Economic and Financial Review

Volume 49 | Number 1 Article 4

3-1-2011

Face to Face with Productivity - a review

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Face to Face with Productivity[++] - A Review

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I. Introduction

Factor productivity concerns often dominate the discourse on economic matters especially in developing and emerging markets for the simple reason that productivity and economic prosperity are often linked. The article focused on the factors contributing to slow growth in per capita income amongst Latin American Countries (LACs) and further postulated that declining growth in per capita income was the result of plummeting factor productivity growth within the region, rather than lack of investment or citizen's willingness to work. A synopsis of the article is presented in section II below, while comments and lessons for Nigeria are discussed in section III.

II. Overview of paper

The article provides an assessment of productivity levels in selected Latin America Countries (LACs)and noted the widening productivity gaps between Latin America and the developed world compared with the fast-paced economies such as China, Japan and Korea. According to the paper, the relative per capita income of Latin America had accounted for 25 percent of the US of America a "half century ago" compared with approximately 17 percent as at today. The authors, however, observed that the poor growth and income levels of Latin America economies were not necessarily due to a lack of investment, but rather resulted from the declining growth of productivity levels. Chile and Costa Rica were identified as regional economies with efficient utilization of resources, but yet accounted for three-quarters of the factor productivity of the US. The authors in a comparative analysis, further pointed out that with the exception of labour productivity in the agricultural sector which compared favorably with the rest of the world (East Asia and developed economies) at a steady rate of >2 per cent annually, the industrial and service sectors within the LAC witnessed a stagnant growth in a period of at least twenty years.

In trying to adapt the industrial revolution approach of the developed economies,

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[++]Published in the IMF Finance and Development, March 2011 by Eduardo Lora and Carmen Pagés.
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the LAC was faced with much more constraints than their counterparts in the developed economies which were in the form of high tariffs, high migration of workers to city centers and an abundance of small and medium-sized firms which led only to a partial success. According to the author(s) within the LACs, 84 per cent of firms employed 10 workers or less. In Mexico and Bolivia, the authors estimated this figure at more than 90 percent, vis a vis 54 per cent of small firms with similar number of workers in the US. Such structural distortion in the employment structure of firms only further worsens the allocation of physical and human capital resources, as resources that otherwise would have been allocated to most productive firms were shifted to least productive firms (large in number, but with fewer employees). Furthermore, small firms were often limited in their scope of expansion beyond the domestic markets. Rather than shifting workers from agriculture to the more productive industrial manufacturing sectors as in the developed countries, LACs workers found recourse in the service sector which employs more than 60 percent of the labor force, while the manufacturing sector accounted for 20 per cent of the employment of the labor force.

A scenario analysis by the authors indicated that with the assumption that productivity efficiency levels between the US and a typical Latin American country were at similar levels, income per capita of the LACs would be double its current ranking. Factors accounting for the low productivity levels in developing economies were summarized in two forms; "market failures" and "bad policies", which weakened incentives for "innovation, discourage competition, prevent efficient companies from growing and further promote the survival and expansion of less productive firms". In as much as the authors acknowledged that fostering higher productivity was complex, certain factors were identified as germane to the objective of increasing productivity growth. These are efficient resource allocation, improving the credit market, improving tax and social policies and promoting competition. Shifting physical and human capital resources from the less productive to the most productive firms were seen as options to enhance productivity efficiency gains in both the manufacturing and service sectors of the economy. The second critical factor was an improvement in credit systems especially via expanded range of financial products. According to the authors, some LACs like Brazil were able to make credit more available and found out that sectors whose investment needs made them dependent on credit had the fastest rate of formalized employment.

Other key measures were improvement in financial and tax policies in a simplified manner which did not encourage inefficient behavior. For instance, corporate tax was considered high at 20 percent in LACs compared with 16 percent in advanced economies. These high taxes act as an incentive for firms to evade tax and in some cases constrain firms' expansion beyond a certain threshold due to growing tax concerns. Other areas of improvement include better regulatory oversight and prudential regulation to protect the financial sectors from internal and external credit shocks as well as improvement in credit and property rights supervision.

III. Comments and Lessons for Nigeria

The paper clearly articulated the causes of low per capita income in LACs. The article, however, placed more emphasis at analyzing the factors responsible for and consequences of slow growth in factor productivity with broad, but vague solutions for improving per capita income growth. Thus, more specific solutions in a country or regional context would have been more appropriate.

In Nigeria, the year 1999 commenced a period of progress in economic reforms aimed at increasing the growth prospects of the economy. However, unfolding economic developments in Nigeria have often questioned the impact of the reforms, especially within the context of the widening gap between strong output growth witnessed in the economy and improvement in physical and social wellbeing of the citizen. The productivity level, measured by the growth in gross domestic product has been estimated, on the average, at 6.9 per cent in 2010 and the World Bank has forecast a growth rate of 7.1 percent in 2011 compared with growth forecast for other world regions. Nigeria even maintained a strong growth even in the face of the global crisis, compared with most developed economies in the world. Available data, further suggests that recent growth performance in Nigeria has been largely driven by the non-oil sector (agriculture, wholesale and retail trade sectors) as well as the structural transformation towards the service sectors led by ICT and construction. A more critical contributor to the growth performance is the increased factor accumulation of capital and labour, albeit with fewer increases in total factor productivity. According to the World Bank (2007), the contribution of TFP to growth declined during 1990 -2002 and any marginal increases witnessed may have been as a result of delayed impact of critical reform decisions embarked upon in 1999 some of which were more focused on the oil/gas and telecommunication sectors with high capacity for earning quick returns. Data from the National Bureau of statistics living standard survey also suggests that about 28 percent of the labor force make up the informal sector, while wage employment further constitutes about 10 percent of the labor force and largely dominated by the public sector. The binding constraints to productivity are well documented in the literature. To mention a few, lack of skilled personnel, distortionary tax and trade regimes, poor controls and standards as well as unreliable and insufficient infrastructure together constitute constraints to productivity. In fact, the Central Bank through the Governor, Sanusi Lamido Sanusi, has often stated categorically that in order to transform the resource potentials of the Nigerian economy, deliberate and strategic investment is required for the development of modern infrastructure that will sustain growth.

What can Nigeria do to address low factor productivity? For starters, the current approach at addressing constraints in the value chain of promising and key sectors of the economy is a measure that could not have been spearheaded sooner by the Central Bank of Nigeria. Most of the value chains are dominated by the large informal sector often characterized by casualisation of workers, low skills level and high substitutability of labor. There is, thus, a need to address these issues holistically either from a public or private sector angle or an enhanced collaboration between the public and private sectors. First, value chain sectors with high employment potentials need to be identified. Literature often suggests ICT, agriculture, wholesale and retail sectors as viable value chains. In Nigeria, these sectors have already shown potential signs of being a critical source of growth and employment creation. Efforts at supporting value chain should also take account of the value adding and value diverting (constraining) aspects of the value chain processes that need to be addressed to increase efficiency within each value chain. A second approach at improving productivity is skill development initiatives which can be embarked upon by both the public and the private sectors via training, business development support services and transfer of technology.

The productivity of any sector is as good as the level of skills that is obtainable within it. A shortage of skilled labor in most cases leads to the use of what is available; which in most cases are low skilled workers and expatriate workers. Therefore, the educational system needs to be overhauled and reviewed. A situation in which the skewed preference for academic education to the detriment of technical and more practical education persists does not augur well for the Nigerian economy. Therefore, concrete and targeted interventions at enhancing technical skills in employment intensive value chains needs to be designed to address growing skills gap. A first step in this regard will be to develop a systematic framework for assessing the relevance of the educational content offered in our public and private educational institutions. In addition, information on skills demanded or required either on a sector, geographic or state-by-state basis should be made widely available. This will direct interventions at skills development in a much more strategic manner such that local educational/training institutions would be made more responsive to the changing demands and requirements of the labor market and indeed emerging technologies. A second option will be to create stronger linkages between public/ private sector employers and training institutions.

Improvement in the area of infrastructure, supply chain, access to finance and trade/tax regime cannot be overemphasized. The World Bank had estimated that most low income countries (LICs) need at least 9 per cent of their GDP invested in infrastructure to achieve the millennium development goals. Currently, in most

LICs, this accounts for less than 3 per cent of GDP. A persisting situation of restrictive trade policy without any major improvements in the provision and maintenance of critical infrastructure for productive activities will only worsen smuggling activities across the Nigerian borders. In 2007, the Nigerian government under the auspices of the Federal Ministry of Commerce and Industry had published a blueprint on a cluster concept as an acceptable approach for Industrial development strategy in Nigeria. However, the implementation of the proposals in the document is yet to witness any significant progress. Credit incentives by government through the Central Bank to boost supply chain of finance need to be monitored beyond the amount distributed and/or utilized to ensure compliance with performance benchmarks (if any) and that intended results are achieved. Interventions in value chain sectors should also be hinged on their sustainability, relevance and feasibility. These are by no means an exhaustive approach to dealing with the productivity constraints in the Nigerian economy. Some measures are short term in nature, while others are long term in approach. Nevertheless, they all attempt to draw attention to critical issues that are worth addressing if the Nigerian economy must achieve its National Vision (NV) 20: 2020 goals.

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