensity of employment problems
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Step 1: Geographical situation

Kyrgyzstan (KR) is a landlocked and predominantly mountainous country. This geographical situation for KR implies small, rather loosely integrated domestic markets, problems in producing essential products (agriculture, energy, and mineral resources), and high dependency on imports/external trade with at the same time unstable political framework conditions for external trade.

Step 2: Patterns of economic development in the past

Since 1996 the Kyrgyz economy started to recover from one of the worst economic declines in the region. The following 16 years showed an impressive average real GDP growth of around 4.7 per cent per year. However, the Kyrgyz economy still systematically underperformed in relation to the region. General as well as extreme poverty declined during the years with constant economic growth in between 2000-2008. Poverty in KR is closely linked to the geographical and economic characteristics of the country: Oblasts (administrative districts) that are predominantly agricultural and remote have higher rates of poverty.

In Kyrgyz Republic, as in most other CIS (Commonwealth of Independent States) countries, the restructuring process has moved labour out of unproductive industries to low productivity activities in agriculture, rather than to more productive sectors in the industrial and services sector. Hence, economic growth in KR was associated with increased employment at the expense of productivity and technology development. Though especially the services sector became more evident in driving economic growth in recent years, the overall process of structural transformation so far failed to provide enough job opportunities.

In general, the observed “underperformance” of the KR in the region can be attributed to problems of developing the economy (e.g. relatively scarce resource endowments, small markets which are not integrated due to insufficient infrastructure and geographic conditions, etc.). But the various downturns/recessions (1998, 2002, 2005, 2009, and 2010) negatively influenced the growth path, as well. Macroeconomic vulnerabilities show themselves in several ways: Because of close economic ties between Kyrgyz Republic and Eurasian Economic Community (EURASEC) neighbours, especially Russia, economic crises in these countries negatively affect the Kyrgyz economy by e.g. reduction in exports and remittances. At the same time, despite joining the WTO in 1998, the Kyrgyz economy was up to now not able to profit to a larger extend from the possibilities of entering the world market, least to say to take advantage of a strong growth in import demand of its EURASEC neighbours, Russia and Kazakhstan in the years 2000-2008. Thus, the regular trade deficit even widened. But the trade deficit is not only the result of an underdeveloped export sector. High shares of imports are further spurred by remittances and the fact that many production inputs need to be imported, making the economy vulnerable to the effects of rising import prices.

In relation to these profound macroeconomic vulnerabilities the scope of monetary and fiscal policies to mitigate possible negative effects of economic fluctuations is clearly limited. Due to a large informal sector and prevalent subsistence economy in the Kyrgyz Republic the size of the formal financial sector is relatively small. This means that much of the economy does not interact with the formal financial sector. So any effects of monetary policy on formal financial sector variables in KR tend to have

weaker effects on aggregate demand. Likewise, in view of chronic budget deficits, underperforming domestic resource mobilization and profound deficiencies in Public Financial Management, the possibilities of fiscal policy to mitigate negative effects are very limited. Instead, foreign aid and external borrowing are the main sources of budget deficit financing since independence, leading to increasing debt and financing risks.

Step 3 and 4: Demographic development and labour migration

In the case of KR these very much restrained dynamics of labour demand coincide with a growing population (annually 1.2% since 2010, before slightly less according to World Bank data), which is underpinned by the country's high birth rate. The growth of the labour force was constantly higher than the growth of employment. The observable high incidence of labour migration can be viewed as a "voting by feet" of the labour force in order to cope with such unfavourable labour market conditions. At the same time, these individual decisions reduced pressures on the domestic labour market. Also, remittances from labour migrants abroad are mainly used for consumption and, hence, reduce poverty. The increased demand of consumption goods spurred trading (small scale like shuttle traders, mostly informal), thus also providing additional jobs/income for the working age population in KR. Altogether, poverty reduction in KR throughout the overall stable years of economic growth between 2000 and 2008 seems to be mainly caused by high and increasing shares of remittances. So, at least through external migration the KR could take advantage of strong growth in demand of its neighbours, namely Russia and Kazakhstan. But the negative side – increased vulnerability to external shocks – showed itself also in the course of the global financial and economic crisis.

Step 5: Labour market trends

Based on estimations of balance of labour resources sectorial employment (formal and informal) shows the following characteristics:

- Profound reforms in agriculture resulted in the formation of individual peasants' farms, in turn leading to an increased number of people employed in agriculture, absorbing some of the surplus labour force (driver of growth and source of employment in the mid-90s). Employment growth in the agricultural sector has

become sluggish in recent years due to slow progress in productivity. Also, around 38% of all employed youth work in the agricultural sector, which is characterized by seasonal work and low salaries.

- Growth in employment was observed in areas such as trade, repair of vehicles, household appliances and private utensils between 1991 and 2004. In 2008 about 45% of the employees were active in the service sector, in 2010 43.1%.
- The industrial sector recovers since 2004 and had a share in the labour market of about 20% (in 2008) and about 22% in 2010.

The labour market is characterized by the following employment problems:

- There is still an on-going shift from regular wage employment to self-employment (especially in privately owned agricultural land and the service sector). Because self-employment dominates the informal economy, this situation indicates increasing shares of informal employment. Underemployment and vulnerable employment conditions are mainly outputs of the informal economy: According to estimations about 70% of the active labour force is employed informally (including agriculture) with the majority in rural areas, but an increasing number in urban areas, too. Consequently up to four out of five jobs in rural areas are not formal, while over 50% of the employed in urban environments work informally.
- Clear linkages between poverty, underemployment and informal employment exist: the majority of the poor are employed in the informal economy (75%) while the share of informal employment for non-poor households is lower, although still significant (60%). Also, households in rural areas are faced with higher poverty but lower intensity of unemployment than households in urban areas. This situation can be explained taking into account the high incidence of seasonal employment in rural areas (which means nothing more than high levels of underemployment).

Step 6: Political situation and economic policy orientation

Political instability is another important factor contributing to the erratic overall growth performance of the Kyrgyz economy since 1996. But it is not only the ef-

fect of political crisis (e.g. the “Tulip Revolution” in 2005 or the most recent crisis in 2010) on the business cycle which adds to unfavourable macroeconomic framework conditions. Looking at the political framework conditions in Kyrgyzstan over the last 20 years since independence reveals a virulent and risky pattern of political and economic relations in the country which reduces the scope of economic policy action in the future. Right from the early years of independence politicians in Kyrgyzstan deliberately used economic policy as a mean to secure their own wealth and personal interests (e.g. manipulating legal business through the gears of law enforcement, imposing high burden of taxation, direct threatening, barring opposition forces from the access to large businesses, etc.). This misuse of economic policy certainly left its traces on government action. Any successful business in Kyrgyzstan is successful not just because of its competitiveness but because of its ties to the political world.

Due to these political framework conditions economic policy making tends to be mostly ad-hoc and short-term oriented. Factors like an unbalanced state budget with a large deficit and high dependency on foreign assistance, and a general lack of capacities in all – private and public – institutions further undermine comprehensive medium- to long-term oriented economic reform efforts. Furthermore, regular budget deficits limit fiscal interventions leading in particular to a low level of public investment (in infrastructure). The need for fiscal consolidation is evident but reduces the growth prospects, especially if it further undermines the possibilities of the poor and vulnerable population in adapting to external shocks.

Hence, the challenge for Kyrgyz decision makers is to reconcile both aspects in their policy actions: fiscal consolidation and improvement of adaptation possibilities of the poor and vulnerable population. But the close ties between the business and political world, described above, create clear incentives for politicians to be business friendly. For instance labour regulations and other meaningful regulations to overcome market failures and protect the population are weakened and/or not implemented in order to increase profits for private businesses.

Stage B: The labour demand-side: the impact of business and sector development on employment generation

B (7-11)	What prevents firms from demanding more labour? Objectives of steps 7 to 11: <ul style="list-style-type: none"> ■ Getting to know the conditions of business environment in general as well as in more detail for specific sectors ■ Identifying the most relevant constraints for business expansion, which subsequently impedes labour demand and employment generation
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Step 7: General factors influencing the business environment

20 years of deteriorating national service provision culminated in severe problems in energy provision. Constant neglect because of the withdrawal of funds and state subsidies on the one side, and increasing demand for infrastructure services on the other led to service delivery below minimally acceptable levels. An important impediment for trade in Central Asia is the insufficient development and poor condition of infrastructure and trade facilitation. Besides severe financing problems the low quality of infrastructure provision is also caused by weak governance and management in these sectors. Reforms in the energy sector in the past failed to address these governance and management problems adequately. As a consequence, necessary energy tariff increases (tariffs are currently too low for attractiveness and sustainability of investments) could not be implemented, because possible compensations, e.g. in better service provision, were not achieved. High transportation costs and unreliable production and service possibilities mainly due to low-quality electricity provision undermine business expansions and domestic and international market integration. This may lead to serious stability problems e.g. caused by climate change, which usually mainly affects the energy sector.

We observe especially high hindrances in doing business with respect to infrastructure provision (see above), paying taxes and regulations concerning trading across borders. Despite the fact that many reforms regarding the regulatory framework have been initiated in the past, the results

were rather poor. Historical evidence points to systematic implementation and commitment problems of the Kyrgyz government (e.g. softening or even reversing reforms with ad-hoc regulatory provisions in the years following the reform). Therefore, overregulation with respect to permits, licences, inefficient tax administration and the abuse of public authority by inspection remain as challenges. The problem of excessive political interferences in business is especially high and pervasive in tax and customs. As a consequence, even registered enterprises with official licences usually report only part of the production volume.

Because many inputs used for production or retail trade in KR have to be imported, regulatory framework conditions for trading across borders create incentives for operating in the shadow irrespective of being legally registered or not. Simplified tax schemes (like e.g. patent systems) or simplified customs clearance procedures clearly created some visible short-term easing effects on the business side with tax avoidance and lesser exposure to tax inspections and higher tax and customs collection rates on the public finance side. However, with respect to long-term economic development and employment generation, these schemes may prove problematic: unless the business climate for middle sized firms does not improve substantially small firms are more inclined to stay small in order to benefit from these tax and customs “protection walls”.

The relative low and volatile gross domestic savings rate presents a significant obstacle to capital mobilization, leading among others to high real interest rates for lending, expensive collateral-based credit and a very limited long-term financing. Reform efforts lead to an overall improved supply of banking services, making the low deposit mobilization for sustainable credit provision the key issue for the banking system. In view of relative high transfers of remittances the unsatisfactory share of deposits point to additional constraints other than capital accumulation, e.g. an unsatisfactory enforcement of the legal and regulatory framework in the banking sector and deficiencies in banking supervision leading to a low level of trust.

Step 8: Identifying important sectors for employment generation

Though the share of employment in agriculture tends to decrease, the agricultural sector is still a very important factor for employment and income generation. Due to its geographical situation the Kyrgyz Republic is very

dependent on trade. Thus, in addition to agriculture we will have a closer look into the business environment of the trade sector. This business environment indirectly affects also the textile/garment industry, because most of the inputs are imported and the majority of outputs exported. In most of these sectors informally operating enterprises represent the majority of economic actors in KR. Consequently, their business environment conditions will be tackled, too.

Step 9: Further sector specific analysis of labour demand conditions

Step 9a: Agriculture

Though in absolute numbers agriculture used to create most employment, most of these jobs are low wage jobs closer to subsistence of informal wages. Consequently, unless framework conditions are changed it is unlikely that the agricultural sector in Kyrgyzstan continues to reduce poverty significantly.

The basic problem in the agricultural sector is land fragmentation. This means that a prevailing number of small-scale farmers exist in the sector (especially in the south) with no chances of benefitting from economies of scale. Though such scattered businesses might be more labour intensive, the low productivity as well as inhibited possibilities of enterprise growth undermine medium- to long-term development and employment creation. The absence of functioning market institutions are seen to be the most important reason for the problems of farm owners not putting together their land plots in larger, commercially viable farms. Past failures of the Kyrgyz government to adequately address the building of market institutions (e.g. agricultural services and general business development services, framework for cooperatives, complementary institutional reforms in the irrigation sector, access to credit, etc.) are not easy to reverse.

Step 9b: Trade

Kyrgyzstan relies highly on trade development. But exports are dominated by gold mining, which shows lower employment elasticity. Exports of oil-products are in fact re-exports and depend heavily on regional and international (political) developments. Employment relevant exports are mainly informal (especially textile and garments with a relatively high growth factor in the number of jobs) and depend on a special import regime for people.

One of the basic problems of trade relations in Kyrgyzstan is the dual trade policy environment (multilateral and regional) with many non-overlapping and politically conflicting areas. Trade within the region is economically more important than trade with WTO members. Thus, external and internal failures for improving the trade environment in the region impact far more intensive on the economy than changes in WTO framework conditions. Political instability in the region and prevalence of policy makers to resort to ad-hoc policy decisions both have constantly undermined the implementation of regional agreements (e.g. transit agreements). Also, sanctioning mechanisms are weaker in relation to WTO rules, leading to profound enforcement problems of regional and bilateral agreements. In addition, poor border management and high corruption rates distort any formally passed agreements.

The customs union will impact decisively on trade flows and, subsequently, employment generation in KR. The most apparent benefit of an active membership in the Customs Union (CU) to the Kyrgyz economy would be the preservation of petroleum import supplies and prices from other CU members. In view of the stated vulnerabilities of the Kyrgyz economy and regional export problems, this positive impact of the CU is likely to be significant. However, the benefits will rest mostly by formally operating enterprises in the respective export sector. In general, many experts expect a significant loss of transit trade from re-exporting (mostly Chinese) goods to Russia and other CIS countries. This will have a tremendous negative impact on the infrastructure (e.g. bazaars, shuttle traders) currently supporting re-export flows and the respective local employment and income generation. In addition, in the case of bazaars being important suppliers for local productions, e.g. garment industry, the respective industry will not only face higher input prices but also pressures to use legal distribution channels. From a long-term perspective these pressures to more formally operating business structures need not to be bad. However, the adaptation and selection process will leave especially poor, unqualified individual entrepreneurs (like e.g. shuttle traders, but also small informally operating garment enterprises) on its way, thus probably further destabilizing the already problematic employment situation in rural areas (e.g. in the south).

Step 10: Employment prospects in MSMEs (including informal economy)

As mentioned earlier, there is an on-going shift from regular wage employment to self-employment. So, a substantial part of the private sector growth in KR took place via MSME development of predominantly informal nature, with a high share of individual entrepreneurs. Thus, we see the majority of employment creation in the domain of individual enterprises while jobs in SMEs disappear. An increasing concentration of MSMEs in urban areas and a clear north-south divide of MSME distribution in the country are observable. MSMEs contributions to value added are low despite their high numbers mostly in construction, trade, repair and services. With respect to the business environment for MSMEs, a particular problem is access to credit in Kyrgyzstan. In general, high interest rates in combination with high collateral values are important cost drivers in financing, especially limiting the scope of individual and small enterprises as their business scale enables less internal financing opportunities. In addition, electricity and taxes are problematic for businesses not only regarding their de jure regulations, but impose heavy costs already on small businesses.

SME policies of the Kyrgyz government are hampered by implementation problems and too much focus on self-employment rather than on entrepreneurs being able to provide high levels of employment. So far, support and development of business development services in KR is totally left to private sector and donor initiatives. Moreover, lack of reforms in regulatory procedures which are relevant for business development and overall decay in administrative structures even undermined many of the often isolated SME initiatives.

Step 11: Employment in the public sector

With a share of GDP of around 5% the public administration ranges in the same area as e.g. finance and lately construction. Taking into account that the value added of public administration is questionable (costs are usually too high due to lack of competition), the public sector plays only a limited role in economic development and employment generation in KR.

Stage C: The Labour supply side: the qualitative dimension of labour force development²⁴

C (12-14)	<p>What prevents the labour force from offering (in sufficient quantities) the skills in need?</p> <p>Objectives of steps 12 to 14:</p> <ul style="list-style-type: none"> ■ Assessing the problem of skill mismatch ■ Getting to know the extent and quality of the provision of educational services ■ Identifying major challenges in the education system to provide adequately skilled labour supply
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Step 12: Qualification of the labour force

The sectorial employment structure corresponds with employment shares by occupation: skilled agricultural workers represent – though with a falling trend - about one third of total employment in 2006, followed by service and market sales workers (16.3% in 2006 with increasing trend), and craft and related trade workers (16.3%) as the main occupation groups (after ISCO) in the Kyrgyz labour market. Data on the labour force by level of educational attainment (for the year 2006) underpin the structural results of employment shares by occupation: Secondary level (based on levels of ISCED) is dominant (55.1%), followed by primary graduation (23.7%) and tertiary (9.6%). Employment among young people is lower and unemployment respectively higher among age groups up to 24 years. Due to the shortage of jobs, over 41% of all unemployed have no working experience. Graduation in vocational and higher education reduces the risk for unemployment: people with vocational education show unemployment rates below the average as well as those with a completed higher education.

At the same time, an incomplete higher education increases the risk of unemployment. This can be explained

by the demand structures for skilled labour: in 2007 the workers in highest demand are those with higher and secondary educations (22.6%), qualified technical workers (20.4%), equipment operators and engineers (22.3%) and labourers (17.7%). “The need for blue collar professions is two to three times greater than the need for office workers and managers. The result is that young people who prefer to get university degrees instead of entering blue collar professions end up filling the country’s low-paid jobs” (UNDP, 2010, p. 29). As these jobs are to a high degree in the informal economy, they mostly do not offer decent work conditions and possibilities of in-house skills development. Thus, apart from problems in the education system (especially TVET) and inadequate information on career and job opportunities we will address soon, this situation points to a fundamental “white collar syndrome” in KR.

Step 13: The education system in the country

The system of Vocational Education and Training (VET) is to a certain extent of insufficient quality. This deficiency is intensified by limited and outdated market information. The VET system is split into primary (PVE) and secondary (SVE) vocational education and mainly two ministries, the Ministry of Education and Science and the MYLE - share the responsibilities. The horizontal and vertical mobility between and within both segments is limited.

Step 14: Challenges in education

While literacy rates are still close to 100%, the number of uneducated among the younger generations has been increasing in rural areas. In 2010, Kyrgyzstan ranked last in the Program for International Student Assessment rating. Secondary **education** suffers from several problems especially in rural schools, including poor teacher training, low salaries and a shortage of qualified teachers in many disciplines. In general, corruption in secondary schools and universities undermines the quality of education. Private schools and universities in major cities offer better-than-average education and are less affected by corruption. But only the more affluent members of the population can afford private education.

The following **VET system specific constraints** can be stated:

- Lack of private sector commitment and involvement in real practice of Vocational Education and Training

²⁴ The main purpose of the Kyrgyz study was to provide background information for the GIZ programme „Vocational Education & Training and Employment Promotion“. Consequently, the authors concentrated on analysing the system of TVET in the country and identified numerous challenges. However, depending on the research interest and purpose of ELMA, the guidelines can cover a broader range of aspects (e.g. also challenges in general education).

(VET). There is a need to increase the cooperation at least in the development of occupational standards, curricula, accreditation (quality assurance of programmes and institutes), certification processes, boards of vocational schools and provision of internships. A tripartite National Skills Development Council (NSDC) was recently founded to tackle this deficit.

- Underfinanced VET system: education decreased as a share of public expenditure from 23.6% in 2009 to 13.3% in 2011. But VET, being a part of the education budget, is not only severely underfinanced in total but also in comparison to other education sectors.
- Fractioned political responsibilities
- Limited decentralisation in administrative and financial areas of Vocational Schools
- Capacity deficits in TVET system of KR:
 - No systematic pre- and in-service training for VET staff
 - Underdeveloped capacity in the Agency for Vocational Education and Training (AVET) for the management of the 110 Primary Vocational Schools (PVS),
 - Limited capacity in the Ministry for Education and Science's VET department to coordinate and further improve the quality of public and private Secondary Vocational Schools (SVS), as well as to initiate the necessary reforms especially towards demand-driven secondary education/training.
- Corruption erodes quality of training and acceptance of certificates and diploma.

Stage D: Matching demand and supply of labour: the impact of labour market institutions and policies on employment generation

D (15-17)	<p>To what extent do labour market institutions, regulations and policies impact positively on the matching process?</p> <p>Objectives of steps 15 to 17:</p> <ul style="list-style-type: none"> ■ Understanding wage formation as the central coordination mechanism in the labour market by connecting wage/productivity development with major factors influencing wage formation, e.g. labour law and regulations, wage policy, collective bargaining system ■ Assessing the effectiveness and efficiency of labour market and social protection policies: To what extent can active labour market policy address inefficiencies in the matching process? To what extent can passive labour market and – more general – social protection policies safeguard people from poverty and loss of income due to unemployment?
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Step 15: Wages, labour law and regulations, collective bargaining system

The Kyrgyz Republic has developed and formally established a comprehensive system of labour regulations. The Labour Code was amended in 2004 better reflecting the interests of employers. The government then argued that the level of protection for workers was too high, making the economic environment of Kyrgyzstan unattractive for foreign investors. However, with a high share in self-employment and a high percentage of businesses operating fully in the shadow economy regulations for many employment relations are de facto irrelevant – being rigid or not. Even for most businesses in the formal sector, inter-linkages with tax and social contribution systems lead to informal employment relations and erosion of the tax base.

This current de facto irrelevance of labour market regulations might lower the costs for employing workers and, therefore, ease business activities in the short term. But the long term consequences of such a situation do not

only impact negatively on employees by e.g. forcing them into vulnerable employment, low income and exploitation, but also the quality of the matching process (systematic distrust between employer and employee). In a situation with predominantly informal working contracts the chances for workers to improve their skills and qualifications are smaller. Many especially small businesses do not have the means to invest in training on the job (because of insecure market positions, high fluctuations). Even if they invest in qualifying their personnel, they face high risks of creating externalities: other businesses might offer more attractive working conditions for the qualified staff, thus free-riding on in-house qualifications. Insufficient government action in overcoming this problem represents one major reason for lack of qualified personnel. But many businesses in Kyrgyzstan do not seem to recognise the necessity for decisive action in overcoming these problems of collective action, as well.

The dominance of informal employment relations is one of the major reasons why collective bargaining does not play a relevant role in the KR (despite 94% of formally contracted workers belong to trade unions).

With respect to wages, strong real wage growth in between 1999-2010 (on average 8% annually) did not correspond well to productivity growth, being a mere 2 per cent on average during this time. Relative moderate inflation rates during most of the time in combination with rapidly increasing remittance inflows are seen to be key drivers of strong real wage growth. By contrast, wage policies seem not to have influenced wage development. In the light of a limited coverage of collective bargaining the effectiveness of wage policy de facto has to rest on minimum wages as well as more general income policies. Though minimum wage legislation does exist in KR, the guaranteed amount does not provide the means for a decent standard of living. Anyhow, due to severe enforcement problems minimum wages are de facto irrelevant in KR. In view of profound inefficiencies in social protection (e.g. lack of targeting, see step 17) current income policies in Kyrgyz are also not able to systematically address disposable incomes for workers with low levels of education and productivity. Instead, the government turned to the only enforceable instrument of income policy which is left: increases of wages in the public sector and pensions. These actions further detached the growth of productivity from growth of real wages and increased financing pressures to the social protection system.

Step 16: Active labour market policies and institutions

The Kyrgyz Public Employment Services' (PES) functions include mainly job search (for employers and job seekers) and referral of job seekers to Active Labour Market Policies (ALMP) such as training, public works and micro credits. Based on numbers of total expenditures for ALMP the instrument of public works has the biggest share of around 50%. Though around half of all registered job seekers participate in public works programmes (23,000 – 26,000 per year, a regionally comparatively high share), the amount paid out per capita was on average much lower than for micro-credit-schemes and trainings. This fact and an average duration of public works jobs of 2.5 months indicate a rather limited income substitution effect of these programmes.

With respect to the function of PES in job search assistance the following challenges exist:

- The PES in the Kyrgyz Republic is underfinanced. Since 2006 the budget of the PES has not been augmented and amounts with about 100 million Som (about 1.6 million EUR) per annum only to about 50% of the sum that has been asked for by the responsible ministry. With the fiscal budget constantly rising, the share of PES financing in total public expenditures (incl. net lending) went down from an already marginal 0.003% in 2006 to 0.0008% in 2010.
- Performance driven management has so far not come into operation in the PES. ICT tools are used only on a small level for internal communication. Adequate labour information or self-service facilities for jobseekers are rare. There are no call centres for job seekers or employers offering vacancies.
- The PES is improving its cooperation with relevant stakeholders, but due to limited services this is not an easy task. Customer-orientation with quality service delivery based on quantitative and qualitative performance indicators as well as integration of services (one-stop service) is not in practice. Capacity development activities (like staff training, organisational development, modern management systems, etc.) are not offered systematically to the staff. It depends strongly on donors' inputs.
- The so-called case load (average number of registered unemployed per PES staff) is a critical constraint to a successful and efficient work of the PES, because an

individual service is depending on adequate case numbers per counsellor. The ILO recommends a relation of 1:100. If measured by the average number of registered unemployed per PES staff the KR has the highest case load in Central Asia (332) and even in the whole Former Soviet Union (FSU). It is understood that the number of advisors/counsellors is inadequate to the needs of the country's PES.

- The working conditions for PES staff are poor. The fragmented network of employment offices lacks modern ICT technology which resulted in a lower efficiency in work and a deficient system of services, especially because of limited access to labour market information systems (LMIS).

Step 17: Passive labour market and social protection policies and institutions

Income earnings in agriculture (indicated by the possession of a plot of land after the transfer of land from state to peasant farms) functioned as a hurdle to register as unemployed. This, in combination with a constant high share of informal activities, caused a very low coverage of the unemployment benefit scheme (UB) in KR. Since the abolishment of UB in 2006 it even decreased further (e.g. in 2009 only 2% of the registered job seekers were eligible). Other passive labour market policy instruments like subsidies to early retirement are not known in Kyrgyzstan.

All social expenditures per capita decreased in real terms by 2-4 times in 2000 from the 1990 levels and did not reach the level of 1990 until 2009. Today only about half of the working people in Kyrgyzstan pay into the country's health and pension system. A growing number of working people do not contribute to the social system. Causes for such a situation are e.g. a significant number of workers have an income which is too small to afford taxes and contributions. Others are intimidated by the machinery of officialdom which goes hand in hand with a widespread lack of trust in the government about the guarantee/warranty of the future returns of the contributions. Additionally, inadequate information on the procedures may limit payment of contributions to social insurances. Finally to mention, tariffs for social insurance are quite high in comparison to the tax burden, thus leading to strong incentives for businesses to employ off the books in order to avoid paying their share of the necessary social insurance contributions.

With almost 80% of public social protection expenditures in 2009 the pension system is the main social protection tool in the Kyrgyz Republic. It covered 10.6% of the total population. There is a dilemma situation: due to the rising informal economy the contributory base decreased substantially while the proportion of the population over the legal retirement age receiving a pension remained stable. Despite the implementation of the pension reform, the average monthly pension benefit is well below the subsistence minimum.

One important challenge of all income protection measures is inefficiency (e.g. lack of targeting), but the lack of fiscal resources is clearly the most constraining factor for social protection spending. In view of a large share of informal, unrecorded economic activities and high incidences of self-employment, tariff increases in order to compensate for increasing financing needs (e.g. via social insurance contributions, taxes) do not seem to be an option. So cuts in public expenditures and reduction of donor support immediately threaten the already very low level of social protection and political stability in Kyrgyzstan.

The described problems of social protection bear the consequences that politicians in KR can only recur to those instruments over which they still have a certain chance of enforcement: increases of wages in the public sector and increases of pensions (financed by the public budget which indirectly means financed by ODA or external borrowing) are the only ad-hoc available instruments with a certain impact on the income situation of important voters in the population. Despite the rather low level of pensions and public wages they provide important market incomes to the recipients who usually try to heave themselves over the subsistence threshold by non-market agricultural activities, seasonal work, informal trading and remittances. Thus, the pension system is of high relevance in the political arena. Increase of payments (despite its questionable effectiveness and distributive effects) has priority in social policy and, very likely, would be safeguarded from any expected cuts in public expenditures and negotiations regarding donor support.

Stage E: Summary and conclusions

<p>E (18-20)</p>	<p>What are the main challenges to employment creation?</p> <p>What kind of consequences can we draw regarding reform efforts in general and in particular of GIZ programmes, supporting employment promotion?</p> <p>Objectives of steps 18 to 20:</p> <ul style="list-style-type: none"> ■ Getting to know the relative importance of the main constraints to employment generation ■ Based on a participative process defining possible areas and options for government action ■ Proposing options for German development cooperation programmes of how to incorporate the findings of ELMA
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Step 18: Summary of challenges and their relative importance to employment generation

So far, we presented the main arguments of the analysis of the employment and labour market conditions in Kyrgyz Republic. The purpose was to give you an example of how ELMA could look like in practice. However, as this exercise already represents a very condensed version of the original analysis we would like to focus more in the following on the relative importance of stated challenges to employment generation.

Clearly, the initial situation for the development of the Kyrgyz economy is difficult: geographical constraints, small markets, oversupply of labour due to high fertility rates are factors which can be changed not at all or only with a very long-term perspective. In this setting, the most relevant hurdle seems to be the constant lack of labour demand (especially in rural areas). This leads to a dominance of structural or cyclical unemployment.

In principal, the political and social instability of the country accompanied by weak public financial governance and the inability of political decision makers to systematically define and implement integrated medium-term reform strategies pose real hindrances to employment generation in the country.

Mismatch effects due to wrong skills are likely to play a minor part among the bunch of employment problems. There is (still) ample supply of qualified labour force. But in some cases the Kyrgyz labour force is equipped with the wrong skills (mismatch situation) and needs (better) qualification, training and vocational education. This situation applies especially for the formal economy. Because the formal economy is not really up-to-date and small, the demand for especially skilled labour is still limited. This aspect may become more important in the future when, based on higher (public) investment - as indicated in the mid-term governmental program, more modern industrial production and services are demanded. It definitely will be important in the course of the Customs Union. As argued in the analysis, due to changed framework conditions the CU will very likely force many up to now informally operating enterprises to come out of the shadow, invest in order to be internationally competitive and, in due course, expand.

Therefore, in order to meet the growing demand for special skills (blue collar worker), the labour force needs better, more demand-oriented skills qualifications. Though vocational education seems already to be beneficial to its graduates, there is still need of gearing up VET in order to integrate more people (especially young women) in a qualitatively improved and better equipped VET-system, which can address the special needs of e.g. youth and women more effectively.

A market, like the Kyrgyz labour market, constantly in difficulties challenges labour market policies, active and passive likewise. KR's labour legislation seems not to have a relevant impact on job creation. The PES is offering its services since the early 90s of the last century. But the volume and the quality is shrinking more and more. There is a risk that the service will be marginalised and its relevance will get lost. One major reason for this development is that PES in the KR operates in a very complicated environment (demand-deficient labour market, high unemployment rate, etc.). Consequently a large number of (registered) unemployed is competing for a very limited number of jobs. And further, these jobs are low-paid, they are for unskilled labour and accompanied with the usual harmful working conditions. Such jobs are hard to be accepted by the jobseekers. Moreover, the limited quality of the labour market information offered by the PES causes many jobseekers to rely more on personal and family

connections as the main way to find adequate employment. Still, if pro-poor and employment-oriented policy is the focus of governmental development approaches, the public employment service can play a relevant role. But the institutional deficits in capacity and resources of the PES are the most relevant constraints.

Passive labour market policies impacting significantly on employment levels are non-existent. Social protection policies concentrate on pension systems. In the past, this had some positive impact on poverty reduction, but did not improve the income situation of the labour force significantly. Additional social protection instruments (e.g. cash benefits) are not very effective and quite inefficient due to lack of targeting. However, the lack of fiscal resources is currently the most constraining factor for social protection policies.

Step 19: Possible options and approaches for the country to take up the challenges

Overall, the country's fiscal situation in the medium-term is going to remain difficult. Hence, **efficiency-oriented reforms need to be implemented**. This concerns not only reforms in public finance (e.g. tax administration) and measures to improve the effectiveness of monetary policy. Moreover, in view of high risks of volatile remittances and food prices, the possibilities of the poor and **vulnerable population in adapting have to be systematically improved**. Awareness should be build up to **realize the limits of much employed ad-hoc oriented policy measures** in the past like blanket wage and pension increases in order to mitigate the effects of higher food and energy price on vulnerable groups. These measures have very likely distortionary impacts, not to mention the negative effect on fiscal balance (as they are hard to reverse). Consequently, another round of public wage and pension increases would not be advisable. Instead, the Kyrgyz Republic needs to address the institutional shortcomings in the social protection sector on a much higher scale than before.

Due to technical progress and enabling government actions, unfavourable factors like what KR faces need not remain binding. However, if – like in the case of Kyrgyzstan – problematic interactions between the political and economic system over a period of two decades prevail, the chances of overcoming this fundamental problem get smaller. Consequently, when discussing the different

challenges to labour demand inherent in the business environment, one **important cross-cutting issue is to study, first of all, the influence of government action in the past with respect to the constraint and the experience with policy measures**. Second, and likewise important, **recommendations for reforms should address consequently the question, whether the government of Kyrgyzstan will be able and committed** to define and adhere to realistic, specific and operational reform steps.

Low domestic resource mobilization is one of the key challenges to employment generation in KR, because many policy areas lack the needed finances to provide important public services to the population and the economy. Therefore, the distribution of only scarcely available public financial means over the different policy areas should reflect their relative importance in impacting on employment generation. In this respect, we stated that VET basically functions in KR though there are different entry points for increasing the effectiveness and efficiency of VET. These **entry points, presented in detail in the original study and expanded by recommendations for possible interventions for German development cooperation, should be discussed in the political process**.

With respect to improving the matching process in the labour market, we concluded that **labour market policies** currently run a high risk of being marginalized furthermore. Recommendations are given in detail of how to make more use of the scarce public financial means. This means foremost that the **whole cabinet and parliament and not only the relevant ministry should be aware of the problematic current situation**. Also it means stabilizing the labour market institutions by **increasing efforts to provide basic services in combination with better-targeted programmes** addressing the needs of specific groups (e.g. youth).

In the *medium-term (years 2014-2016)* more financial resources are needed for these purposes. Well prepared and targeted **ALMPs** and even broader employment programs will find donors' assistance because they have proven to be relevant for the achievement of the MDGs. But also the **government should put more emphasis on such activities**, especially if the ambitious investment programs (e.g. infrastructure and energy sector) will be implemented. More sophisticated instruments of labour market counselling (activation of job seekers, better profiling of jobseek-

ers, etc.) and modern management techniques as well as labour market prognostic instruments will only be relevant if the basic services are functioning well.

Step 20: Conclusions and consequences for German development cooperation

The study was conducted in the framework of the implementation of the GIZ Programme Vocational Education & Training and Employment Promotion in Kyrgyzstan. Hence, the recommendations for German development cooperation were mainly focussed on vocational education aspects and options for youth initiatives. Especially the recommendation to expand and optimise *training opportunities* and framework conditions in *energy-efficient construction* was taken up by the expert team which conducted the project progress review. It acts as a starting point for further analysis and discussions of a new focus within the GIZ Programme.

Annex B: Overview of the stepwise approach of ELMA

ELMA in five stages	
A (1-6)	What is the basic potential for employment in the country? Objectives of steps 1 to 6: <ul style="list-style-type: none"> ■ Familiarising with basic factors influencing labour demand and labour supply ■ Getting to know degree and intensity of employment problems
B (7-11)	What prevents firms from demanding more labour? Objectives of steps 7 to 11: <ul style="list-style-type: none"> ■ Getting to know the conditions of business environment in general as well as in more detail for specific sectors ■ Identifying the most relevant constraints for business expansion, which subsequently impedes labour demand and employment generation
C (12-14)	What prevents the labour force from offering (in sufficient quantities) the skills in need? Objectives of steps 12 to 14: <ul style="list-style-type: none"> ■ Assessing the problem of skill mismatch ■ Getting to know the extent and quality of the provision of educational services ■ Identifying major challenges in the education system to provide adequately skilled labour supply
D (15-17)	In which way do labour market institutions, regulations and policies impact on the matching process? Objectives of steps 15 to 17: <ul style="list-style-type: none"> ■ Understanding wage formation as the central coordination mechanism in the labour market by connecting wage/productivity development with major factors influencing wage formation, e.g. labour law and regulations, wage policy, collective bargaining system ■ Assessing the effectiveness and efficiency of labour market and social protection policies: To what extent can active labour market policy address inefficiencies in the matching process? To what extent can passive labour market and – more general – social protection policies safeguard people from poverty and loss of income due to unemployment?
E (18-20)	What are the main challenges to employment creation? What kind of consequences can be drawn regarding reform efforts of the respective country in general and in particular of German development cooperation programmes, supporting employment promotion? Objectives of steps 18 to 20: <ul style="list-style-type: none"> ■ Getting to know the relative importance of the main constraints to employment generation identified before ■ Based on a participative process defining possible areas and options for government action ■ Proposing options for German development cooperation programmes of how to incorporate the findings of ELMA

Steps	Labour Supply	Matching in the Labour Market	Labour Demand
A (1-6)	<p>What is the basic potential for employment in the country?</p> <p>Objectives of steps 1 to 6:</p> <ul style="list-style-type: none"> ■ Familiarising with basic factors influencing labour demand and labour supply ■ Getting to know degree and intensity of employment problems 		
<p><i>Orientation: We start ELMA with checking for the basic conditions for growth, because a growth potential is a necessary precondition for labour demand and subsequently employment.</i></p>			
1	Geographical situation		
2	Patterns of economic development in the past		
<p><i>Orientation: In order to realize as much employment as possible the demand for labour should correspond in terms of numbers, but also in terms of skills and qualifications to the supply of labour. The identified growth patterns can be used as a first rough indicator for quantitative aspects of labour demand. We will focus on quantitative aspects of employment also in the following steps 3 and 4 by looking into demographic structure and labour migration. Both factors shape labour supply: demographic structure indicates an increase or decrease of the working age population in need of jobs; the extent of labour migration represents an indicator for excess labour supply generally reducing (or increasing) the labour force.</i></p>			
3	Demographic structure		
4	Labour migration		
<p><i>Orientation: After having identified possible basic constraints to productive employment on the demand and supply side of the labour market we turn to the performance of the labour market in general, pinning down (among others) the dimensions of employment problems.</i></p>			
5	Labour market trends		
<p><i>Orientation: Many developing countries face development constraints (e.g. locational, geographical, resource endowments, climate change) which more or less have to be taken as given. But this does not necessarily mean that the country is doomed to fail in generating employment and income. In this case special responsibility is borne by the public sector and the way the government carries out its function. The quality of public actions might compensate for unfavourable initial conditions for employment creation. Therefore, we complement our first round of diagnostic with analysing the basic situation regarding this role of the public sector.</i></p>			
6	<p>Public Sector as a cross-cutting issue:</p> <p>Political situation and economic policy orientation</p>		

Steps	Labour Supply	Matching in the Labour Market	Labour Demand
B (7-11)	What prevents firms from demanding more labour? Objectives of steps 7 to 11: <ul style="list-style-type: none"> ■ Getting to know the conditions of business environment in general as well as in more detail for specific sectors ■ Identifying the most relevant constraints for business expansion, which subsequently impedes labour demand and employment generation 		
7			Business environment in general Infrastructure conditions and policy Regulatory framework for businesses Financial market conditions and policy
			<p>Orientation: Based on this first inventory of challenges to business expansion and subsequently employment generation we look at the business environment and the respective sectorial policies in specific sectors.</p> <p>The first step of this specific sector analysis is to explain your choice of sectors by referring to their relevance for employment generation (step 8).</p>
8			Explaining the choice of sectors, which need to be analysed in more detail regarding their business environment
			<p>Orientation: After checking for challenges in the business environment in the selected sectors, the conditions for MSMEs (including informal economy) and in the public sectors should be scrutinized. This step is advisable because labour demand in both sectors usually exerts influence on the formal and informal labour market. Therefore, you should state to what extent and in what way this is the case in the actual country.</p>
9			Sector specific analysis of labour demand conditions
10			Employment prospects in MSMEs (including informal economy)
11			Employment in the public sector

Steps	Labour Supply	Matching in the Labour Market	Labour Demand
C	What prevents the labour force from offering (in sufficient quantities) the skills in need?		
(12-14)	Objectives of steps 12 to 14:		
	<ul style="list-style-type: none"> ■ Assessing the problem of skill mismatch ■ Getting to know the extent and quality of the provision of educational services ■ Identifying major challenges in the education system to provide adequately skilled labour supply 		
	<i>Orientation: The first step of stage C (supply-side analysis of labour) is to try to assess to what extent skill mismatch is indeed an issue in the actual country.</i>		
12	Qualification of the labour force		
	<i>Orientation: Principally, a mismatch of skills can be the result of problems (a) in the education system, and/or (b) inefficiencies of the matching process in the labour market. The latter refers, for example, to the role of Public Employment Services in providing job counselling services which might not be very effective. We will deal with such possible constraints in the matching process of the labour market in stage D. For the remainder of this stage we focus on the outcomes and conditions of the education system.</i>		
13	Describing the education system		
14	Challenges in education and training with special focus on TVET		

Steps	Labour Supply	Matching in the Labour Market	Labour Demand
D (15-17)	<p>To what extent do labour market institutions, regulations and policies impact positively on the matching process?</p> <p>Objectives of steps 15 to 17:</p> <ul style="list-style-type: none"> ■ Understanding wage formation as the central coordination mechanism in the labour market by connecting wage/productivity development with major factors influencing wage formation, e.g. labour law and regulations, wage policy, collective bargaining system ■ Assessing the effectiveness and efficiency of labour market and social protection policies: To what extent can active labour market policy address inefficiencies in the matching process? To what extent can passive labour market and – more general – social protection policies safeguard people from poverty and loss of income due to unemployment? 		
15	Wages, labour law and regulations, collective bargaining system		
16	The role of active labour market policies and institutions		
17	The role of passive labour market and social protection policies and institutions		

Steps	Labour Supply	Matching in the Labour Market	Labour Demand
E (18-20)	<p>What are the main challenges to employment creation?</p> <p>What kind of consequences can be drawn regarding reform efforts of the respective country in general and in particular of German development cooperation programmes, supporting employment promotion?</p> <p>Objectives of steps 18 to 20:</p> <ul style="list-style-type: none"> ■ Getting to know the relative importance of the main constraints to employment generation ■ Based on a participative process defining possible areas and options for government action ■ Proposing options for of German development cooperation programmes of how to incorporate the findings of ELMA 		
18	Summary of challenges and their relative importance to employment generation		
19	Possible options and approaches for reforms to take up the challenges		
20	Conclusions and consequences for German development cooperation		

Glossary

Activity rate¹	is the ratio between labour force and working-age population (= labour force/population of working age).
Actual dependency ratio ¹	can be calculated as (total population – the labour force) / labour force. This indicator is used to describe demographic structures and assess their pressures on the labour market to create jobs (see also age-based dependency ratio).
Age-based dependency ratio ¹	is defined as the total population in the inactive age-groups (typically under 15 and over 65 years) divided by the total working-age population, typically 15-64 years old. This indicator is used to describe demographic structures and assess their pressures on the labour market to create jobs (see also actual dependency ratio).
Average monthly wages ³	<p>The statistical series in KILM 15 show gross nominal wages, which represent the total due to workers before deductions are made for their contributions to health insurance, unemployment, pension and other schemes, as well as for personal income taxes.</p> <p>Wages are important from the workers point of view and represent a measure of the level and trend of their purchasing power and an approximation of their standard of living. This indicator complements information regarding the average compensations costs incurred by employers (see employers' average compensation costs for the employment of workers, KILM 16).</p>
Bilateral labour migration agreements ¹⁵	An agreement between two countries specifying the requirements in order to follow recruitment and employment rules of legally employed foreign workers. By contrast, in unilateral labour migration programs only migrant-receiving governments establish rules that employers must follow in order to receive permission to have legal foreign workers admitted. After receiving government approval to hire foreign workers some countries allow employers to recruit migrants anywhere, subject only to sending-country rules, others refer to bilateral labour migration agreements.
Deficit of productive employment ¹	consists of those who are in the labour force but do not have productive employment. It encompasses two categories: the working poor and the unemployed.
Discouraged workers ³	are persons not currently in the labour market who want to work but do not actively “seek” work because they think they will not find any (e.g. they view job opportunities as limited, or they do not seek work because they have restricted labour mobility, or face discrimination, or structural, social or cultural barriers (also called the “hidden unemployed”). Discouraged workers are a subgroup of the inactive labour force. Regardless of their reasons for being discouraged these potential workers are generally considered underutilized. The presence of discouraged workers is implied if the measured labour force grows when unemployment is rising (although demographic pressures should also be taken into consideration). People who were not counted as unemployed (because they were not actively searching for work) may change their mind and look for work when the odds of finding a job improve.

Domestic credit to private sector ¹⁰	refers to financial resources provided for the private sector, such as loans, purchases of non-equity securities, and trade credits and other accounts receivable, that establish a claim for repayment. For some countries these claims include credit to public enterprises.
Domestic savings rate	share of domestic savings as a percentage of GDP
Economically active population ¹	all persons of either sex who furnish the supply of labour for the production of goods and services during a specified time-reference period (see also working-age population)
Employed ¹	all persons above a specific age who during a specified brief period, either one week or one day, were either in paid employment or self-employment, employers, own account workers, or unpaid family workers
Employers' average compensation costs for the employment of workers ³	KILM 16 presents both the level and structure of compensations costs, with distinction made between total hourly direct pay and hourly social insurance expenditures and labour-related taxes. Assessing the change in labour costs over time can play a central role in wage negotiations and in implementing and assessing employment, wages and other social policies. Information on labour cost per unit of labour input (that is, per time unit) is particularly useful in the analysis of certain industrial problems, as well as in the field of international economic cooperation and international trade. This indicator provides an estimate of employers' expenditure toward the employment of its workforce. This indicator is complementary to the average monthly wage indicator, because both wage indicators reflect the two main facets of existing wage measures; one aiming to measure the income of employees (see average monthly wages), the other showing the costs incurred by employers for employing them.
Employment by sector ³	This indicator disaggregates employment into three broad sectors – agriculture, industry and services – and expresses each as a percentage of total employment. The indicator shows employment growth and decline on a broad sectorial scale, while highlighting differences in trends and levels between developed and developing economies. Sectorial employment flows are an important factor in the analysis of productivity trends, because within-sector productivity growth needs to be distinguished from growth resulting from shifts from lower to higher productivity sectors.
Employment-to-population ratio ³	is defined as the proportion of a country's working-age population that is employed (the youth employment-to-population ratio is the proportion of the youth population – typically defined as persons 15 to 24 years – that is employed). A high ratio means that a large proportion of a country's population is employed, while a low ratio means that a large share of the population is not involved directly in market-related activities, because they are either unemployed or out of the labour force altogether.

Foreign direct investment (FDI)	<p>An investment made by a company or entity based in one country into a company or entity based in another country. Foreign direct investments differ substantially from indirect investments such as portfolio flows, when overseas institutions invest in equities listed on a nation's stock exchange. Entities making direct investments typically have a significant degree of influence and control over the company into which the investment is made. Open economies with skilled workforces and good growth prospects tend to attract larger amounts of foreign direct investment than closed, highly regulated economies.</p>
Gazelles⁵	<p>are – unlike the majority of SMEs – fast growing businesses (sustained annual growth rate of 20% over a three to four year time period) with high employment creation (positive net new jobs).</p>
Gross Capital Formation rate¹⁴	<p>(formerly gross domestic investment) consists of outlays on additions to the fixed assets of the economy plus net changes in the level of inventories. Fixed assets include land improvements (fences, ditches, drains, and so on); plant, machinery, and equipment purchases; and the construction of roads, railways, and the like, including schools, offices, hospitals, private residential dwellings, and commercial and industrial buildings. Inventories are stocks of goods held by firms to meet temporary or unexpected fluctuations in production or sales, and incomplete goods. According to the 1993 SNA, net acquisitions of valuables are also considered capital formation.</p>
Gross Domestic Product (GDP)	<p>is the market value of all officially recognized final goods and services produced within a country in a given period of time (usually calendar year). This indicator is a very broad, macroeconomic measure for how well the economy is performing. Frequent, regular and quite consistent measuring of GDP in practically all countries of the world allows comparing economic performances as well as – together with other indicators – the nexus between economic growth and e.g. poverty reduction or labour force developments.</p> <p>Real GDP measures the total income of everyone in the economy (adjusted for the level of prices).</p> <p>GDP per capita is calculated as GDP divided by the average (or mid-year) population of the same reference period as GDP. It is a measure of the average income in an economy.</p> <p>GDP indicators are often used as a measurement for the standard of living. However, GDP has its limitations in measuring living standards:</p> <ul style="list-style-type: none">■ it does not inform about the distribution of wealth within a country;■ does not differentiate between economic output that actually benefits the population and economic bads in a country;■ does not reflect non-market activities such as unpaid housework.■ Increasing GDP does not necessarily correspond with increasing employment: due to technological advances requiring less employment, the employment ratio may actually decrease.

Human Development Index (HDI) ⁴	is a composite index developed by UN which tries to measure human development more adequately than GDP per capita alone. It measures the average achievements in a country in three basic dimensions of human development: a long and healthy life, access to knowledge and a decent standard of living. Four indicators underpin these dimensions: life expectancy at birth (health), mean years of schooling and expected years of schooling (education), and gross national income per capita (standard of living). Data availability determines HDI country coverage. A Human Development Index (HDI) adjusted for inequality in distribution of each dimension across the population, a gender inequality index, and a multidimensional poverty index are provided by the Human Development Report Team, as well.
Inactive people ³	Individuals are considered to be inactive if they are neither employed nor unemployed, that is, not actively seeking work. Inactive people are, by definition, outside of the labour force. There are a variety of reasons why some individuals do not participate in the labour force; such persons may be occupied in caring for family members; they may be retired, sick or disabled or attending school; they may believe no jobs are available; or they may simply not want to work.
Inactivity rate ³	is defined as the percentage of the population that is neither working nor seeking work (that is, not in the labour force). When added together, the inactivity rate and the labour force participation rate will add up to 100 per cent.
Income distribution ¹⁶	The Gini index is a convenient summary measure of the degree of inequality based on either income or expenditure. It measures the inequality among values of a frequency distribution (for example levels of income). A Gini coefficient of zero expresses perfect equality, where all values are the same (for example, where everyone has an exactly equal income). A Gini coefficient of one (100 on the percentile scale) expresses maximal inequality among values (where only one person has all the income)
Informal economy ¹	forms part of the market economy. It covers informal employment both in informal enterprises (small unregistered or unincorporated enterprises), and outside informal enterprises. Informal entrepreneurs and workers share one important characteristic: they are not recognized or protected under existing legal and regulatory frameworks. The informal economy does not include the criminal economy and the reproductive or care economy.
Informal employment ¹	includes all remunerative work, i.e. both self-employment and wage employment, that is not registered, regulated or protected by existing legal or regulatory frameworks, as well as non-remunerative work undertaken in an income producing enterprise. Informal workers do not have secure employment contracts, worker's benefits, social protection or workers' representation.
Interest rate spread ⁹	is the interest rate charged by banks on loans to prime customers minus the interest rate paid by commercial or similar banks for demand, time, or savings deposits.

Labour force³

is the sum of the number of persons employed and the number of unemployed. The fact, that the unemployed are part of the labour force needs to be stressed, because the terms “labour force” and “employment” are sometimes mistakenly used interchangeably.

Labour force participation rate³

is calculated by expressing the number of persons in the labour force as a percentage of the working-age population.

The indicator for labour force participation rate plays a central role in the study of the factors that determine the size and composition of a country’s human resources and in making projections of the future supply of labour. The information is also used to formulate employment policies, to determine training needs and to calculate the expected working lives of the male and female populations and the rates of accession to and retirement from economic activity – crucial information for the financial planning of social security systems.

The indicator is also used for understanding the labour market behaviour of different categories of the population. According to one theory, the level and pattern of labour force participation depend on employment opportunities and the demand for income, which may differ from one category of persons to another. For example, studies have shown that the labour force participation rates of women vary systematically, at any given age, with their marital status and level of education. There are also important differences in the participation rates of the urban and rural populations, and among different socio-economic groups.

Malnutrition, disability and chronic sickness can affect the capacity to work and are therefore also considered as major determinants of labour force participation, particularly in low-income environments. Another aspect closely studied by demographers is the relationship between fertility and female labour force participation. This relationship is used to predict the evolution of fertility rates, from the current pattern of female participation in economic activity.

It is related by definitions to other indicators as the employment-to-population ratio which is equal to the labour force participation rate after the deduction of unemployment from the numerator of the rate.

Labour productivity³

Labour productivity is defined as output per unit of labour input. Two measures are used e.g. in ILO KILM, GDP per person engaged and GDP per hour worked. Labour productivity is a key measure of economic performance, because economic growth in a country or sector can be ascribed either to increased employment or to more effective work by those who are employed. The latter can be described through data on labour productivity. An understanding of the driving forces behind it, in particular the accumulation of machinery and equipment, improvements in organization as well as physical and institutional infrastructures, improved health and skills of workers (“human capital”) and the generation of new technology, is important in formulating policies to support economic growth.

Micro, Small, and Medium Enterprises (MSME)	No universal definition; the choice of MSME definition could depend on many factors, such as business culture; the size of the country's population; industry; and the level of international economic integration. However, usually a combination of different characteristics are used, e.g. number of employees, annual turnover, investment level, etc.. Common basis for definition is employment with variation in defining the upper and lower size limit. Despite this variance a large number of sources define an MSME to have a cut-off range of 0-250 employees.
NEET	Part of the working age population which is not in employment, education or training. NEET encompasses the unemployed, discouraged and/or inactive persons.
Non-performing loans ¹³	Bank nonperforming loans to total gross loans are the value of nonperforming loans divided by the total value of the loan portfolio (including nonperforming loans before the deduction of specific loan-loss provisions). The loan amount recorded as nonperforming should be the gross value of the loan as recorded on the balance sheet, not just the amount that is overdue.
Official development assistance (ODA) ⁷	Grants or loans to countries and territories on the DAC List of ODA Recipients (developing countries) and to multilateral agencies which are: (a) undertaken by the official sector; (b) with promotion of economic development and welfare as the main objective; (c) at concessional financial terms (if a loan, having a grant element of at least 25 per cent). In addition to financial flows, technical co-operation is included in aid. Grants, loans and credits for military purposes are excluded. Transfer payments to private individuals (e.g. pensions, reparations or insurance pay-outs) are in general not counted.
Overall outstanding loans ¹²	is the nominal amounts of outstanding loans inclusive of accrued interest. Loans outstanding can be used to see what percent of the total is delinquent and how much.
Paid employment jobs ²	are those jobs where the incumbents hold explicit (written or oral) employment contracts which give them a basic remuneration. This is not directly dependent upon the revenue of the enterprise for which they work. Persons in these jobs are typically remunerated by wages and salaries, but may be paid by commission from sales, by piece-rates, bonuses or in-kind payments. Often also referred to as "wage and salaried workers".
Poverty ³	Poverty can result when individuals are unable to generate sufficient income from their labour to maintain a minimum standard of living. The extent of poverty, therefore, can be viewed as an outcome of the functioning of labour markets. An estimate of the number of people in poverty in a country depends on the choice of the poverty threshold. However, what constitutes such a threshold of minimum basic needs is subjective, varying with culture and national priorities. Definitional variations create difficulties when it comes to making international comparisons. Therefore, in addition to national poverty measurements the ILO KILM indicator presents data relative to the World Bank international poverty lines of US\$1.25 and US\$2 per person per day.

Productive employment ¹	Encompasses those who are in the labour force and who are neither unemployed nor working poor. Hence, the concept of productive employment stands for employed persons, whose income is sufficient to permit them and their dependants a level of consumption above the poverty line.
Qualitative analysis	is defined in the present context as a structured report of observer impressions concerning the underlying reasons for the country-specific employment situation.
Real lending rate ⁸	or “real interest rate”; is the lending interest rate adjusted for inflation as measured by the GDP deflator.
Self-employment jobs ²	are those jobs where the remuneration is directly dependent upon the profits (or the potential for profits) derived from the goods or services produced (where own consumption is considered to be part of the profits). The incumbents make the operational decisions affecting the enterprises, or delegate such decision while retaining responsibility. (In this context “enterprise” includes one-person operations.)
Share of long-term financing ¹¹	credit with original contractual maturity longer than one year (or five years) divided by total credit
Technical and Vocational Education and Training (TVET) ⁶	a comprehensive term referring to those aspects of the educational process involving, in addition to general education, the study of technologies and related sciences, and the acquisition of practical skills, attitudes, understanding and knowledge relating to occupations in various sectors of economic and social life.
Total employed according to their status of employment ³	Indicators of status in employment distinguish between four important and useful categories of the employed – (a) wage and salaried workers, (b) employers, (c) own-account workers, and (d) contributing family workers. Categorization by employment status can help in understanding both the dynamics of the labour market and the level of development of countries. Over the years, and with growth of the country, one would typically expect to see a shift in employment from the agriculture to the industry and services sectors with a corresponding increase in wage and salaried workers and decreases in self-employed and contributing family workers previously employed in the agricultural sector.
Underemployment ¹	is underutilization or inefficient use of a worker’s skills, qualifications or experience, or where the worker is unable to work as many hours as he or she is willing to do.
Unemployed ¹	all persons above a specified age who during the reference period were “without work”, i.e. not in paid employment or self-employment, “currently available for work”, i.e. available for paid employment or self-employment during the reference period and “seeking work”, i.e. have taken specific steps in a specified reference period to seek paid employment or self-employment.

Unemployment rate³

is calculated by taking the unemployed (equals the number of persons, which are during a specified reference period without work, but currently available for work and seeking work) as a percentage of the total labour force, which itself is the sum of the total persons employed and unemployed in the group. It should be emphasized that it is the labour force or the economically active portion of the population that serves as the base for this statistic, not the total population. This distinction is not necessarily well understood by the public. Indeed, the terms “labour force” and “employment” are sometimes mistakenly used interchangeably.

The overall unemployment rate for a country is a widely used measure of its unutilized labour supply. If employment is taken as the desired situation for people in the economically active population (the labour force), unemployment becomes the undesirable situation. Still, some short-term unemployment can be both desirable and necessary for ensuring adjustment to economic fluctuations. Unemployment rates by specific groups, defined by age, sex, occupation or industry, are also useful in identifying groups of workers and sectors most vulnerable to joblessness.

The unemployment rate simply tells us the proportion of the labour force that does not have a job but is available and actively looking for work. However, this indicator says nothing about the economic resources of unemployed workers or their family members. Its use should therefore be limited to serving as a measurement of the utilization of labour and an indication of the failure to find work. Other measures, including income-related indicators, would be needed to evaluate economic hardship.

That is why, paradoxically, low unemployment rates may well disguise substantial poverty in a country, whereas high unemployment rates can occur in countries with significant economic development and low incidence of poverty. These results occur because of well-developed social protection schemes and/or available savings or other means of support which enable workers to better afford to take the time to find more desirable jobs.

A useful purpose served by the unemployment rate in a country, when available on at least an annual basis, is the tracking of business cycles. When the rate is high, the country might be in recession, economic conditions might be bad, or the country might somehow be unable to provide jobs for the available workers. The goal then is to introduce policies and measures to bring the incidence of unemployment down to a more acceptable level. What that level is, or should be, has often been the source of considerable discussion, as many consider that there is a point below which an unemployment rate cannot fall without the occurrence of intense inflationary pressures. Because of this supposed trade-off the unemployment rate is closely tracked over time.

Vulnerable employment¹

is defined by labour market status and includes those who are working on their own account or as contributing family workers (unpaid family workers).

Working age population ^{3,1}	is the population above a certain age – often aged 15 and older – prescribed for the measurement of economic characteristics (see also economically active population). Typically the working-age population is defined between 15 and 65 years old.
Working poor ¹	employed persons, whether for wages, on their own account or as unpaid family helpers, whose income is insufficient to bring themselves and their dependents out of poverty. Simplified method to obtain an approximate number of working poor (see ILO (2012a), p. 41): Working poor = total employed population aged 15+ multiplied by headcount poverty rate
Youth	Young people aged between 15 and 24, part of the labour force.
Youth unemployment ³	According to ILO data on youth unemployment could be presented in the following ways: (a) the youth unemployment rate; (b) the youth unemployment rate as a percentage of the adult unemployment rate; (c) the youth share in total unemployment; and (d) youth unemployment as a proportion of the youth population. These measures should be analysed together; any of the four, when analysed in isolation, could paint a distorted image. For example a country might have a high ratio of youth-to-adult unemployment but a low youth share in total unemployment. The presentation of youth unemployment as a proportion of the youth population recognizes the fact that a large proportion of young people enter unemployment from outside the labour force.

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