Why an integrated approach to structural economic transformation is needed for inclusive and sustainable industrialization and poverty eradication in a Multiple Crises African Context

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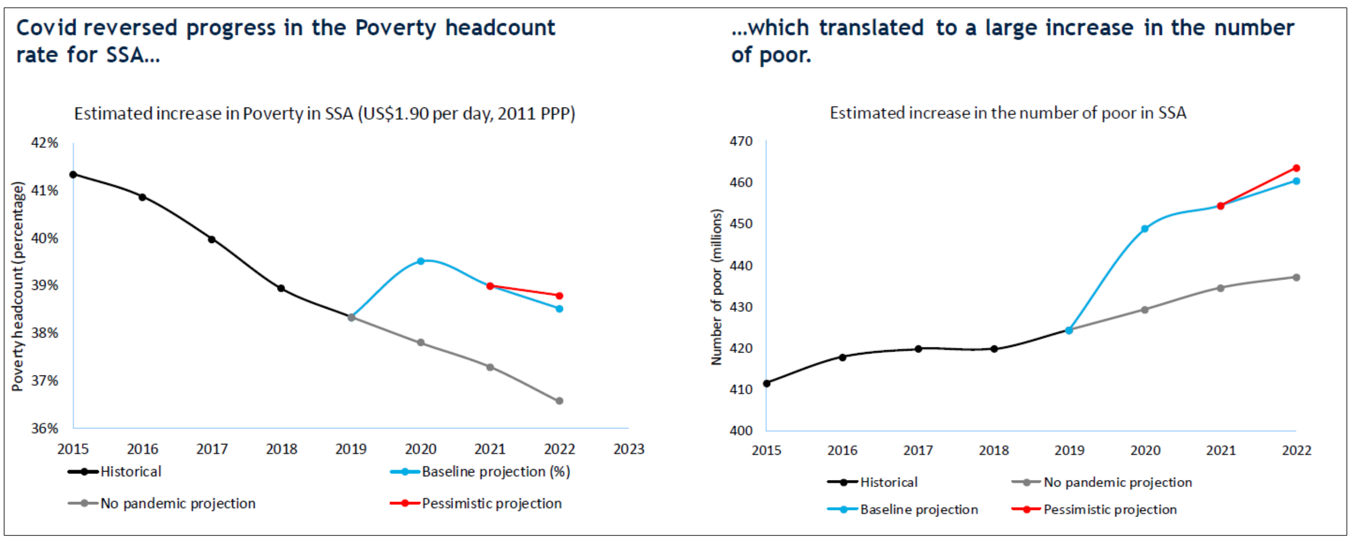
Introduction

In the wake of the COVID-19 pandemic and amid a confluence of crises, including the conflict in Ukraine and heightened climate change, the need for transformative change in Africa, specifically in the form of structural economic transformation, has gained remarkable prominence. The pandemic has resulted in an unparalleled reversal of poverty reduction, which continues to be further compounded by rising inflation and spikes in food, fertilizer, and energy prices due to the conflict in Ukraine. The impact of COVID-19 on African economies has been profound, disrupting supply chains and reducing demand for the continent's natural resource commodities, thereby slowing down growth and reversing poverty and inequality reduction efforts. The World Bank estimates that at least 40 million additional Africans have been plunged into extreme poverty in 2020 as a result of the pandemic (see Figure 1).

Figure 1: Effect of COVID-19 on Poverty Rates in Africa

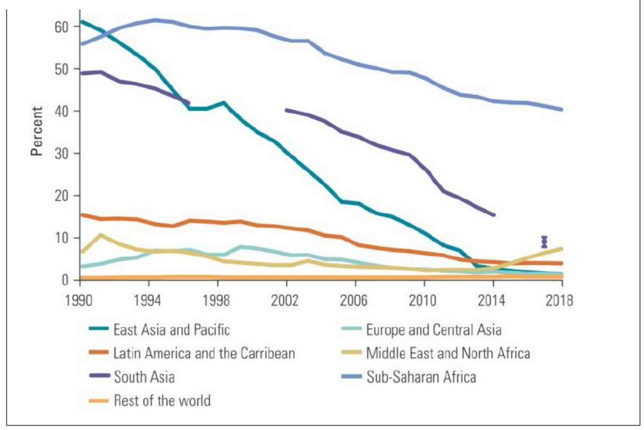


Source: World Bank (2020)

This realization along with the fact that extreme poverty since 1990 remains concentrated in parts of the world where it is hardest to eradicate: sub-Saharan Africa, conflict affected areas and rural areas, and the recognition that without a concerted "SDG push", at least 492 million people will be left in extreme poverty in Sub-Saharan Africa in 2030, is an increasingly daunting prospect. There is now a growing and inevitable sense in Africa that the nature and process of growth experienced in Africa over the last two decades needs to fundamentally change if a large segment of the African population is to escape and stay out of poverty, and inequality is to be reduced (see Figure 2).

Put differently, it has become increasingly apparent that the current pattern of growth in the context of multiple and intersecting shocks and crises will not be a sufficient and sustainable path to prosperity in Africa. Rather, it will be imperative that concerted efforts are made towards achieving structural economic transformation to mitigate the adverse effects of these crises and promote sustainable and inclusive growth in Africa.

Figure 2: Global Poverty Trends



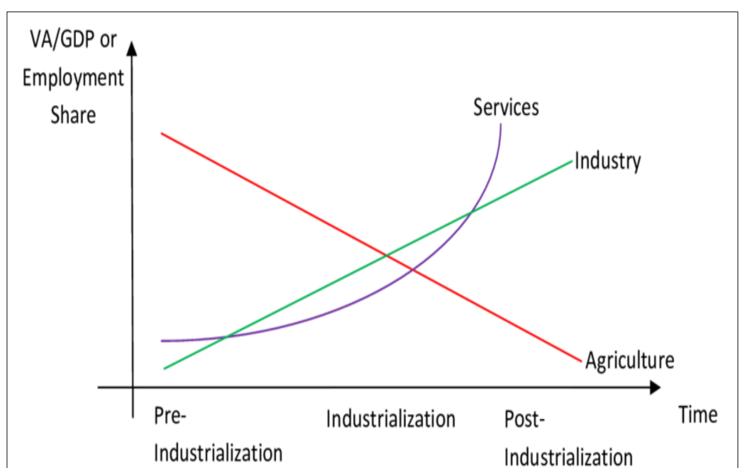
Source: World Bank (2020)

Hence in line with the objectives of this meeting, this background paper explores an innovative approach to accelerate poverty eradication in this decade of action to deliver the Sustainable Development Goals (SDGs). More specifically, this background paper explores the potential for structural transformation for inclusive and sustainable industrialization and poverty eradication in Africa. It examines the key drivers and challenges of structural transformation in Africa and highlights successful country examples that can used to gain policy insights. Finally, the paper touches on the role of international cooperation and partnerships in supporting structural transformation and inclusive and sustainable industrialization.

What is structural transformation and how does it unfold?

Simply put, structural transformation refers to the shift of economic activity from traditional sectors (such as low productivity agriculture and natural resource extraction) to more modern and productive sectors (such as mechanized agriculture, manufacturing, and services). Structural transformation is typically driven by multiple factors such as technological advancements, changes in demand, better infrastructure and institutions, and government policy shifts. It often results in significant growth and changes in the output and employment structures, as well as in the trade and investment patterns.

Figure 3: Schematic of Structural Transformation Process



Source : https://www.researchgate.net/figure/The-Structural-Transformation_fig1_24112167

The ultimate goal of structural transformation – as elaborated by several international organizations - is to create a more dynamic and competitive economy that can sustain high levels of growth and provide widespread benefits for populations, including better employment opportunities, higher wages, and improved well-being (see for example, UNDP, African Development Bank, UNCTAD and World Bank). However, this process can also be disruptive, particularly for workers and industries that are displaced by the changes, and it requires careful management and support from policymakers and other stakeholders. Theoretically, the journey towards structural transformation is a gradual and multi-stage process, characterized by a shift from subsistence agriculture to modernized agriculture, industry, and services (Lewis, 1954, Hirschmann, 1958, Kuznets, 1966 and see Figure 3). At the onset, the agricultural sector dominates offering employment and livelihoods to a significant proportion of a country's population. But with increasing agricultural productivity and the expansion of the economy, fresh opportunities emerge (such as agro-processing) which spawn new industries that initiate a slow but steady reallocation of the workforce away from agriculture and towards manufacturing and services.

This process by its very nature drives value-addition and diversification of products and services. In due course, the manufacturing sector grows at an exponential rate, further expanding its share of the economy and absorbing more and more labor. The unbridled momentum of industrialization fuels the rapid expansion of urban centers, accelerating the process of urbanization. This sets the stage for the third stage of structural transformation, where the service sector becomes the leading sector, and the economy becomes increasingly knowledge based. As the economy transitions to a service-oriented focus, there is a marked upswing in education levels, and higher-skilled jobs become the norm.

As mentioned above, the entire process of structural transformation is driven by many factors, including the quality of human capital and industrial policies. Although structural transformation can pose challenges, it should ultimately lead to significant improvements in the well-being of the population and overall economic progress.

What are the challenges to structural transformation in Africa?

This section will focus on key challenges inhibiting structural transformation in Africa, including the lack of diversification and value addition, low levels of productivity, limited market access, lack of sophisticated social safety nets and finally, weak governance. Though not exhaustive, the discussion on these challenges aims to holistically frame the socio-economic and policy landscape, particularly the lack of redistributive policies that have slowed down structural transformation on the continent.

The first key challenge facing many African economies in their pursuit of structural economic transformation is the lack of diversification and value-addition. Many African countries rely heavily on a narrow range of commodities such as the export of oil, minerals, and agricultural products, which makes them vulnerable to fluctuations in commodity prices and limits their potential for higher-value-added activities. For example, in 2019, oil exports accounted for over 90% of Nigeria's total exports, while minerals accounted for over 80% of Zambia's exports.[1] To drive structural transformation, many African countries need to create the enabling conditions and invest in industries that have higher productivity and generate higher value-added, such as manufacturing and services. Yet, Africa's manufacturing sector is small and underdeveloped, accounting for only 10% of the continent's GDP. In 2019, Africa's manufacturing value added per capita was $178, compared to $1,000 in South Asia.[2]

Another challenge is the exceptionally low levels of productivity in many African economies. The majority of Africans work in low-productivity agriculture, which accounts for 53%[3] of total employment. Moreover, according to a report by the International Labour Organization (ILO, 2019), the informal economy (both agricultural and non-agricultural) in Africa employs up to 85% of the workforce, making it essentially the real economy of the continent. The report further suggests that investments in the informal economy – where the bulk of the poor find their

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[1] https://data.worldbank.org/ (much of the data was generated from this open data world bank website).
[2] https://data.worldbank.org/
[3] https://data.worldbank.org/indicator/SL.AGR.EMPL.ZS?locations=ZG

livelihoods and entrepreneurial opportunities - have the potential to contribute significantly to productivity growth and poverty reduction in Africa. However, factors such as poor infrastructure (energy, roads, communication, digitalization), inadequate skills and education, and limited access to finance stand in the way of productivity-growth and value-addition. For example, only 43% of the population has access to electricity[4], a fundamental input into the structural economic transformation process.

A third challenge is the limited access to markets, both domestically and internationally. Many African countries have small and often informal domestic markets, which limit opportunities for economies of scale and hinder the growth of industries. In addition, many African countries face barriers to trade and limited access to international markets. Addressing these challenges requires investments in trade facilitation, the development of regional markets and value-chains, and the negotiation of trade agreements that benefit African countries.

Another key challenge is the lack of social safety nets and more importantly inadequate social protection for vulnerable and excluded populations. This limits their ability to participate in economic activities and hinders efforts to achieve inclusive growth. To address this challenge, African countries need to invest in social protection programs that not only provide a safety net for the poor and vulnerable, but also serve to improve the prospects for economic inclusion and equality of opportunity including through social transfer schemes. Gender disparities in education, employment, and access to resources remain a significant challenge in many African countries. For example, in Sub-Saharan Africa, only 41% of women participate in the labor force, compared to 73% of men.[5]

Finally, lack of enabling governance remains a major challenge to economic development in many African countries, which undermines growth and poverty reduction by diverting resources away from productive activities and towards rent-seeking. To achieve structural transformation, African economies will increasingly need to find ways to improve governance by introducing conducive regulatory and legislative frameworks, strengthening institutions for their implementation, and promoting transparency and accountability.

Why should Africa focus on structural transformation for driving inclusive and sustainable industrialization for poverty eradication?

To discuss the significance for driving inclusive and sustainable industrialization for Africa's poverty eradication pursuits, it is first essential to understand the crux of this approach. Inclusive and sustainable industrialization means the process of developing and implementing industrial activities that foster an innovative integrated approach to social-economic inclusion, environmental sustainability, and economic growth.

In essence, inclusive industrialization strives to ensure that the advantages of industrialization are equitably distributed throughout society, irrespective of gender, ethnicity, or socio-economic status. This necessitates the promotion of equal access to economic opportunities, education, technology, and training, as well as the safeguarding of workers' rights, health, and safety. Conversely, sustainable industrialization seeks to limit the environmental impact of industrial activities while promoting green growth. This entails employing cleaner production methods, minimizing waste and pollution, shifting to cleaner, renewable sources of energy as well as harnessing the potential for green commodity industries.

Through the combination of both inclusive and sustainable approaches, industrialization can pave the way for a more just structural transformation which allows inclusion and sustainability to be pursued simultaneously while stimulating growth and job creation. In this manner, structural transformation enables countries to transition from

[4] https://databank.worldbank.org/source/world-development-indicators
[5] https://data.worldbank.org/

a low-productivity and narrow-based economy to a more diversified one that is more resilient to external shocks. Diversification can promote inclusive and sustainable industrialization, generating opportunities for growth and job creation in new and emerging sectors. Structural transformation can raise productivity by facilitating the transition from low-value-added activities to high-value-added sectors such as manufacturing and services. This can lead to higher wages and poverty eradication. With the increasing availability of cleaner technologies, reducing waste and emissions, and promoting resource efficiency, structural transformation can be promoted towards a greener pathway. Moreover, with the abundance of natural resources and access to sustainable practices in Africa, there is tremendous potential for promoting green commodity value-chains (such as in agriculture, forests, and fisheries). This can help eradicate poverty and support the achievement of the Sustainable Development Goals by promoting the transition to more sustainable forms of industrialization. Such an integrated approach can stimulate inclusive growth by providing employment and income-generating opportunities for the poor, excluded and marginalized groups. By providing access to new and emerging sectors that are more productive and offer higher wages, it can also reduce inequality.

Put differently, structural transformation can be a critical driver of inclusive and sustainable industrialization and poverty eradication. By encouraging economic diversification, increasing productivity, promoting sustainable industrialization, and fostering inclusive growth, structural transformation can help to promote inclusive growth and support the achievement of the SDGs.

In Africa, there are shining examples of countries forging a path towards inclusive and sustainable industrialization through structural transformation. Take Ethiopia, for instance, which has made significant strides in recent years with a resolute focus on industrial development. The country has gone to great lengths to bolster its infrastructure, erecting industrial parks, and expanding its transportation network. By doing so, Ethiopia has piqued the interest of foreign investors, who have invested in industries like textiles, leather, and food processing. This has not only created new job opportunities but also made inroads into poverty reduction.

Meanwhile, Mauritius whilst known for its service centers such as financial services and tourism, has undergone a transformation, turning from a low-income, agrarian economy into a thriving, middle-income economy with a robust manufacturing sector. This transformation has been driven by a heavy investment in education and training programs designed to hone the skills of its labor force, along with infrastructure and technology that supports economic growth. On top of that, Mauritius has made a strong push towards sustainable development, investing in renewable energy and eco-tourism industries.

Rwanda too has embarked on a mission of structural transformation, with an eye towards promoting inclusive and sustainable industrialization. Through a heavy investment in education and training programs that upskill the labor force and attracting foreign investment to develop its manufacturing and service sectors, Rwanda has made strides towards its goal. Additionally, it has championed green industries like eco-tourism and sustainable agriculture to promote inclusive green growth.

Lastly, Ghana has a rich history of pursuing structural transformation, diversifying its economy by modernizing its agricultural sector. Starting with primary industrialization in early to mid-1960s, the country introduced ISI policies for light manufacturing for the domestic market. Despite limited diversification, Ghana, through a concerted effort, has now established a strong manufacturing sector, particularly in textiles and food processing, and has drawn foreign investment to these industries. Ghana has also pursued inclusive green growth, investing in renewable energy and eco-tourism.

Though each of these countries has encountered their own set of obstacles and triumphs, they are all united in their steadfast commitment to investing in education and training, promoting innovation, and developing green industries. By adhering to these principles, they are forging a path towards long-term inclusive and green growth, demonstrating that the pathway to inclusive and sustainable industrialization is one is increasingly possible in Africa.

What integrated policy approaches are needed for inclusive and sustainable industrialization for poverty eradication in Africa?

It is vital to first provide further background and rationale for the integrated policy approaches needed for inclusive and sustainable industrialization for poverty eradication in Africa. Drawing on experiences and lessons from other parts of the world, it becomes clear that African nations face significant challenges in promoting structural economic transformation with inclusive growth[6]. The crux of the issue lies in the fact that such transformations, which involves shifting from traditional agriculture to modernized agriculture, industry, or services, often results in a rise in inequality and can exacerbate poverty. This is because access to education, skills, and other resources varies widely among individuals and groups, and the playing field is often not level. As inequality increases, it can hinder inclusive growth and social cohesion, and even lead to political instability and conflicts. Therefore, it is imperative that African countries find ways to balance the goals of growth and inequality reduction, while also managing the trade-offs between growth and inequality. To address this challenge, an integrated, systematic, and partnered approach is needed for structural economic transformation and inclusive growth.

In Africa, the winds of change are blowing, and the potential for inclusive and sustained prosperity is on the horizon. A transformational journey that begins with an integrated approach to policymaking, one that combines a range of measures designed to unleash the continent's immense potential.

At the heart of this approach is investment in infrastructure. For too long, Africa has suffered from a dearth of quality infrastructure, impeding the movement of people, goods and services and stifling growth. But by investing in critical infrastructure such as roads, ports, and power grids, governments can unlock the full potential of the continent's natural resources and promote investment in manufacturing and other productive sectors. In this, we must also be aware of the technological awakening that we exist in, and work towards harnessing the benefits of digitalization as an opportunity to catch up and leapfrog through structural transformation.

Equally important is the design and implementation of industrial policy, which involves government intervention in the economy to encourage industrialization and diversification. Tax incentives, subsidies, and trade protectionism can be used to spur the development of targeted sectors such as manufacturing and technology, creating new sectors and industries including to support global green transitions for growth and employment. Successful transitions will require **innovation** and the harnessing of digital technologies in all levels of the economy.

But a transformational journey cannot be undertaken without a skilled and educated workforce, one equipped with the skills needed for the modern economy. This is where human capital development comes in, with governments ***investing in education and training programs to equip their citizens with the tools*** they need to compete on the world stage.

[6] Inclusive growth refers to economic growth that benefits all segments of society, particularly the poor and marginalized groups of concern. It is used as synonymous with poverty and inequality reduction.

Agriculture and natural resources remain a critical sector in Africa, employing the majority of the population and providing a significant portion of export earnings. By investing in agricultural and natural resource transformation policies such as mechanization and research and development, governments can boost productivity, create new jobs, and spur economic growth particularly in ***agro-processing, development minerals as well as textile industries***.

The financial sector is also a critical constraint for small and medium-sized enterprises in Africa. To promote financial sector development, African governments must ***create conducive regulatory environments, expand access to credit, and promote the development of capital markets***. The previous economic crises have also demonstrated the importance of monetary policy in influencing economic growth. For example, India and Nigeria, through their ‘’Priority Sector Lending” approach post COVID-19, have shown that policy instruments coupled with innovative finance can protect key economic sectors from severe external shocks and inherently, propel structural transformation.

Regional integration can be a game-changer in promoting structural transformation by creating larger markets, facilitating trade, and attracting investment. By eliminating trade barriers and harmonizing standards and regulations, governments can create a more conducive environment for industries to grow and thrive.

At the heart of the inclusive and sustainable industrialization approach lies social protection for enhancing human capital and empowering individuals to gain equal access to economic opportunities. At one end, social protection instruments such as safety net programs, play an instrumental role in building resilience to shocks and crises for all in Africa. Social protection must also play an instrumental role in just structural transformation by enabling the poor, marginalized, and excluded to gain access to resources such as skills, training, credit, and technologies that can improve their access to economic opportunities. Simultaneously, social transfers and re-training programmes are needed for workers who find themselves displaced by structural transformation processes.

Taken together, such policies, tailored to each country's unique context, can form the basis for an innovative integrated approach to promoting structural transformation for driving inclusive and sustainable industrialization in Africa. However, ***international cooperation and partnerships will be essential for supporting structural transformation and inclusive and sustainable industrialization in Africa***. By facilitating technology transfer, expanding fiscal space, capacity building, and policy coordination, international cooperation can help to promote inclusive and green growth by making policy investments possible.

Conclusion

Inclusive and sustainable industrialization and poverty eradication require a vital component: structural transformation. Effectively implemented, this transformation can fuel economic growth, generate employment opportunities, and reduce poverty and inequality. However, as highlighted, structural transformation can also produce negative social and economic outcomes if executed without proper consideration for the poor, excluded and marginalized groups.

In order to promote inclusive growth and reduce poverty and inequality, policies must be implemented in a manner that takes into account the needs of all members of society. This necessitates not only policies that promote investment in human capital, support small and medium-sized enterprises, and encourage sustainable industrialization. But also, policies that are committed to promoting socio-economic inclusion through social protection measures and levelling the playing field.

The significance of structural transformation for inclusive and sustainable industrialization and poverty eradication cannot be overemphasized. It is a critical element in the efforts to achieve the SDGs and ensure that economic growth benefits all members of society. By collaborating and building partnerships to implement policies that promote inclusive growth and account for the needs of all members of society, all stakeholders can play an instrumental role in constructing a future that is prosperous and equitable for all in Africa.

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