

IFAD – 50X2030 Initiative Research Brief

Rural Non-Farm Enterprises Dynamics and Youth Employment Challenges in Ethiopia

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Summary

In Ethiopia the contribution of the rural non-farm enterprise (RNFE) sector to employment and income has increased overtime, and this contribution is unlikely to diminish in the future given that rural businesses will be needed to support the job creation and hence livelihood to the growing number of youths who do not have access to farming land. However, the dynamics of the sector has to be explored to understand the contributions of RNFE and its implications for development. In this report, we analyse dynamics in RNFEs in Ethiopia and recommend policy options to make the sector serve as a way out of poverty especially for the youth.

Main messages

- Participation in RNFE, and transition into and out of high-return RNFE is high among young households than among matured households.
- Initial capital endowments such as assets, human capital, land and livestock do not affect entry into RNFE implying the poor can enter into the sector. However, these endowments are highly important for optimizing returns from RNFE, indicating the fact that the sector requires initial investment and skills to develop.

Background

Rural nonfarm business evolves overtime as households try to adjust their income portfolio to changing opportunities, capacities and challenges, including experience of shocks. In many of the poor agrarian economies such as much of Africa, RNFE is a potential alternative to agriculture for stimulating rural income

growth. Evidences suggest that over time the contribution of the sector to employment and income has increased. With economic growth recorded and rise in the rural economy in Ethiopia and corresponding rise in youth population in the rural areas, it is expected that rural non-farm enterprises grow in number, size and type of business operations.



Source: IFAD Image Bank

However, the contributions of RNFE and implications for development not only depend on entry into off-farm employment but also on the ability to remain employed. In this regard, an understanding of the dynamics of non-farm enterprise and participation of the youth is imperative for any policy-maker who seeks to create employment opportunity for the youth and improve household's income from non-farm sector.



Source: IFAD Image Bank

Research methodology

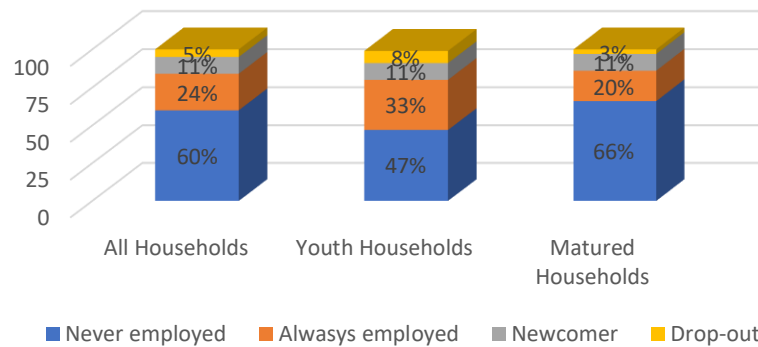
We use the national, longitudinal and multi-topic household survey data for Ethiopia generated as part of the World Bank Living Standards Measurement Study (LSMS-ISA)¹ initiative to analyse dynamics of RNFEs in Ethiopia. We employ two estimates in the RNFE analysis. First, we estimate households' participation in RNFE and its determinants. Second, we estimate dynamics of RNFEs where we analyse mobility between business enterprise status and the factors explaining transition to a higher work status. In order to examine if youth have a different choice, and if the factors that determine upward movement in the business ladder are different for youth, we analysed dynamics of RNFE by disaggregating participants into youth and matured households, i.e., household heads aged 15 to 34 are categorized as youth and those aged 35 to 64 as matured households.

Research findings

Initial capital endowments are more important for intensity of participation than for entry into RNFE: Initial capital endowments such as assets, human capital, land and livestock affect intensity of participation but they do not affect entry into RNFE. This infers that initial capital endowments are not barriers to entry into RNFE implying the poor can enter into the sector. However, for optimizing returns, these endowments are significant indicating the fact that the sector requires initial investment and skills to develop.

Women's rural non-farm entrepreneurship is common but their intensity of participation is low: Female headed households often attempt to diversify income sources to non-farm enterprises, however, their intensity of participation expressed by amount of income earned from the sector is low. This is often due to the fact that women's participation in RNFE is derived by push factors. Unless additional assistance in terms of capital and skills development is given, women's participation remains confined to low paying rural non-farm enterprises that require less capital as well as skills.

Figure 1: Dynamics in RNFE participation by age category over the period 2011 - 2015



Youth participate in RNFE more than mature households: Figure 1 shows the dynamics in RNFE participation in rural Ethiopia. The figure indicates the proportion of rural households who entered and exited RNFE and who were never or always employed in RNFE over time. We observe that a large proportion of the households, at least 60%, were never employed in RNFE in Ethiopia. This is a large figure indicating that RNFE is not yet developed in rural Ethiopia. However, the participation rate is different among the youth and matured households. While 67 percent of the matured households never participated in RNFE, the figure for the youth households is 47 percent. This indicates that the older households get, the more risk averse they

¹ For additional information on the LSMS-ISA, see the World Bank's website www.worldbank.org/isms-isa

become. Moreover, it could also mean that the youth are more educated and entrepreneurial than the old and this makes them to diversify to non-farm business activities. With a high population growth in Ethiopia especially the growth rate for the youth, it is possible that the youth may not have access to land as the old households and this may push them towards diversifying to non-farm activities.



The share of people who are continuously in RNFE is higher among the youth than the old. Close to one third of the youth households continuously participate in RNFE compared to

only one-fifth for the matured households. Though, entry rates are the same between the youth and matured households, exit rate is higher among the youth than the matured households, indicating more dynamics among the youth than among the matured households.

Transition into and out of high-return NRFE is higher among youth than among matured households: Table 1 reports proportion of households who transitioned into and out of high return RNFE in 2013 or 2015. Both transition into and out of high-return RNFE is higher among the youth households than among matured households. Out of the youth households engaged in pure agriculture or low-return RNFE in 2011, 12.6 percent transitioned into high-return RNFE in 2013 or 2015. Similarly, 7.2 percent transitioned out of high-return RNFE in 2013 or 2015. The figures for matured households are 9.7 percent and 4.2 percent respectively, indicating that dynamics in movement into and out of high-return RNFE is higher among the youth.

Table 1: Proportion of households who transitioned from pure agriculture or low-return RNFE in 2011 to high return RNFE in 2013 or 2015

Household type	Transition into high-return RNFE in 2013 or 2015	Transition out of high-return RNFE in 2013 or 2015
Youth households	12.6	7.2
Matured households	9.7	4.2
All households	10.7	5.2

Source: Own calculation based on LSMS-ISA data for Ethiopia

Initial capital endowments influence transition into and out of high-return RNFEs: Table 2 indicates initial capital endowments and transition into high-return RNFE. It indicates that initial capital endowments are correlated with the transition into high-return RNFE. Households who moved into high-return RNFE have on average lower land and livestock holdings, and more number of adults and better education level. When disaggregated by age of household head,

we observe that human capital in the form of larger number of adult household members and higher level of education are important to transit to high-return RNFE among the youth, whereas for matured households physical assets mainly land and livestock holding are important, i.e., matured households who transitioned to high-return RNFE have lower land and livestock holdings than otherwise.

Table 2: Initial capital endowment and accumulation by transition into high-return RNFE

Capital endowment in 2011	Transition from pure agriculture/low-return RNFE into high-return RNFE in 2013/2015	Youth Households		Matured Households		All Households	
		Stayed	Moved	Stayed	Moved	Stayed	Moved
		Average land holding (hct.)	1.15	0.86	1.43	0.84***	1.39
Average number of adult HH members	2.09	2.27**	2.57	2.56	2.54	2.48	
Average adult education: Above elementary	0.35	0.44	0.42	0.55	0.41	0.51	
Average adult education: Elementary	0.60	0.85***	0.70	0.79	0.70	0.83***	
Average livestock holding in tropical livestock unit	3.19	2.40	4.75	2.92***	4.36	2.75***	

Population statistics are corrected using sampling weights. *p<0.10, **P<0.05, ***P<0.01

Source: Own calculation based on LSMS_ISA data for Ethiopia

Policy implications

Policy actions that support enterprise owners are needed if RNFES are to serve as a way out of poverty especially for the youth. The following are some of the policy actions

- Instruments such as entrepreneurial skills development and access to finance that enhance investments and gradual accumulation of capital are vital especially for the youth to earn higher returns and also to transit to high-return RNFES. Hence, it is critical to **identify and support talented young entrepreneurs** that have the potential to take on more risky but also more productive types of businesses.
- Shocks that reduce agricultural productivity are significant not only in limiting the probability of the transition to high-return RNFE but also on increasing the probability

of transiting out of high-return RNFE. This signifies the **need for social protection schemes including measures that can mitigate shocks.**

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