CONFERENCE DOCUMENTATION

Employment and Development

What Do We Know and What Can We Do?

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Keynote Lecture by Professor Dani Rodrik

“Employment, Structural Change and Economic Development”

Summary

Dani Rodrik is the Rafiq Hairiri Professor of International Political Economy at the John F. Kennedy School of Government at Harvard University. He has published widely in the areas of international economics, economic development, and political economy. Some of his articles have been published in the top journals of the field including the American Economic Review, the Quarterly Journal of Economics and the Journal of Political Economy. More recently, Mr. Rodrik has become famous among researchers and policy makers alike for his Growth Diagnostics Approach and his blog on ‘Unconventional thoughts on economic development and globalisation’.

Professor Rodrik started his talk by making the point that labour is the most abundant resource in developing countries. While capital as a production factor is scarce in this context, most developing countries are characterised by a substantial part of the population being unemployed or at least underemployed. The key to development therefore is to put those workers into productive jobs.

According to Professor Rodrik, creating employment in the productive parts of the economy is fundamental for achieving sustainable growth in the developing world. This process of successful structural change occurs already in some parts of the developing world but not in others. In particular, Asian countries have been very successful over the last four decades in increasing productivity levels in many sectors of their economy while at the same time creating many new jobs in these sectors. Therefore, productivity growth went hand in hand with employment creation.

However, as Rodrik pointed out, structural change and sector-specific productivity growth is not an automatic escalator up to higher economy-wide growth levels. In Africa and Latin America, despite their relatively high growth rates over the last two decades, productivity growth, especially in the manufacturing sector, has led to massive employment destruction in these parts of the economy. Although productivity levels in manufacturing have increased in Africa and Latin America over this period, average economy-wide labour productivity levels have decreased due to a large number of laid off workers from manufacturing who could only find jobs in low-productivity jobs.

In the subsequent part of his talk Rodrik singled out some of the conditions that contribute to successful structural change. In principle, the objective is to exploit the productivity differences across sectors in the early and medium phases of the development process by shifting employment from low-productivity sectors to high-productivity sectors of the economy. Thus, under certain circumstances it is more important from a policy perspective to focus on shifting employment patterns across sectors than on productivity growth within each sector as a means of achieving higher economic growth.

Based on his recent empirical research using new industry and employment data for a larger group of developing countries Professor Rodrik highlighted three factors that contribute to successful structural change.

First of all, a country’s wealth of natural resources seems to have a negative effect on successful structural change. Rodrik explained that although some primary sectors such as minerals do operate at very high levels of labour productivity they have a very limited capacity to generate substantial employment. In addition, a rich wealth of natural resources reinforces traditional specialisation patterns and seems to reduce the incentive to diversify into, for instance, modern manufacturing where more employment can be created.

A second related issue concerns the real exchange rate. Countries in Latin America and Africa have typically liberalised in the context of overvalued currencies – driven either by disinflationary monetary policies or by large foreign aid inflows. Overvaluation squeezes industries in the tradable sector of the economy more, especially damaging the more modern ones in manufacturing that operate at tight profit margins. Asian countries, by contrast, have often targeted competitive real exchange rates with the express purpose of promoting their tradable industries.

Third, countries with rigid labour markets seem to show a much slower rate of successful structural change. The reasoning behind this observation seems to be that inter-sectoral reallocation into and within manufacturing industries is slowed down by entry barriers. When employment conditions are perceived as rigid, say because of firing costs that are too high, firms are likely to respond to new opportunities by upgrading plant and equipment (capital deepening) rather than by hiring new workers. This slows down the transition of workers to modern economic activities.

Professor Rodrik concluded his talk with an optimistic outlook on the development prospects for many poor countries. Since 1990, and for the first time since independence, many countries in Africa, Asia and Latin America have achieved higher growth rates than industrialised countries. This positive growth has translated into a substantial decrease in poverty rates in the developing world. However, there are remarkable differences between the success of Asian countries vs. African and Latin American countries. Asia has managed to create a substantial number of jobs in the high-productivity sectors of the economy – something that Africa and Latin America still need to do.