

## Economic Report | Labour Market

### Working Hard or Hardly Working?

Economic Snapshot			
August 2016 Inflation Data/Indices			
	MoM	YoY	Prev YoY
<b>Headline</b>	1.0%	17.6%	17.1%
<b>Food</b>	1.2%	16.4%	15.8%
<b>All Items Less Farm</b>	0.9%	17.2%	17.0%
<b>Imported food</b>	1.0%	20.7%	20.4%
<b>Energy</b>	1.2%	30.4%	30.0%
Currency Markets			
	Latest	Daily Chg	YTD
<b>USDNGN</b>	315.25	-0.1%	-58.2%
<b>EURNGN</b>	353.58	-0.1%	-63.4%
<b>GBPNGN</b>	402.81	-0.5%	-37.2%
<b>JPYNGN</b>	305.00	0.3%	-83.7%
Monetary Aggregates – August 2016			
	(₦'bn)	MoM	YoY
<b>M2</b>	21,647	-2.4%	17.1%
<b>CPS</b>	22,664	1.3%	21.6%
<b>NCG</b>	3,291	18.2%	19.2%
<b>NFA</b>	7,623	0.8%	38.6%
<b>NDC</b>	25,955	3.2%	21.3%
External Position			
	Latest	QoQ	YoY
<b>Trade Balance (\$'mn)</b>	-1,292	165%	131%
<b>External Reserves (\$'mn)</b>	24,596	-5.9%	-18.0%
<b>Foreign Debt (\$'mn)</b>	10,718	0.9%	10.4%
Growth Data – Q2 2016			
	(₦'bn)	% of total	YoY
<b>Real GDP</b>	16,102	100%	-2.1%
<b>Agriculture</b>	3,636	22.6%	4.5%
<b>Oil</b>	1,332	8.3%	-17.5%
<b>Services</b>	6,003	37.3%	-1.8%
<b>Wholesale and Trade</b>	2,834	17.6%	0.0%
<b>Manufacturing</b>	1,602	10.0%	-3.4%

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Over the last 6 months, Nigerian corporates have responded to the economic headwinds and slowing demand by restructuring their operations and pruning workforce with the National Bureau of Statistics (NBS) reporting 879,000 people lost their jobs in H1 2016. Complicating the labour market scenario is the expansion in the economically active population and in the participation rate. Given the correlation between higher unemployment and socio-political unrest, beyond setting constraint on GDP growth, the rising unemployment also stokes uncertainty around investment in Nigeria. The latest labour market data from the National Bureau of Statistics covers the period from April to June 2016—the period in which the economy officially entered a recession.

### Weak labour data crowns deplorable macro milieu

In line with the weak stream of macro-economic data over H1 16, the NBS reported deterioration in Nigeria's labour market with the unemployment and underemployment rate climbing 120bps and 20bps QoQ to 13.3% and 19.3% respectively in Q2 16.<sup>1</sup>

Unbundling the report, labour market slack stemmed from continued increase in labour force (YoY: +7.9%, QoQ: +1.8%) as well as a decline in the number of people in full-time employment (YoY: -1.4% YoY, QoQ: -0.7%)<sup>2</sup>.

<sup>1</sup> Under the old NBS measurement Q2 16 unemployment is 32.6%.

<sup>2</sup> First decline in full-time employment since the introduction of the new unemployment classifications in 2015

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The cutback in labour demand mirrors underlying weakness across segments of the economy with companies in recession hit Manufacturing (-3.36% YoY)<sup>3</sup>, Industrial (-9.53% YoY), Construction (-6.3% YoY) sectors, responding by slashing head count. Over the period, the NBS reported that a further 351,000 people lost their jobs in Q2 16 which extends a pattern from Q1 16 when circa 528,000 jobs were lost.

On the supply side, expansion in labour force emanated from an increase in the participation rate (+340bps YoY, +90bps QoQ) to 74.9% as more individuals in the working group between the age of 15-24 (+12.6% YoY) and 25-34 (+11.7% YoY) came into the labour force<sup>4</sup>.

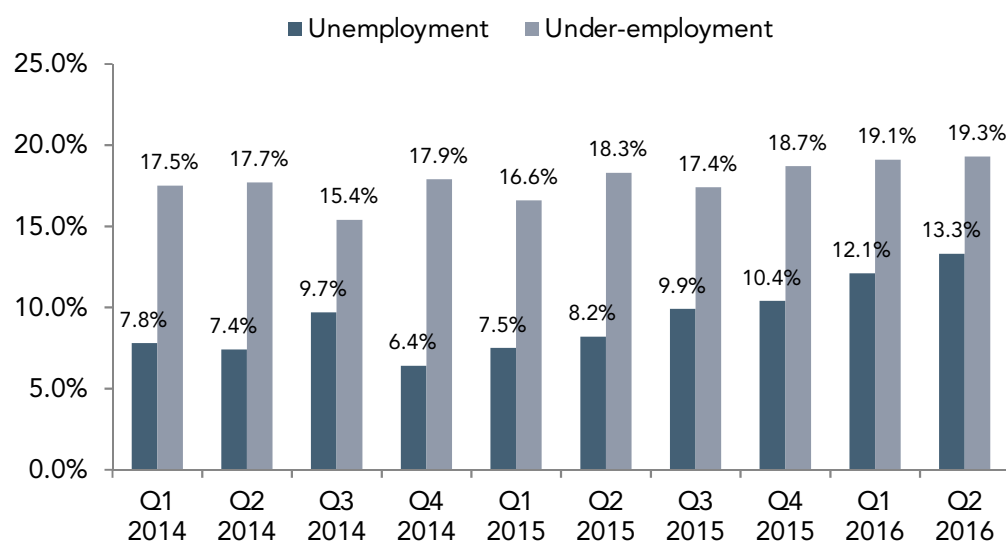
Nonetheless, as there were not enough jobs to absorb these individuals (15-24 and 25-34), unemployment rate for the two age cadres expanded 910bps and 560bps YoY to 24.5% and 14.5% respectively. Using attribution analysis to examine unemployment data based on educational groupings, the expansion in labour force stemmed from individuals with post-secondary education (+19.4% YoY). Again, not enough jobs to absorb this class meant that unemployment rate for the group jumped 14pps YoY to 23.5%. However, underemployment figures from individuals with post-secondary education expanded 12.8% YoY to 2 million, though the faster rise in labour force from this category (+19.4% YoY to 11.8 million) led to a decline of 100bps in underemployment rate by 1pps YoY to 17.2%. To add, the decline in the number of people not in the labor force by 2.6% QoQ (-9.3% YoY) alongside a 1.8% QoQ (7.9% YoY) increase in the labor force indicates that more people who previously were not economically engaged are now deciding to look for work. In summary, the unemployment report is that the Nigerian labour market is unable to cater for increasingly more people looking for work even as the recessionary conditions across sectors of the economy is leading to job losses.

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<sup>3</sup> Albeit at a slower rate compared to the 7.0% YoY contraction in Q2 16

<sup>4</sup> These two age groups account for half of the labour force

**Figure 1: Trends in unemployment and underemployment rate**

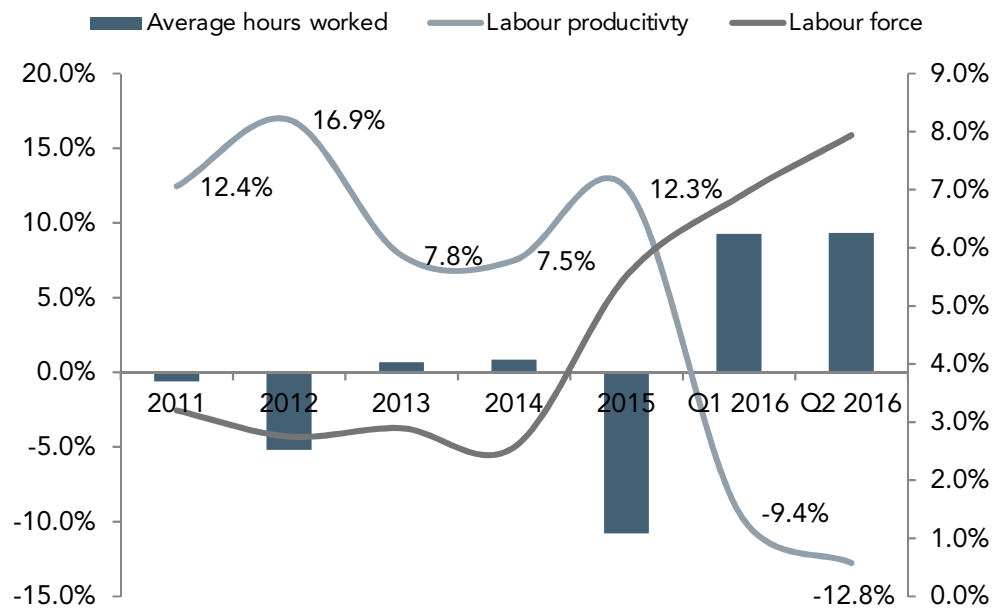


Source: NBS, ARM Research

### **Slowing productivity highlights labour market disequilibrium**

Completing the round-up of weak labour data, the NBS also reported that labour productivity, measured in GDP per hours worked, declined 12.8% YoY. The contraction reflects a quicker rise in hours worked (+18% YoY) relative to output (+2.9% YoY). Growth in total hours worked stems from expansion in labour force and above trend growth in average hours worked (+9.3% YoY). Robust growth in hours worked despite severe bouts of fuel shortages during Q2 16 is largely flattered by base effects from 2015—when fuel scarcity, combined with a heightened election season in H1 15, drove compression in average hours worked (-10% YoY).

**Figure 2: Growth rate in hours worked, output and labour productivity**

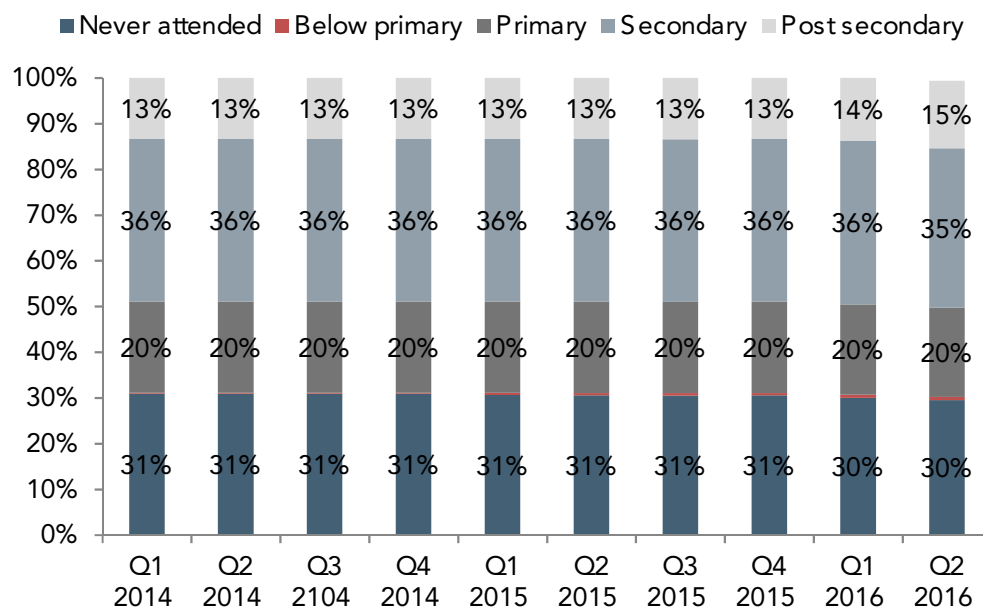


Source: NBS, ARM Research

The weak productivity performance could be seen as the consequence of a slower output growth and faster rise in hours worked. As a matter of simple arithmetic, the new highs in hours worked and a failure for output to surpass growth in hours worked means labor productivity is lower - the total number of hours worked increased by 18.0% YoY while real nominal GDP grew by 2.9% YoY. An increase in the number of hours worked can be regarded as a feed-through of a tight labor market, stemming from higher inflation and lower corporate profits. Despite paucity of data to make direct inferences to the numbers, lower productivity has generally been known to be root causes of lower business and capital investment, significant declines in foreign direct investment and poor economic growth. Given that only 15% of the labour force possess post-secondary education whereas the high skilled sector of the economy -- Services (37%) constitute the lion share to GDP even as Real Estate sector (7.5%) -- another high skilled sector tracks closely to Crude Oil GDP, points towards a structural mismatch. More clearly, labour supply, is dominated by low skilled workers, and is set against an economy which produces output requiring high skilled workers. Beyond the concerns over labour quality, Nigeria's infrastructural constraints, a fall-out of low investment implies lower capital

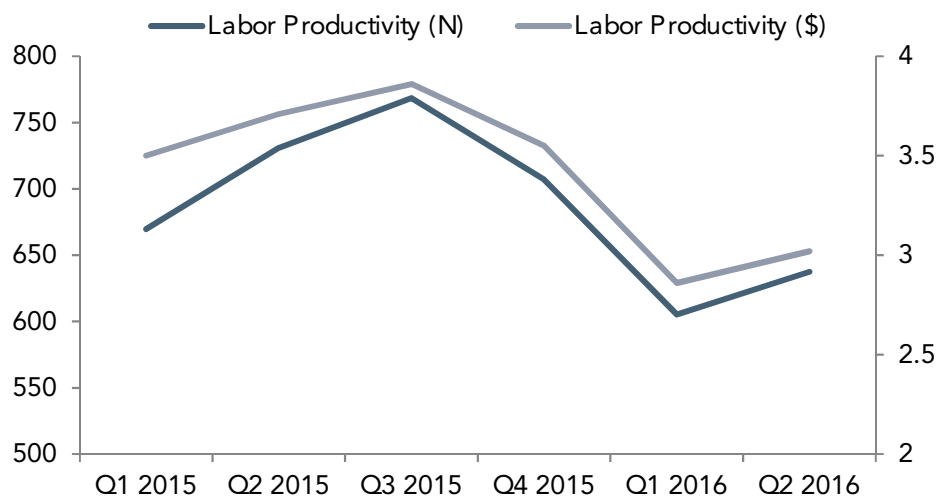
per worker ratio and accounts for gap in labour productivity to peers<sup>5</sup>. Put simply, the burden of sustaining national output rests on poorly equipped individuals.

**Figure 3: Labour force by educational classification**



Source: NBS; ARM Research

**Figure 4: Labour Productivity Trend in (Naira and USD)**



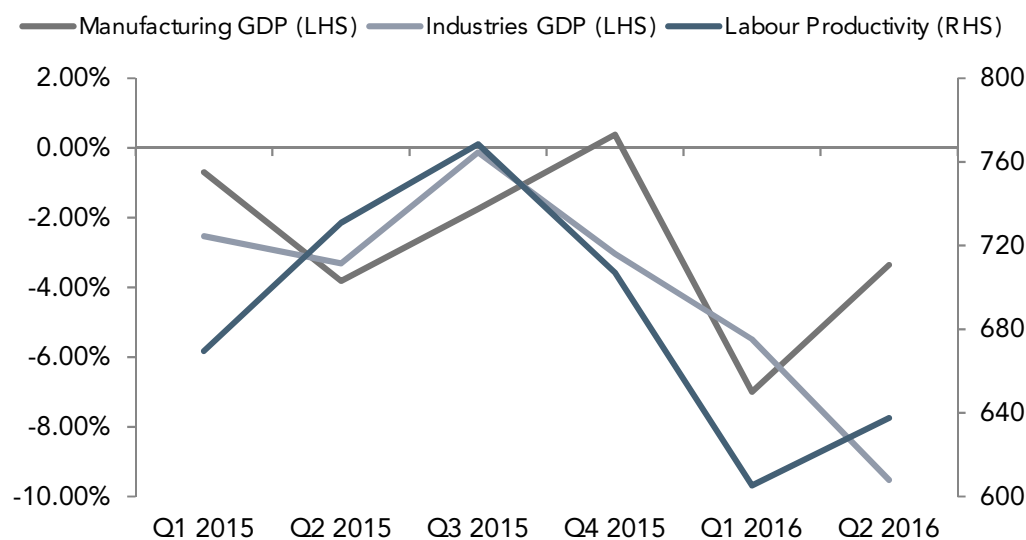
Source: NBS, ARM Research

<sup>5</sup> In dollar terms, Nigeria's labour productivity at \$3./hour trails peers: South Africa \$19.3/hour, EM average: \$23/hour

## Smoke on the water, Fire in the sky

The snags get more worrisome when matching the numbers. At first, NBS report further points out that only ~ 14% of Nigeria's labor force population has post-secondary education while nearly half of domestic output is being driven by low skilled employment and underemployment. In another twist, the poor productivity number manifests as a striking paradox when overlaid with the structure of the economy. Specifically, given significant weight of services (37%) and manufacturing (10%) in the nation's GDP basket, the mismatch between low productivity and a largely tertiary economy—as implied by Services' domination—is in stark contradiction to the directly proportional relationships between productivity and economic development stage in most countries. What this posits is that a large chunk of the entire value adding segment of the economy which should serve as the bridge between raw inputs and final output is hardly existent or slowing. This, as we had always highlighted, is also indicative of the real loss from challenging sectors like manufacturing and industries. In particular, currency woes, inadequate power, access to capital, and lack of infrastructure have frustrated manufacturing activities over the period.

**Figure 5: Labour Productivity (NGN) vs. Manufacturing and Industries GDP (%)**



Source: NBS; ARM Research

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That said, the likelihood of the currently negative GDP growth rate, amidst significant macro headwinds to stoke further productivity concerns continue to ascent. We align with the view that productivity is likely to remain in a soft trend in coming quarters as output continues to contract' albeit at a modest pace and hours worked continue to move ahead. The pace of productivity growth is a critical ingredient in determining the rate of growth for worker pay, consumer prices and the economy as a whole. Weak productivity growth, or continued outright declines, could restrain worker pay, corporate profits and overall economic growth in the coming years. We find that more jobs are needed today to hold the unemployment rate steady than in previous cycles, and therefore the economy will continue to be hit by a downtrend in hiring pace.

To add, the outlook for job growth remains shaky given our GDP expectation (FY 16: -1.3%), this perturbing outlook even gets more pronounced for the urban related sectors which continues to falter with Q2 numbers affirming the gloomy outlook— underemployment rate for the labor force with post-secondary education (most qualified workers) fell to 17.2% (Q1 16: 19.8%) whereas unemployment rate for the group rose from 23.2% (Q1 16: 15.6%).

As said earlier, this persistent slower productivity most likely reflects the subpar pace in capital and investment spending given economic challenges. Assuming capital and investment spending picks up, the productivity numbers is likely to show some recovery. Stronger productivity would help to improve the standard of living and drive corporate profits. If productivity growth fails to strengthen, the implications over time will be significant. Adding further anxiety for investors, softer labor force growth and slower productivity growth appear to be the new phenomenon.

### **Challenging the status quo requires policy stimulus**

Beyond immediate efforts to kick-start economic growth to ensure resumption in job creation, the challenge for policy makers is to find means of addressing the issue of the labour market disequilibria and the challenge of improving labour-capital ratio to boost productivity. In seeking to tackle the unemployment milieu, the solution must include expanding the capacity/quality of the country's educational systems to

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upskill labour force and re-calibrate the economic structure towards sectors with higher low-skill labour requirements. On this wise, the need for fixing the infrastructure and logistic bottlenecks which constrain both sectors, stresses the need for long term financing at lower rates. Productivity is determined by a mix of supply and demand side factors while most productivity gains come from the private sector of the economy. Thus, the focus of policies should be about making businesses and markets more competitive – effective demand-side policies will be needed to sustain a higher level of aggregate demand to keep the level of capacity of utilization high. Combination of policies (fiscal incentives and supply side interventions) will be more effective to boost the level of capital investment (as a % of GDP).

For monetary policy, as the CBN does not have a dual mandate of price stability and full employment like some global central banks, the weak unemployment numbers do have a direct impact on policy trajectory. That said, our aforementioned position about the need for supply of long term funding at lower rates implies that the apex bank has an indirect role to play in supporting structural reforms to the labour market. Overall, the scenario calls for stronger fiscal policy action to address the skills gap deficiency and recalibrate the jobs market to match current reality.



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