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Livelihood Diversification in Developing Countries

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LIVELIHOOD DIVERSIFICATION IN DEVELOPING COUNTRIES[1 & 2]

1. What is the issue and why is it important?

It has been realised for some time that rural people do not specialise in crop production, fishing, forest management or livestock rearing to the exclusion of other sources of income. Rather they combine a range of activities and occupations to construct a diverse portfolio[3] of activities (Dercon and Krishnan 1996, Ellis 2000, Unni 1996. Although few longitudinal studies exist, there is general agreement among scholars that occupational diversification and the proportion of non-farm income in household income are increasing.

While the potential importance of non-farm occupations for poverty reduction is well recognised among governments and donors, most of the efforts have been aimed at creating such opportunities ***in situ***: In addition, there it is also widely believed that an important driver of the rural non-farm economy (RNFE) is agricultural growth. The focus has therefore remained on increasing farm incomes and supplementing this with efforts to enhance skills, improve access to credit and productive assets which would enable poor people to diversify into small enterprise, trade and agro-processing etc. However recent research on rural livelihoods has shown that many non-farm occupations are closely linked with ***urban*** areas. The synergy between agricultural production and urban based enterprises is key to local economic development and, at a wider level, to more pro-poor growth (Tacoli 2004). It is also becoming more apparent that many non-farm occupations, especially those pursued by people who live in ***marginal areas***[4]., are actually ***situated*** in urban locations and, in the absence of prospects for substantial increases in farm incomes locally, are providing an important livelihood source.

Underpinning this trend, are the interlocking ***logjams of disadvantage*** that characterise many marginal areas; a combination of mutually reinforcing environmental, physical, institutional, social and political factors that trap people in low agricultural productivity as well as low levels of diversification with few prospects for exiting poverty. But policies remain curiously ill-informed

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2. Further information on this topic is available on the POVNET website under http://webdomino1.oecd.org/COMNET/DCD/PovNet.nsf).

3. Livelihood diversification is defined as the process by which rural families construct a diverse portfolio of activities and social support capabilities in their struggle for survival and in order to improve their standards of living (after Ellis). Here we use the term to indicate diversification away from farm income to off-farm and non-farm sources.

4. According to IFPRI some 1.2 billion people live in less favoured areas. While LFAs may not be exactly the same as marginal areas, there are significant overlaps as also with low potential areas, remote rural ares, poorly integrated and weakly integrated areas. These terms are often used synonymously.

about such constraints and also associated ***spatial diversification*** patterns. Policies are also ill-equipped in supporting ***multi-locational livelihoods***. Part of the problem is the inadequacy of official statistics in understanding diversification patterns by social group and capturing part-time and seasonal activities. Another problem is that mobility and informal sector activities, both of which are important in livelihood diversification, are actively discouraged by many governments in an effort to control urban "explosions".

The objective of this paper is to stimulate debate about the importance of diversification in poverty reduction, agricultural development and economic growth. It argues for:

- A broader entry point for poverty reduction that is multi-sectoral instead of a sole focus on increasing farm incomes;
- The need for a better understanding of market and non-market constraints faced by the poor in marginal areas;
- A greater recognition of the role of mobility and rural-urban links in poverty reduction and regional development in marginal areas.

2. The current evidence: what we know so far

A number of empirical studies across Asia and Africa have established that occupational diversification levels are much higher and more complex than official statistics indicate. According to Ellis the reliance on non-farm income sources in sub-Saharan Africa ranges between 30% and 50%; but it may attain 80–90% in southern Africa. In south Asia, on average, roughly 60% of rural household income is from non-farm sources[5]. Among the important determinants of RNFE are agricultural development and access to productive assets, infrastructure, proximity to urban centres and markets and education levels. However, diversification patterns vary substantially by country and regions within countries, making generalisations difficult and not particularly helpful for designing interventions.

Diversification, risk management and poverty reduction

What is clear is that diversification helps to reduce risks, especially those related to ***seasonality*** in rainfed agriculture. Furthermore, diversification can be a part of a household strategy of combining sequentially or in parallel activities that contribute to the accumulation of wealth at different points in the life cycle of the household.

Diversification is also a response to ***new risks***; especially those related to:

- A trend towards smaller landholdings and increasing landlessness as population pressure increases;
- Growing environmental risks (persistent drought, falling groundwater levels etc.);

5. Data from the National Council of Applied Economics research show that non-farm income contributed about one third (34%) of total household income in rural India.

- Structural adjustment policies: removal of agricultural price supports, reducing input subsidies, and rising user charges for public service delivery;
- Higher commodity price risks due to market liberalisation.

It has been postulated, especially through research in Sub-Saharan Africa and Latin America, that becoming less dependent on agriculture is part of the process of becoming better off. The poor and the better off may diversify to the same degree but the absolute level of non-farm income of the better off is several times that of the poor. Perceptions in South Asia have been rather more mixed: some studies note that non-farm incomes are lower and less reliable than agricultural incomes, particularly in marginal areas and that agricultural development is an important pre-requisite for more remunerative kinds of rural non-farm sector employment[6].

Rural-Urban links, agriculture and diversification

There is evidence from some locations that ***agricultural growth*** is a major ***driver*** of RNFE associated with, for example, agro-processing and equipment repair. Likewise a slowdown in agriculture can lead to a decline in RNFE activity. This has reinforced the view that investment in agriculture is the main route to poverty reduction. While this logic has been refuted through some studies on diversification in South Africa and Latin America where other sectors such as tourism have been drivers of RNFE, new research from India also shows that non-farm sector growth has not been dependent on the expansion of local agricultural productivity (Foster and Rosenzweig 2003)[7]. In fact ***urbanisation*** has been an important driver of diversification in recent years, offering many ***new opportunities***. The flow of money, goods and services between rural and urban areas can create a *virtuous circle* of local economic development by increasing demand for local agricultural produce, stimulating the non-farm economy and absorbing surplus labour (Tacoli 2004). But this is crucially dependent on three pre-requisites:

- access to infrastructure;
- trade relations/markets;
- market information.

The importance of infrastructure and the returns to investment in terms of poverty reduction are undisputed (Fan 2004). However the other two pre-requisites are rather more challenging in terms of offering easy policy solutions because of widespread ***market imperfections*** such as ***interlocked*** markets for credit, agricultural produce and inputs. Such imperfections tend to be weighed against the poor, especially in marginal areas so that they buy expensively and sell cheaply. Access to market information is equally problematic and suffers from ***elite capture*** in the same way as other assets and resources that are essential for diversification. The poor are thus ***adversely incorporated*** in the market and not free, rational players as neoclassical theories would assume. The challenge for donors and governments is to ensure that *markets work for the poor.*

6. See for instance Dev and Evenson (2003), NRI (2003).

7. Based on the analysis of National Sample Survey panel data for 15 states over 30 years.

In addition, there is widespread failure of services and institutions which combined with low levels of human, physical, natural and social capital create mutually reinforcing disadvantages (described by De Haan and Lipton as "*interlocking logjams of disadvantage*") which seriously constrain efforts to both improve agricultural incomes and, diversify Into non-farm occupations. It may also explain why non-farm occupations pursued by the poor living in marginal areas are often located in urban areas.

Mobility

A manifestation of this is the tremendous increase in temporary movements from marginal areas to access markets outside the village[8]. In countries such as China and India (important as they are the most populous countries, comprising 38% of the world population and more than a fifth of global agricultural GDP), remittances from urban areas have overtaken local agricultural income sources in several locations. Remittances can reduce overall vulnerability and poverty through a number of routes (improving access to food, transport, health services, investment in agriculture as well as non-farm enterprise and have contributed significantly to the reduction of poverty and vulnerability worldwide (Deshingkar and Grimm 2004). Policy makers need to be made aware of this so that they can think of ways of improving remittance mechanisms.

The Informal Economy

Many jobs in urban areas are in the ***informal*** economy which is expanding and larger than the formal economy in some places as in India where, according to Barbara Harris-White, it accounts for 60% of the GDP. The share of informal workers by sector and continent is shown in the table below.

Informal Workforce as a share of	**Africa**	**Latin America and Caribbean**	**Asia**
Non-agricultural employment	78%	57%	45–85%
Urban Employment	61%	40%	40–60%
New jobs	93%	83%	NA

Source: Becker 2004

Contrary to conventional wisdom, informal sector jobs do offer prospects for accumulation and exiting poverty because even if wages are not higher than rural areas, more work is available and there are unmatched opportunities for switching rapidly between different non-farm jobs

8. Close to a 120 million people were estimated to migrate internally in China in 2001 against a mere 458,000 people migrating internationally for work. In Vietnam roughly 4.3 million people migrated internally in the five years before the 1999 census whereas the numbers of international migrants was fewer than 300,000. In India too, internal migration numbers run into millions while international migration is only a fraction of this.

where entry barriers are low (e.g. security guards, street vendors, bicycle rikshaw pullers, house maids, porters, attendants, petty traders etc.)[9].

Segmented opportunity

However opportunity is not uniform; the heterogeneity of non-farm employment in terms of ***gender, ethnicity, and class*** is well known. For example men have done better than women especially in South Asia being more mobile and able to exploit better opportunities while women have been limited to low-paid local work. ***Education*** is a critical determinant of the type of work that is undertaken. Those with more education can enter high return enterprise and salaried jobs while those with less education often remain as subsistence farmers or work as casual, unskilled labourers in low wage labour markets. Discrimination related to ethnic group or caste also prevents many from gaining access to better paid jobs; this points to the need for a clear focus on the kinds of *non-market barriers* that are faced by the poor.

Official Statistics are unable to capture diversification fully

Official occupational and demographic surveys tend to miss out part-time and seasonal activities. This problem is partially related to using quantitative methods. For example quantitative data on diversification in the Indian state of Andhra Pradesh show very low levels of diversification among the poor. But qualitative methods show that many who report their primary occupation as agricultural labourer switch between local farm work and seasonal non-farm work such as hair-cutting, brick-kiln work etc. Also missed are *unregistered and illegal* activities as respondents are, understandably, reluctant to report them. While official data for 1994 suggest that non-farm occupations in AP are associated with being poor, multidisciplinary studies show that the richest have diversified into high return non-farm occupations such as informal money-lending. Similar patterns have been reported elsewhere in India. Similarly data on migration are notoriously inadequate as most cover only permanent moves and registered migrants.

3. Policy Concerns

Diversification has been found to reduce the vulnerability of poor households by smoothing seasonal income fluctuations and improving their resilience to shocks. But this rural reality is not reflected in policy which continues to treat rural people as mainly agriculture-dependent and sedentary. A key focus of development policy has therefore been to raise farm incomes. Added to this is the view that agricultural growth is the main driving force or “motor” for the RNFE.

Huge amounts of money are currently invested in improving productivity in marginal areas – for example in excess of $500 million is invested in watershed development projects in India. But recent evaluations have started to show that watershed development in itself is not *sufficient* to ensure rural livelihoods. There is also some evidence that landless labourers are better off than marginal farmers in locations where agriculture has become highly risky and urban labour markets have expanded. Given the fiscal, environmental, institutional, infrastructural and governance constraints in marginal areas that have shown little improvement over the years and are unlikely to change dramatically in the next 10-20 years, the goal of keeping people in rural

9. See Harris 2004, Phillipson 2004

areas seems elusive. On the other hand well supported rural-urban links can reduce regional inequalities through transferring some of the benefits of intensive agriculture, construction, and urbanisation to poorer regions.

As noted by other authors in this series, investing in infrastructure and human capital are important policy objectives (Hazell and Thompson 2004) and these could help to overcome some of the logjams of disadvantage referred to previously. Equally important is the need to strengthen local institutions by building capacity, financial devolution, upward and downward accountability (Tacoli 2004). But the enormous difficulties associated with overcoming entrenched social attitudes, corruption etc. should not be under-estimated. People's own efforts at diversification need greater recognition and there is a case to review investment policies that are trying to keep people in marginal areas. Investing in small towns and infrastructure such as cheap transport services and communication technologies should be a priority. The concept of supporting mobility is already accepted in some policy circles (for instance by the Club du Sahel and West Africa (SWAC); new Chinese policies on supporting mobility) but there is still a policy gap in many countries.

Another area for attention, though not necessarily for agriculture policy, is the role of the informal economy and its potential for poverty reduction. Many governments continue to regard it as a low-productivity sector that perpetuates poverty and all kinds of social ills. In fact many activities in the informal sector continue to be illegal because very few permits are issued. But because both demand for, and supply of these services are so overwhelming, they continue and support rent-seeking among petty officials and policemen that is of gargantuan proportions. There is a need to review government and donor policies to ensure that they are not hostile to the livelihood strategies pursued by a majority of the poor in the informal sector.

Knowledge gaps

There is an urgent need to improve the understanding of the kinds of market imperfections that have hampered the diversification efforts of the poor especially in marginal areas. This calls for different methods that move away from conventional household surveys, especially those that can understand the opportunities and constraints by gender, ethnicity, caste etc. since non-farm sector markets are so strongly segmented along these lines.

In sum, policy priorities are as follows:

At donor level

- Invest in less favoured areas but not in ways that stifle people's own efforts at diversifying away from increasingly risky agriculture and into more rewarding urban occupations;

- Support multi-locational livelihood strategies through investment in small towns, cheap transport services, accessible communication technologies;

- Enhance human capital through programmes on health and education but with due recognition of the implementation difficulties in marginal areas and a focus on women and other disadvantaged groups. Piloting of different modalities is important.

At government/policy level

- Move away from a single-sector focus to a multi-sector livelihoods approach by reorienting thinking within public institutions dealing with poverty reduction;
- Create the conditions for convergence between different line departments for agriculture, rural development, urban development, labour, especially at the local level;
- Decentralise service delivery and financial control putting in place effective mechanisms to ensure that local government is transparent and accountable;
- Identify locations where it makes sense to support mobility and where it makes sense to create jobs, recognising that these may be separate;
- Develop ways of regulating the informal sector without stifling entrepreneurial activity;
- Provide migrant support through more flexible schooling, food provision and health systems.

Private Sector/Business

- Invest in urban infrastructure in small towns;
- Invest in roads, transport and communication technologies.

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