

The youth employment challenge in developing countries: Promoting entrepreneurship and reducing skills mismatch

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Introduction

As many as 600 million jobs must be created worldwide over the next decade to keep employment rates at their current level (ILO, 2012). The employment challenge is particularly pressing in developing countries, where demographic pressures are stronger, wage employment opportunities are scarce and formal job creation is insufficient to give most youth access to decent work. Weak enforcement of labour standards keeps many young people in low quality jobs and as working poor.

In this context, fostering youth entrepreneurship has gained importance on the global and national policy agendas as a way to expand employment and earning opportunities. Many governments in developing countries are also realising that good quality jobs matter for development and that dedicated efforts are needed to boost the quality of jobs and make work pay, as conveyed in Goal 8 of the 2030 Agenda for Sustainable Development.

As attractive as being one's own boss may sound, entrepreneurship is not for everyone, and not in the least for a large number of youth that is low-educated and low-skilled, which is the case in many developing countries. In addition, little is known on what actually matters for young people in terms of job characteristics and employment conditions. Many young people start a business or become self-employed by default rather than by choice. Today, in many developing and emerging economies, a key development challenge is that jobs do not live up to youth's expectations and aspirations.

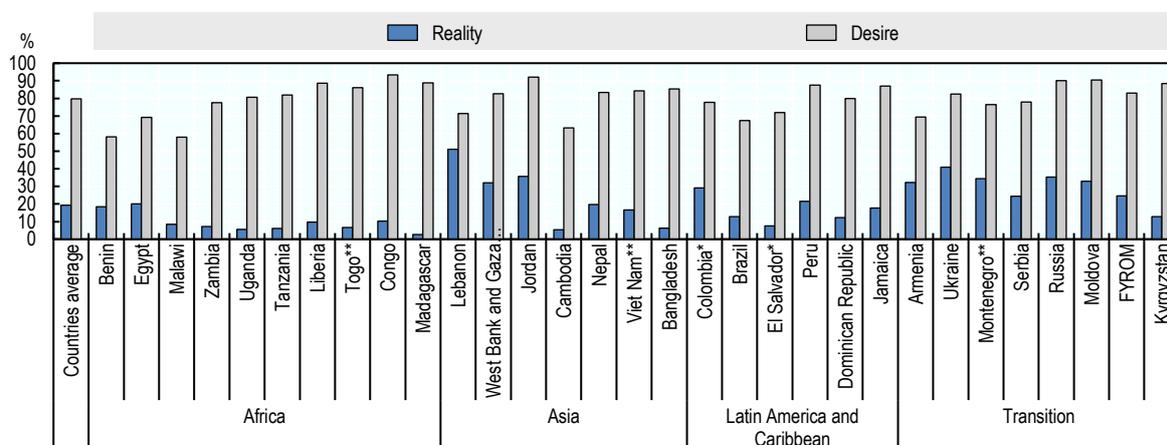
There are large gaps between young people's career aspirations and employment reality

In most developing and emerging countries, large gaps between career aspirations and the reality of the labour market constitute a key challenge. The moment career aspirations affect young people educational choices, the alignment between youth career aspirations and the reality of the labour market becomes critical to understand youth well-being, firm productivity and youth labour market performance. Evidence from the School-to-Work Transition Surveys (SWTS) conducted in 32 developing and emerging countries, and the International Labour Organization (ILO) employment projections, indicate that youth career aspirations by skills level are overly optimistic in the light of today's and tomorrow's labour market needs (OECD, 2017a).

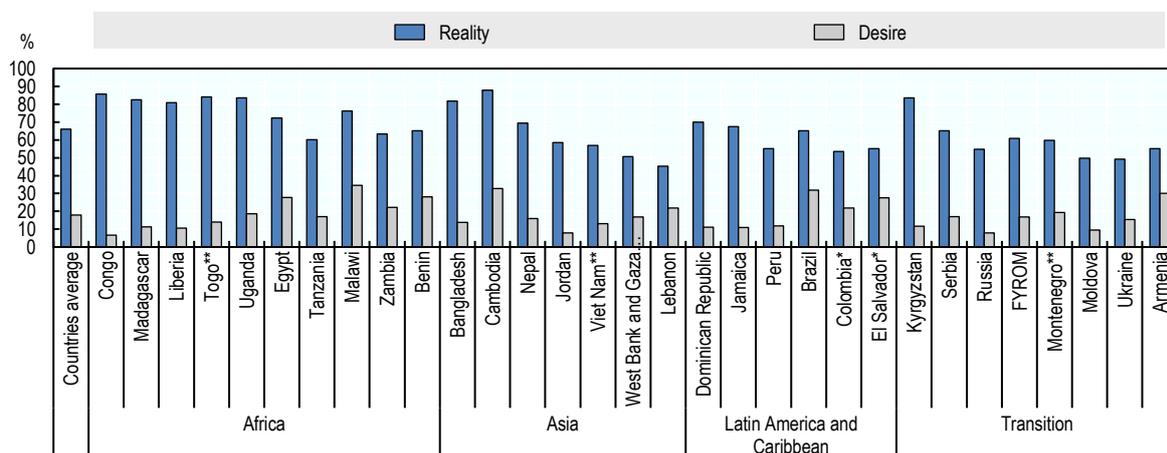
Overall, about 60% of students willing to work in high-skilled occupations will unlikely fulfil their career aspirations; while as many as 73% and 80% of those young workers who occupy, respectively, medium- and low-skilled jobs have not been able to satisfy their career preferences (Figure 1). Using employment projections until 2021 yields similar results and points to a large misalignment between youth career preferences by level of skills and projected labour demand. Career aspiration gaps by skills level are particularly pronounced in Africa and Latin America.

Figure 1. Difference between the distribution of aspirations and the distribution of workers at different skills levels of the occupations by country (%)

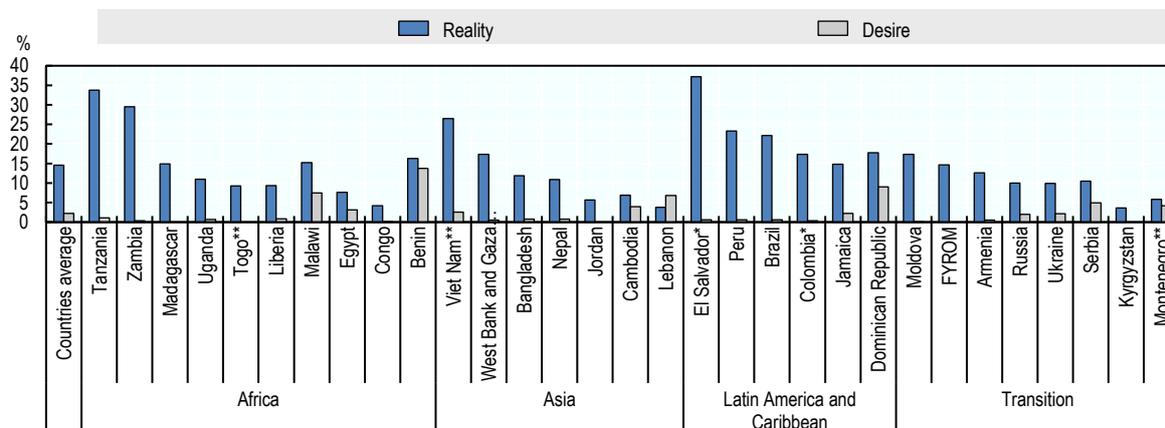
Panel A. High skilled occupations (ISCO 1-3)



Panel B. Medium skilled occupations (ISCO 4-8)



Panel C. Low skilled occupations (ISCO 9)



Note: Countries are sorted by the difference between the share of young students who say they want to work in a high skilled (Panel A), medium skilled (Panel B) or low skilled (Panel C) occupation and the proportion of these categories in the 15-29 working population. Data are missing for Tunisia. FYROM corresponds to Former Yugoslav Republic of Macedonia.

* Data for Colombia and El Salvador refer to the urban population only.

** Estimations for Montenegro, Togo and Viet Nam do not account for sampling weights as they are missing in the data.

Source: OECD (2017a)

Strong preferences to work in the public sector are unlikely to be met. On average across the 32 developing and emerging countries, the proportion of students who want to work for the public sector but unlikely to end up doing so is as high as 40%.

Interestingly, the gap between career aspirations and the reality of the labour market persists for tertiary educated youth. On average, around 48% of tertiary educated individuals willing to work formally in a high-skilled job will unlikely be able to do so. This mismatch is less pronounced in more developed economies where employment opportunities for the highly skilled are greater. Africa has the highest share of tertiary educated working in medium- or low-skilled jobs.

Surprisingly, earning criteria does not seem to be the strongest motivation across occupations. In countries and territories like Armenia, Ukraine, Benin, Kyrgyzstan, Lebanon, Liberia, West Bank and Gaza, Peru and Tanzania, the average earnings are higher for medium-skilled and/or for low-skilled occupations than for high-skilled occupations. Earning cannot explain the large misalignment in career aspirations and the reality of jobs.

Certain facets of jobs matter for job satisfaction. Being self-employed by choice or as required by the family tends to increase job satisfaction, as observed among a non-negligible proportion of young people in low-income countries. In Congo and Malawi, one out of three young workers is engaged in self-employment by choice.

Low-skilled employment in developing countries tends to bring job satisfaction down. Low-skilled jobs constitute a quarter or more of youth employment in countries like Brazil, El Salvador, West Bank and Gaza, Peru, Tanzania, Viet Nam and Zambia. Agriculture, which is the main source of jobs for more than 40% of young workers in Kyrgyzstan, Madagascar, Nepal and Togo, also brings job satisfaction down.

Other job facets such as the low level of job security, informality, skills mismatch and the lack of training opportunities make young workers unhappy. Job insecurity is particularly pronounced in countries such as Egypt, Malawi, Montenegro, Peru, and Viet Nam, where 50% or more of all young wage employees work as temporary employees with fixed-term employment contracts. Informality is also dominant in Africa, where it concerns 80% of young workers. In Asia and Latin America, 48% and 33% of young workers, respectively, are in a non-registered activity. As for skills mismatch, it concerns 55% of young workers and only 20% on average are offered training opportunities.

Governments are promoting entrepreneurship but it is no panacea for the youth employment challenge

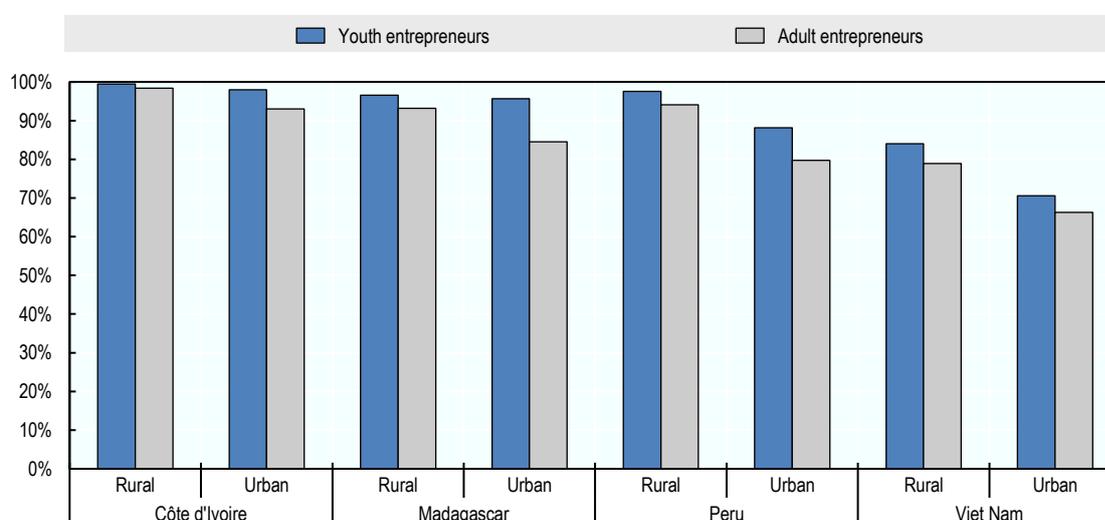
In the face of a global youth employment challenge, governments are promoting entrepreneurship among youth as a solution. However, empirical evidence from four countries – Côte d'Ivoire, Madagascar, Peru and Viet Nam – shows that only a tiny portion (on average 5%) of youth entrepreneurs proves to be successful (OECD, 2017b). A large number of youth entrepreneurs are confined to subsistence activities, especially in developing countries. In fact, the vast majority of young entrepreneurs, as high as 86% in the case of Côte d'Ivoire, records profits below the average wage earned by their peers in salaried jobs. The fact that a large majority of youth are failing to succeed as entrepreneurs cautions policy makers to move carefully in promoting entrepreneurship as a solution to the youth employment challenge.

Youth entrepreneurship can be defined as self-employment among youth. There is no internationally agreed definition of entrepreneurship due to the complexity of the notion and its multifaceted nature. This leaves room for a multiplicity of definitions. The concept of entrepreneurship encompasses a very heterogeneous reality that can be seen as a continuum of businesses operating at different performance levels, ranging from own-account workers and micro-enterprises to large companies; from necessity-driven, subsistence and informal businesses to opportunity-driven, highly profitable and innovative

formal enterprises; from businesses relying on informal networks to enterprises well-connected to local and global value chains and markets.

In developing countries, informality is the norm (Figure 2), and therefore businesses that operate in the informal sector must be included. While data gaps and limitations make it difficult to obtain representative and reliable quantitative information on entrepreneurship in developing countries, a number of surveys, with varying levels of representativeness and detail, can be used to measure entrepreneurship. OECD (2017b) uses linked labour force and enterprise surveys for Côte d’Ivoire, Madagascar, Peru and Viet Nam to understand the role of youth entrepreneurship in generating decent employment for youth and the drivers of youth entrepreneurial performance. Youth entrepreneurs operate in different conditions in these four countries, mirroring the diversity of the developing world, in terms of both geographical location and income level.

Figure 2. Share of unregistered businesses (%)



Note: Agriculture excluded. Youth are aged 15-29 and adults 30-64. Businesses unregistered with the authorities are considered informal.

Source: OECD (2017b)

Few youth entrepreneurs actually succeed in making profits and generating jobs

Youth entrepreneurship is defined in OECD (2017b) as comprising all non-farm household unincorporated businesses operated by youth, either as own-account workers or employers. Although it is not the dominant form of youth employment, youth entrepreneurship is a significant phenomenon in developing countries. The majority of young entrepreneurs work in rural non-farm businesses, and most of them are poorly educated.

The extent of youth entrepreneurship as the main occupation varies greatly across countries, ranging from 14% in Viet Nam to 43.9% in Côte d’Ivoire of the total youth employed (outside agriculture). The vast majority of entrepreneurs, in particular youth, are own-account workers. While youth-run businesses account for a non-negligible share of all businesses, a number of these are secondary occupations. Interestingly, there seems to be a generational transition towards wage employment as countries develop economically.

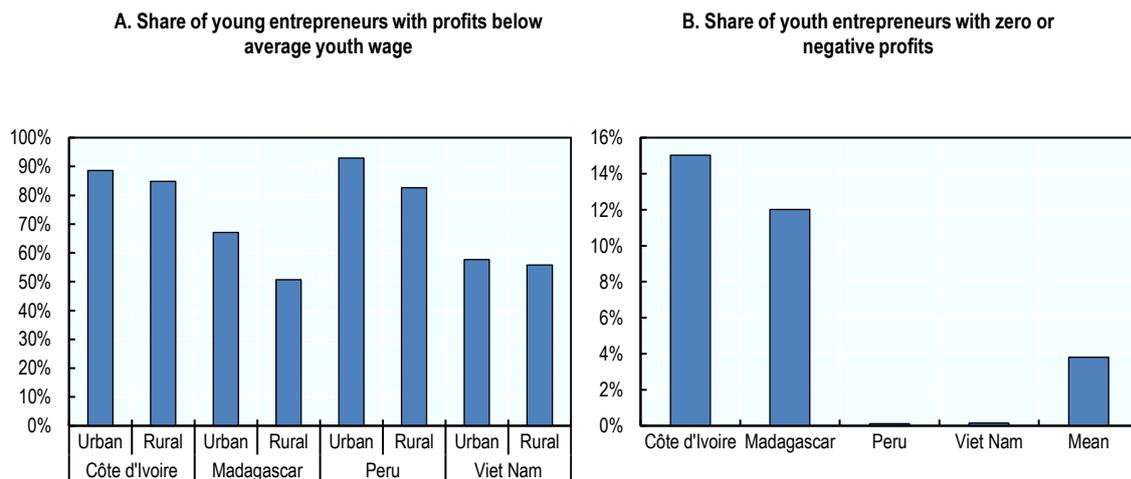
The majority of young people start a business for lack of better choice. In Côte d’Ivoire, Madagascar, Peru and Viet Nam many young entrepreneurs declare that they are running a business by choice, but

when probed further, they are more likely to be underemployed and to hold multiple jobs than their peers in salaried jobs. This reveals that youth entrepreneurship is most likely driven by necessity, notably due to the lack of wage employment opportunities. The youth employment challenge is thus primarily structural and driven by insufficient aggregate labour demand.

Few youth entrepreneurs possess basic business skills. Information shows that very few young entrepreneurs use written accounts. Available data from Madagascar highlight the lack of business practices among young entrepreneurs. Youth businesses are typically very small. They primarily operate in petty trade and services, often referred to as free-entry sectors, and almost none of them are registered with the authorities.

Youth entrepreneurship is less financially rewarding than wage employment. Although the vast majority of young entrepreneurs generate profits, these are most often modest and below the level of income earned by youth in wage employment (Figure 2). The distribution of profits is more unequal than in the more advanced countries. Relatively few youth businesses generate employment. When youth entrepreneurs recruit, they rely almost exclusively on family members. Only a tiny proportion, on average 5%, of youth entrepreneurs can be considered top performers (Figure 3), i.e. they generate both profits and jobs.

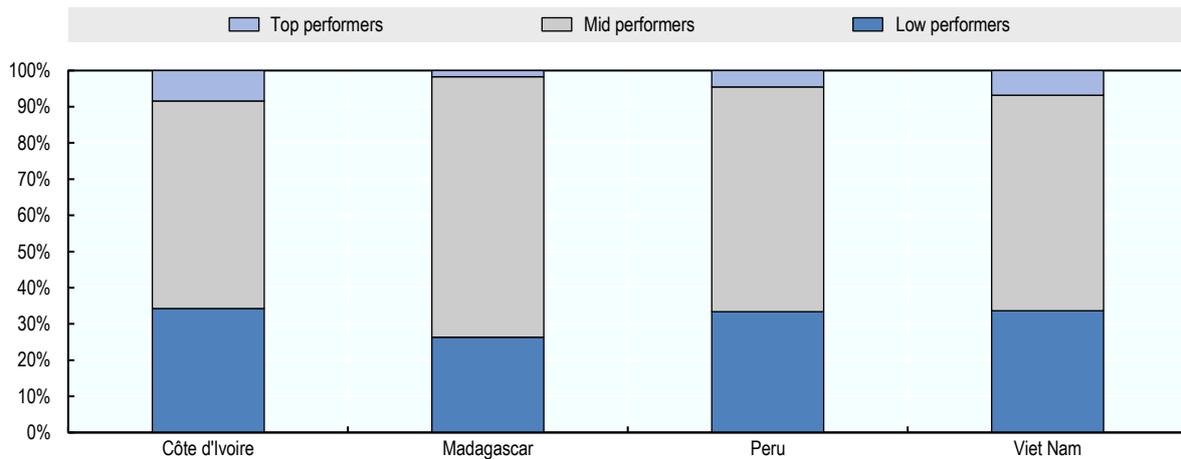
Figure 3. Profits of youth businesses



Note: Agriculture excluded. Youth are aged 15-29. Profits are measured by asking surveyed business owners for their complete list of sales and expenditures during a reference period.

Source: OECD (2017b)

Figure 4. Distribution of youth businesses by performance level (%)



Note: Agriculture excluded. Youth are aged 15-29. Top performers = youth businesses that recorded the highest profits (top tertile of the distribution of profits) and generated employment since their inception. Mid performers = youth businesses with the highest profits (top tertile) that did not create jobs and youth businesses with intermediate levels of profits (second tertile). Low performers = youth businesses with the lowest profits.

Source: OECD (2017b)

The majority of youth entrepreneurs remain in subsistence activities

Measuring youth entrepreneurship and entrepreneurial performance is challenging in the developing world. Using profitability and job creation, we analyse the determinants of youth entrepreneurial performance to understand what makes a successful entrepreneur.

Education significantly increases youth entrepreneurial performance. Managerial capital and business skills are key ingredients for success. Cross- and within-country econometric analyses show that entrepreneurial performance is driven by multiple factors, which are explained below. Two groups in particular face disadvantages in terms of business performance: young women and rural dwellers.

Informality weakens youth business performance. While the quality of the business environment varies significantly across countries, informality is common everywhere and unambiguously drives youth business performance down. Depending on the country, reasons for being informal range from tax avoidance to the high cost of registration or simply lack of information. There is also evidence that the sector of activity affects performance, although this varies across countries. For instance, in more economically advanced settings, activities in manufacturing seem to offer the highest chances for youth to move up the entrepreneurial performance ladder.

Favourable physical operating conditions raise entrepreneurial performance. The vast majority of youth businesses operate on the streets or at home. Only few have dedicated premises. Favourable operating conditions – such as access to a dedicated place or office, basic infrastructure services and information and communication technologies (ICT) – often lead to higher youth entrepreneurial performance. Yet few youth businesses have access to basic infrastructure and services such as water and electricity, and in particular to ICT (phone and Internet).

Access to finance and market integration presents major challenges. Access to credit is a primary concern for a large number of youth businesses. Youth have to deal with limited personal savings and resources; inadequate youth-friendly financial products, including micro-lending and seed funding; high credit and collateral requirements, and excessive restrictions (e.g. age limit to open a bank account); low financial literacy; and limited knowledge of financing opportunities. The fact that youth businesses are poorly integrated into markets is another barrier to performance. Youth businesses rarely

interact with larger private companies, and in particular with the public sector. By and large, they buy and sell products or services to individuals and other small businesses.

Policy recommendations

Unlocking the youth entrepreneurship potential

Support youth entrepreneurs with the most potential and re-train those that are struggling on subsistence activities to find wage jobs. The high heterogeneity observed among youth entrepreneurs calls for policy solutions and interventions that should be carefully targeted to profiles with real entrepreneurial potential, while those engaged in subsistence activities should be trained and redirected to transition into the labour market or public works programmes. Recent evidence makes a strong case to redirect entrepreneurship programmes to those young people with the highest entrepreneurial potentials and offer programmes on business development services as well as on a package of training and access to finance services that have proven to work best for micro-entrepreneurs.

Invest in comprehensive entrepreneurship programmes. Impact evaluation shows that adopting a comprehensive, integrated approach works well, while stand-alone programmes are generally found to be less effective. Entrepreneurship programmes are indeed more successful when they provide comprehensive packages offering multiple services simultaneously. Business development services have an established track record of contributing effectively to business performance and employment generation, and there is a strong case for supporting them.

Integrate entrepreneurship education in formal schooling. Education policy and the formal schooling system must integrate comprehensive entrepreneurship education into the national curriculum at all levels. Comprehensive curricula need to be developed to provide young people with different sets of competencies, including technical, non-cognitive and life skills as well as entrepreneurial behaviour. More attention should also be paid to business development skills and real-world knowledge in vocational training. In addition, the schooling system must include a TVET-level qualification for the agricultural sector, and introduce agriculture education at the primary and secondary level.

Promote youth entrepreneurship spirit through success stories and role models. The talent of young entrepreneurs should be highlighted by organising conferences and highly visible summits, and by supporting youth entrepreneurship competitions, awards and events to raise the profile of young entrepreneurs and create awareness about entrepreneurship. The development of networks of young entrepreneurs must be encouraged through peer networks grouping youth entrepreneurship organisations, business associations, youth-led organisations and other stakeholders. Entrepreneurship potential can also be promoted via knowledge exchange between established businesses and aspiring young entrepreneurs. Ultimately, young entrepreneurs must be given more visibility. To this end, media and other communication tools and platforms can be used, in particular to promote role models.

Simplify administrative procedures. This can be achieved by making business registration quicker and less expensive, simplifying tax filing requirements and accounting methods, and reviewing bankruptcy laws to make them more tolerant of risk taking and business failure. Tax regimes must be rendered more supportive, for instance by lowering tax rates or introducing tax and social contribution exemptions for young entrepreneurs. In addition, the business regulatory environment needs to be more predictable. Since lack of knowledge about business registration and licensing strongly drives informality, improving access to information on the regulatory framework and better communicating the benefits of formalisation are important.

Encourage formalisation as a way to support business expansion. A right mix of incentives and sanctions is needed to encourage formalisation. Formalisation allows businesses to access financing

and increase their scale of operation. However, not all enterprises benefit in the same way, and among the smallest and most precarious production units, the effect of formalisation is still unclear. Rather than strict enforcement of formality, which is often socially costly and rarely efficient, the way to go is probably to encourage registration, especially through fiscal incentives, awareness-raising campaigns, simplification of business regulations, and business advice and training for informal entrepreneurs.

Reduce incentives for remaining informal. This requires careful monitoring of the impact of taxes and social contributions. For youth entrepreneurs, the benefits of operating formally often relate to the possibility to enjoy the legal ownership of their place of business and means of production, to benefit from enforceable commercial contracts and tax breaks, or to be covered by affordable social protection schemes, while the costs of entry into the formal economy encompass the need to pay taxes and social security contributions, obtain a license, or register their accounts. The cost-benefit ratio may be different for informal wage workers, for whom formalisation mostly means obtaining a formal wage job with a secure contract and statutory social protection.

Reducing skills mismatch

Develop a comprehensive information system on education and the labour market. A sound governance and informed policy making requires collecting a variety of information on people's trajectory in the education system and the labour market. Governments should follow how many students engage in various fields of study at different levels, follow the quality of educational resources, including pedagogical materials and teachers, and eventually track how students perform in the labour market. In parallel, information about the skills needed by the private sector should be collected. This can provide an accurate picture of the quantity and type of skills available and needed, and inform on the types and sources of skills mismatch in the country.

Strengthen mechanisms to improve industry engagement in curriculum development, training provision and financial contribution. Reinforcing the relationship between the education system (and TVET in particular), students and the private sector can significantly improve the relevance of education and facilitate students' transition into the labour market. The private sector can be involved at various steps of education provision, starting with consultation on curriculum development. Indeed, the private sector can identify up-to-date skills and knowledge students should acquire to work in various occupations and make sure there are no training gaps in the curricula. It can also be involved in delivering training through internships and apprenticeships. Governments should support these private sector efforts through incentive mechanisms. Finally, the government could increase partnerships with strategic sectors to develop specific skills in exchange of the financial contribution of enterprises.

Improve education quality at all levels, notably by investing in teachers. The lack of adequately trained teachers constitutes a major drawback to provide quality education at all levels. Governments should make sure they have sufficient training capacity to maintain adequate teacher-student ratio. Particular attention should be given to the training and recruitment of TVET teachers to supply the needs in high demand fields of study. Training should ensure teachers possess sufficient knowledge of theories and practical application of up-to-date equipment and production techniques. It is also crucial for teachers to receive pre-service training in pedagogy and teaching methodologies and gain experience through in-service training. In addition, remedial support and training should be available to teachers throughout their careers to ensure they keep up with technology and develop their competencies. To attract and retain qualified individuals, the system should offer competitive salaries and interesting career opportunities. Special incentives should be provided to teachers posted in rural areas.

Provide skills development and second-chance programmes for rural youth. Despite the potential for new jobs in agro-food value chains and non-farm activities in rural areas, the majority of rural youth in developing countries are low-educated and low-skilled. Skills mismatch, mostly related to under-qualification hinders any attempt at moving up the value chain or getting better jobs. At the same time, private sector employers including small and medium enterprises (SMEs) struggle to find qualified candidates to fill posts, even in promising sectors where labour demand is high. Traditional TVET

programmes either fail to reach out-of-school and low educated youth or do not train in subjects relevant for the labour market. There exist various training modalities and a wealth of information on what works and does not in TVET. Collaboration with the private sector to train young workers should be further explored. For example, more financial incentive schemes for SMEs to invest in youth skills development should be offered.

Increase and diversify the supply of quality TVET opportunities. In many developing countries, the share of TVET in total enrolment is extremely small in comparison to the share of young people leaving the education system with postsecondary education. Investing in the training capacity in technical education should therefore be a priority. Yet, governments should invest strategically, in co-ordination with the private providers of education in order to make the most of the TVET system. In particular, they should aim at diversifying the type of training provided, and the public sector should make sure they set high standards.

Recognise the importance of informal training and support traditional apprenticeships. Informal training, notably apprenticeships, constitutes a major source of training for school dropouts and low skilled youth. To improve the quality and relevance of informal training, the government should engage with the informal providers and help them find opportunities to develop their capacity (including pedagogical skills), support them financially to acquire modern equipment and promote community involvement to reduce the administrative and organisational burden of training. Developing certification for informal trainers and disseminating guidelines about required competencies for apprentices to obtain official certification could also improve functioning.

Guide student learning and career choices. While it is important that young people do not give up on their dreams or curtail their ambitions, policy makers need to ensure that young people can access accurate information about labour market prospects and receive effective guidance on the best way to get closer to their goals. Better and well-informed career guidance and counselling is thus necessary.

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