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International Growth Centre and Bank of Uganda Public Lecture

Falling Oil Prices and a Rebased Economy: Implications for Growth and Unemployment in Uganda

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My questions and focus

- What have we learned about ‘poverty reduction’, and how it can be accelerated?
- How does this “generic” model apply to Uganda?
- What can and should we do?

What have we learned about successful poverty reduction?

- Lots of recent success e.g. in Asia but also Latin America and some African countries.
 - Extreme poverty in world has dropped from 36% to 14.5% between 1990 and 2011
- Three ingredients – without a clear recipe on how to achieve them:
 - A growth process that succeeds in being inclusive of poorer groups via labour absorption into better, higher productivity jobs and activities
 - Functioning social sector systems, delivering basic health, education, security
 - Forms of basic protection for the poorest
- Even if unclear about recipe, the necessary utensils to cook the dish:
 - An effective state, functioning in way that allows economic growth and foster social sector systems
 - A politics in which leaders and elites are committed to growth and poverty reduction

Theory of growth and inclusion

- Growth theory and empirics: focus on misallocation within and across sectors (Klenow, Hsieh)
 - Growth as reallocation as moving from less productive to more productive activities within and across sectors;
- In development, consistent with long-standing thinking on existence of dual economy
 - with less productive sector (agriculture) and more productive (urban, manufacturing sector) e.g. as in Lewis (and modern versions e.g. Gollin (2014)).
- If more reallocation of (low skilled) *labour*, the faster poverty reduction (e.g. Eswaran and Kotwal, 1991) (as the poor “have but their labour to sell” (Marx)).
- (Probably) broadly consistent with East-Asian experience:
 - growth in urban, manufacturing, absorbing labour from informal and rural sectors.
 - Fast poverty reduction driven via expanding job opportunities.
- Note prediction (Lewis): not necessarily fast reduction of poverty in urban areas (not clear what happens to real wages), but definitely reduction of rural poverty in process
 - Consistent with e.g. China evidence or more recently Bangladesh

Some other implications

- Role of growth and labour market
 - Best policies probably not about labour market itself (Fields, WDR 2012). Job need to be offered by the economy. Labour market policies cannot create these.
 - Labour demand (by firms in more productive activities) is the main constraint – not labour supply characteristics
- Role of human capital of the poor (and therefore social sectors)
 - In the poorest settings, definitely provides means for poor people to be more included in growth process, but less clear that it will drive growth or drive job creation.
 - In both: social sector outcomes have value in themselves (not just for incomes)
 - But in themselves usually not enough to create the opportunities

Role of agriculture? Growth lens

- Long-standing view: in poor settings, growth must start with agriculture
 - Especially smallholder agriculture (small is beautiful), view largely peddled by agricultural economists (see also WDR2010)
 - Not quite consistent with evidence (many countries did not start their growth spurts in agriculture!) and with modern growth theory and reallocation, with agriculture low productivity sector (Gollin, 2014)
- Lens of modern growth theory meets structural transformation:
 - Development will involve reduced share of agriculture, as a low productivity sector, losing out to urban and even manufacturing.
 - Also within agriculture scope to reallocate to more productive activities (commercial, export, high value crops) (Udry, 2012)
 - No obvious, policy-relevant prediction on primacy of (very) small scale (Dercon, 2010; Gollin 2015)
- BUT: Agriculture has key role in growth – fuelling and feeding growth,
 - but what happens elsewhere IS crucially important for agriculture (demand linkages, e.g. Eswaran and Kotwal, 1993)

Role of agriculture? The poverty reduction lens

- A focus on agriculture and smallholder can be driven by concern for the poor (even if not necessarily best for growth)
 - As Agriculture by far largest employer of the poor
 - As Smallholders uses labour intensively
- The faster labour reallocation can be achieved, the better for poverty reduction.
 - big role for rural-urban linkages (also for cost of food for those leaving agriculture determining real wages)
 - Migration will be correlate of success, so valuable to invest in rural areas in transferable skills
- But note of warning: reallocation and transformation will be slow and messy process
 - Reallocation process will be slow – so in poorest countries, there will be huge numbers of peasants for a long time to come, probably requiring support
 - Observing migration may nevertheless also be sign of failure, leading people to migrate to cities in search of support and better basic services

Summary: ingredients for success

- (1) Strong growth as reallocation towards more productive sectors;
- (2) Necessary condition: sufficiently strong state capabilities and political commitment of elites to make this work.
- (3) More high productivity jobs as a key driver for poverty reduction (so the faster growth processes reallocates more labour into more productive activities, the better);
- (4) Social sector and human capital policies that facilitate inclusion while recognising that labour demand (not labour supply) will drive poverty reduction
- (5) (Smallholder) agriculture unlikely to be main driver of growth but has a key role in supporting growth and poverty reduction; successful reallocation will often be out of agriculture into high productivity urban sectors such as manufacturing, and take time.

Examples from the world

- (1) Growth as reallocation
- (2) State capabilities and political commitment
- (3) More high productivity jobs as a key driver for poverty reduction
- (4) Social sector and human capital policies that facilitate inclusion
- (5) (Smallholder) agriculture unlikely to be main driver of growth but has a key role in supporting growth and poverty reduction

Examples: China, Vietnam, India, Bangladesh, Ghana, Rwanda, Ethiopia

Challenges: Nigeria, DR Congo,

Few (? Botswana, Australia, Peru?) have managed to handle natural resource booms well.

Applying to Uganda? Oil

- Incentives to tradable goods sector
 - Incentives to governance and politics
 - Incentives to get distracted...
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- Oil price consequences?
 - Value proposition
 - Incentives to delay
 - Opportunity to go for a more cautious and effective rebalancing of governance and economy to cope with oil.

Uganda: preparing for oil

(1) Growth as reallocation

- Build the productive, tradable sector further, no least (regional) exports
- Think about the linkages to the oil sector more carefully

(2) State capabilities and political commitment

- too early to be totally distracted
- Work more on accountability
- Sustain political commitment to inclusive growth

(3) More high productivity jobs as a key driver for poverty reduction

- Urbanisation as centre of productive activities (not consumption cities)

(4) Social sector and human capital policies that facilitate inclusion

- a social contract for sharing resources

(5) (Smallholder) agriculture unlikely to be main driver of growth but has a key role in supporting growth and poverty reduction

- Build the productive capabilities in agriculture
- Work on tradable aspects: value addition, processing, driven by demand (urban, export)

Uganda in coming decade?

- Preparing for oil – take the time to do so
- Transforming the economy and political governance to be resilient to oil shock, and use it as an opportunity for a more investor friendly and accountable state
- Strong focus on export and tradable goods capabilities
- Linkages to oil (and other) natural resources, building on upgrading existing capabilities
- Social contract, committed to productive cities and to inclusion via jobs, social sector provision and social protection
- Special attention to the North, still waiting for its full peace dividend.