SEP
Skills for Employment Programme

A1.2.6 M4P Analysis of Labour and Skills Market in Nepal

2019

In Collaboration with

Contents

Acronyms

AAER	Adopt-Adapt-Expand-Respond
ADB	Asian Development Bank
BIA	Business and Industry Association
CEHRD	Centre for Education and Human Resource Development
CF	Challenge Fund
CNI	Confederation of Nepalese Industries
CPSC	Colombo Plan Staff College for Technician Education
CSITC	Cottage and Small Industry Training Centre
CTEVT	Council for Technical Education and Vocational Training
DAG	Dis-Advantaged Group
DCSI	Department of Cottage and Small Industries
DFID	Department for International Development
DOFE	Department of Foreign Employment
ESC	Employment Services Centre
FNCCI	Federation of Nepalese Chamber and Commerce and Industries
FNCSI	Federation of Nepalese Cottage and Small Industries
FPTEN	Federation of Professional Training and Employment of Nepal
FPTS	Federation of Private Technical Schools
FWEAN	Federation of Woman Entrepreneurs' Association of Nepal
GESI	Gender Equality and Social Inclusion
HAN	Hotel Association of Nepal
ICT	Information and Communication Technology
IDMP	Investment Decision Making Principles
ILO	International Labour Organization
KOICA	Korea International Cooperation Agency
M&E	Monitoring and Evaluation
MEL	Monitoring, Evaluation and Learning
MOALD	Ministry of Agriculture and Livestock Development
MOICS	Ministry of Industry, Commerce and Supplies
MOCTA	Ministry of Culture, Tourism and Civil Aviation
MOEST	Ministry of Education, Science and Technology
MOLESS	Ministry of Labour, Employment and Social Security
NAFEA	Nepal Association of Foreign Employment Agencies
NGO	Non-Governmental Organization
NMEFN	National Micro Entrepreneurs Federation Nepal
NSTB	National Skills Testing Board
NVQF	National Vocational Qualification Framework
OJT	On the Job Training
PABSON	Private and Boarding Schools Organisation of Nepal
PPP	Public Private Partnership
PWD	People with Disabilities
RPL	Recognition of Prior Learning
SDC	Swiss Development Corporation
SEE	Secondary Education Examination
SEP	Skills for Employment Programme
SLC	School Leaving Certificate
TECS	Technical Education Community School
TITI	Training Institute for Technical Instruction
TM	Training Model
TOT	Training of Trainers
TTPs	Technical Training Providers
TVET	Technical and Vocational Education and Training
UNDP	United Nations Development Programme
VET	Vocational Education Training
VQF	Vocational Qualifications Framework
WB	World Bank

Executive Summary

Unemployment is a major problem in Nepal, and one that seems set to worsen in the coming years. As land has become saturated, farming practices have not kept up with the times; subsistence farming has become a less viable livelihood option for Nepal's youth. A poor educational system, a history of conflict and political instability compound these physical and demographic constraints. Young people chose not to improve their skillsets and employers face growth challenges because of a low skilled workforce. At the same time, slower job and wage growth (labour demand) in more skilled industries is not in-step with skilled graduates (labour supply), impelling many skilled people to migrate to developed countries for better job prospects, stability, and wages while leaving behind many semi- or unskilled workers. These factors often result in low incomes on migration, underinvestment in training, and poor labour productivity.

Development intervention in this area has tended to focus on direct training of individuals and support to government training systems. However, this has failed to achieve large-scale or sustainable results, as it has not altered the underlying causes of these poorly performing skilled development systems.

Issues in skills development exacerbate issues in the broader labour market in Nepal, which is dysfunctional, particularly at a regional level in more rural provinces. Here, infrastructure as well as several behavioural norms inhibit the effective placement of workers into jobs.

The UKaid Skills for Employment Programme in Nepal (SEP) is a DFID-funded development initiative which aims to overcome issues affecting labour and skills markets in Nepal with a view to creating jobs. Cognisant of problems with previous development intervention in the sector, SEP seeks to adopt a 'Making Markets Work for the Poor' (M4P) approach to analysis and intervention development. M4P is an approach that foregrounds sustainability and scale of impact by examining the underlying causes of underperformance and working with local actors to develop solutions in line with their own incentives and capacities.

This document is the M4P analysis of the labour market in Nepal and the skills development market, which is linked to it. It identifies several symptoms of underperformance including low quality of labour, and low wages in the labour market as well as low quality of training supply including the appropriateness of curricula and, in some geographical areas, low quantity of supply of training services. It identifies several underlying causes of these performance issues which lie in the supporting functions and formal and informal rules which affect these markets. In the labour market, these critical constraints include information on both the jobs that are available to labourers and the labour that is available to employers, while in the skills market, they include curriculum development, information on industry demand for certain skills, and the standardisation of qualifications to give employers and employees confidence in the skills they will receive.

This deliverable is part of a suite of documents that is a significant portion of the skill-strengthening component of SEP. These include a high-level view of the skills sector in Nepal (**A1.1.1**), a document identifying existing best practices in Nepal and abroad (**A 1.2.5**) and this M4P analysis which examines the skills and labour systems and offers approaches for consideration and adoption (through the life of the project) in response to these analyses (**A1.2.6**).

1. Background and Context

Nepal is a country with an agricultural past and present but one, which needs a secondary and tertiary future. Fertile lands have become fragmented, populations have grown, and productivity increases cannot keep pace with the resulting pressure. A poor educational system, a history of conflict and political instability compound these physical and demographic constraints. Nepal already has a high youth unemployment rate at 19.2% and the World Bank estimates over a quarter of a million additional jobs need to be created per year, just to maintain it at this level. The need, then, is clear. However, the root cause of the problem or viable ways to address them are not.

There are many reasons for the underperformance of the economy including the geopolitics of being sandwiched between two industrial giants in China and India providing huge competitive pressures. Nepal also has internal challenges to competitiveness. One of the major challenges is productivity, of both capital and labour. This can be seen in key sectors such as manufacturing, tourism, and commercial agriculture. To overcome these challenges, improving the labour market in Nepal is a key poverty reduction objective that must be addressed for the future prosperity of the country.

DFID have recognised this challenge and commissioned the Skills for Employment Programme (SEP) in order to address some of supply side issues in the labour market. Skills are not seen as an end in themselves but as a means to increase wages and create jobs in the labour market. The objective is to do this in a way that is both sustainable and large scale. As such, SEP will employ a Making Markets Work for the Poor (M4P) approach to understanding labour and skills markets and seek to intervene according to these principles. This document, using the other accompanying research undertaken during the inception phase, represents this analysis and demonstrates how SEP's interventions address critical constraints in the labour market in a sustainable way.

2. The Analytical Process

The M4P diagnostic process has five broad phases as outlined below. The first two of these phases have been coded into programme design and so are explained in brief here. Phases 3, 4 and 5 form the core of the analysis and so are described from a methodological point of view in Section 2 before being employed in Section 3 of this document for the core of the analysis. The way by which the data for the analysis is collected is summarised in **Figure 1** below.

2.1 Define the parameters of the programme

Development is a normative pursuit. As such, the funders of development determine what they want to achieve by investing in what they want to invest in. A market systems analysis requires that certain programme parameters are fixed in order to focus the analysis in the areas that will have the greatest impact. These parameters always include definition of a **development objective** and a **target group** for whom that objective is to be achieved. Further, specifications can be made in the form of **geographies of impact** and **sectors** through which that impact must be delivered.

SEP has defined its key development objective as an **increase in income and increase in formal or contract employment in key sectors, with preference for select geographies**. This is the key criterion which led to decisions about mechanisms to arrive here and these mechanisms are reflected in other intermediate indicators such as the skill levels of employees and the productivity of sectors. The target group is quantitatively defined as:

- For the skills component
    - At least 70% will be in 5 priority sectors for structural transformation,
    - At least 50% will be women, and
    - At least 40% will be from disadvantaged groups (including 500 of total component target for those living with disability to access employment).

In terms of sectors, the 'key sectors for structural transformation' have been defined as the ICT, tourism, commercial agriculture, light manufacturing, and hydropower sectors, as these are key economic drivers in Nepal and contributing to growth in these sectors is seen to have a potentially catalytic effect to broader economic growth. Provinces 2 and 5 have been accorded priority.

2.2 Verify the relevance, feasibility, and opportunity of intervention in different systems

Having defined what the programme is trying to achieve, this component of the diagnostic process seeks to identify or verify whether there exists the potential to generate the desired benefit in three ways:

Relevance: Are significant numbers of the target group present in these systems? At the highest level, SEP will address cross-cutting constraints affecting the labour market and as such, there are huge numbers of people to whom this is relevant. Of the 70% of projected impact within priority sectors, while they vary in terms of the number of people they do or could employ, all are deemed to be of relevance to a sufficient number of the target group to be of interest.

Opportunity: Are there key drivers of change which would make intervention in this system more likely to have impact? In the case of the priority sectors, this is the principal reason for their selection. In the case of the broader labour market, opportunity can be seen in the fact that both the labour market and the skills market which underpins it are unsophisticated and underdeveloped relative to their potential.

Feasibility: Are there any clear blockers which would make intervention in these sectors unlikely to deliver impact? The priority sectors have been prioritised according to government interest which means that the enabling environment is more likely to be permissive of intervention. Broader labour market intervention can often face feasibility challenges caused by informality and fragmentation, making impact difficult to get to scale. However, the skills market here provides a useful area of leverage to make broader and larger scale reform more feasible.

Methodology

Data collection methodology in M4P is iterative and contextually dependent according to budget, timeframe, and the feasibility of different tools. Generally, the deeper into the diagnostic process, the more intensive data collection becomes.

In this case, a review of existing literature related to the five selected sectors, different aspects of skill and labour markets in Nepal was conducted to gain an understanding of the current labour market situation, employment conditions, trends and patterns.

Key informant interviews were conducted with various stakeholders, including prospective applicants to the Challenge Fund. The purpose of these interviews was to understand: (i) the demand-and-supply relationships regarding employment opportunities (ii) the process of recruiting, selecting and preparing the workforce; (iii) the nature of involvement of government institutions in vocational training; & (iv) general information services relating to workplace training and hiring.

An in-depth firm survey covering 238 firms along with ideation labs and round tables with industry, providers and sector experts was successfully completed and has formed the foundation for the M4P analysis.

Figure 1: Data Collection Methodology

2.3 Understand how the system works

The objective here is to understand in what way the market is underperforming. M4P understands markets as a series of interconnected transactions. The principal market is the market where the target group can extract a benefit and they play the role of either supply (of labour or as producers) or demand (of goods and services).

The performance of this principal market is assessed by one of three dimensions, explained here for the labour market.

- Quality: Are the jobs of sufficient quality to meet the programme's needs in terms of working conditions, job satisfaction etc.?
- Quantity: Are there enough jobs available?
- Price: Are the wages paid for these jobs sufficient?

These three dimensions of underperformance can be seen as the symptoms of the problem. The causes, however, often lies in the broader institutional environment which dictates the terms of that transaction.

We refer to these as supporting functions and rules. **Supporting functions** are the actions that dictate the terms (price, quality, quantity) of the core transaction. They must be something that an actor does/ actors do.

Formal and informal rules comprise the remainder of the institutional framework and can be considered as

Figure 2: Principal Market System

legal, regulatory, and behavioural rules and norms which impact on the terms of the core transaction. Again, an actor will be involved in setting and enforcing them, which will be different in different settings. The structure of the market is captured in **Figure 2**.
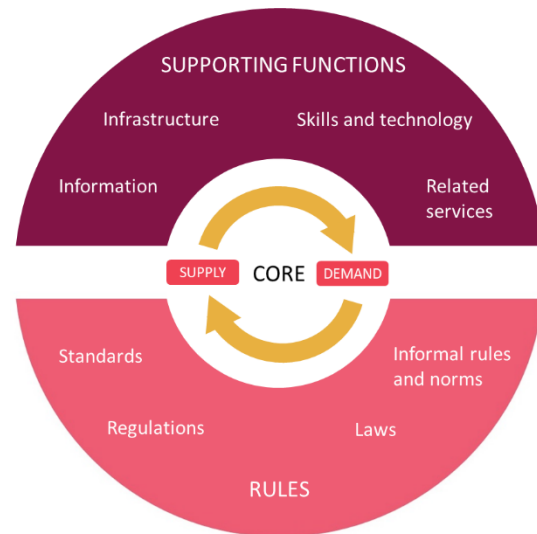
2.4 Understand the root causes of underperformance

Each supporting function or rule is also subject to its own transaction. Whether the supporting function is a particular type of information, drafting or enforcing of a law, or indeed skills, there is a supplier or producer as well as consumers. The terms of this transaction are also governed by different supporting functions and rules which, together, we call a support market as depicted in **Figure 3**. It is here where the root causes of underperformance often lie.

Figure 3: Markets and Support Markets

2.5 Develop interventions which address these causes in a way that will lead to large scale, sustainable impact

Having identified where the systemic constraints to improving the performance of the target systems are, a programme is charged with intervening in such a way that will lead to sustainable and large-scale change.

Building in sustainability

In order to intervene in a system in a way that is likely to deliver long-term impact, a programme must consider the **capabilities** and **incentives** of the particular actor to do so in the period after the programme support has ended.

Capabilities can be financial, physical or technical. If the programme has a role in providing any one of these capabilities in the short term, it is important to have a realistic vision of which actor has the ability to do it afterwards.

Incentives are far more complex and include financial, political, and intellectual among many others. Again, where a programme has a role in performing a function in the short term to generate impact, sustainability rests in the identification of an actor who has sufficient incentive to perform the role once the programme has ended its support.

Planning for scale
In designing an intervention, it is important to develop a vision of how this change will go beyond a programme-supported partner. Here, examining the transferral of information between actors is important and the mechanisms by which scale would be achieved. This is something which can be built into intervention design and should not be simply considered after an intervention has ended.

Challenge funds & market systems development
Challenge funding is an instrument used to generate ideas from the market to respond to a particular challenge. It is best suited to technical rather than structural constraints. In responding to a challenge fund call, actors are responding to their financial incentive in the short term – they are being incentivised for changing their behaviour in a given way. If that is to develop a particular product to which finance or risk are a

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Market Failure and Systemic Constraints

Market failure is a term from neoclassical economics that focuses on rationality of decision making in maximising economic returns to the entire group. It describes situations where a market is not Pareto efficient.

M4P is an approach derived from new institutional and behavioural economics that acknowledges complexity, irrationality, and, above all, the normativity of 'development'. As such, the problems we see in markets are not 'failures' as such, but constraints to the realisation of the improved outcomes we define for the group that we want to receive them.

M4P sees the 'market' as an institutional environment that produces a given outcome. It does not seek to separate government from the private sector in any normative way and, as such, separating out government and market failures belies the context specific and pluralistic solutions that emerge to improve development outcomes. M4P doesn't take a normative position on who should perform a given function but rather looks in an evidence-based way at what works. As such, 'systemic constraints' to the realisation of a particular outcome are favoured over terminology around market failures.

This represents a logical progression from the business case, the ToR and other analysis completed during the inception phase. The constraints represent a refinement and clarification on the market failures identified earlier. The constraints are also consistent with the expressions of interest received during the first round of the challenge fund. Applications respond to the constraints identified and, as detailed in section 5.4, it may be beneficial in the future to refine windows around the constraints.

Figure 4: Clarifying market failures and systemic constraints

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significant barrier, but which can subsequently be adopted by others, this can be very useful. If it is to improve their business model, then the barrier to them doing so is unlikely to be the absence of a programme call with matched funding.

SEP has been designed with a significant challenge fund component. This has to be carefully designed by diligently using the design of windows, selection criteria, and marketing tactics to ensure it has the highest potential to deliver systemic change.

Market Failure and Systemic Constraints
As noted in **Figure 4**, the problems we see in markets are not 'failures' as such, but constraints to the realisation of the improved outcomes we define for the group that we want to receive them. The constraints are also consistent with the expressions of interest that are being received during the piloting phase of the challenge fund.

3. Analysing Nepal's Labour Market

3.1 How the labour market in Nepal works and in what way is it underperforming

The sale of one's labour can be seen as a transaction. It has a supply side (your labour) a demand side (the actor who wants to buy your labour) and an exchange function (the factors that allow supply and

demand to meet). From the perspective of a development programme, we are usually looking at how this transaction is or isn't working for a particular group, which would usually be poor or underserved suppliers of labour.

In a market system, there are three dimensions of performance: quantity, quality, and price. In labour markets, that translates to the number of jobs, the working conditions of jobs, and the wage rate of jobs. In this respect, Nepal can be seen to be underperforming in the labour market in each of these regards from the perspective of the groups that DFID wishes to benefit from SEP. According to the Nepal Labour Force Survey 2018, the unemployment rate is 11.4% and Nepali employees earned an average of Rs.17,809 per month. However, gender disparities were obvious in the mean monthly earnings gap between males and females of Rs. 5,834 in favour of males.

3.2 The root causes of labour market underperformance in Nepal

The underperformance of Nepal's labour market (depicted in **Figure 5**) is caused by issues with supply, demand and exchange.

In terms of the *demand* for labour, these are primarily sectoral considerations which are beyond the remit of SEP in terms of intervention. Nevertheless, it is important to be aware of the factors affecting the supply of jobs because it can negate any efforts in skills development. These are effectively the factors effecting competitiveness, firm growth and investment in the target sectors. These will vary by sector but will likely include macro-economic conditions, availability of inputs, and the availability of skilled labour. The availability of skilled labour has a pro-cyclical relationship with job creation – if firms have better labour available, they will be able to grow and create more jobs, underlining the importance of skills development.
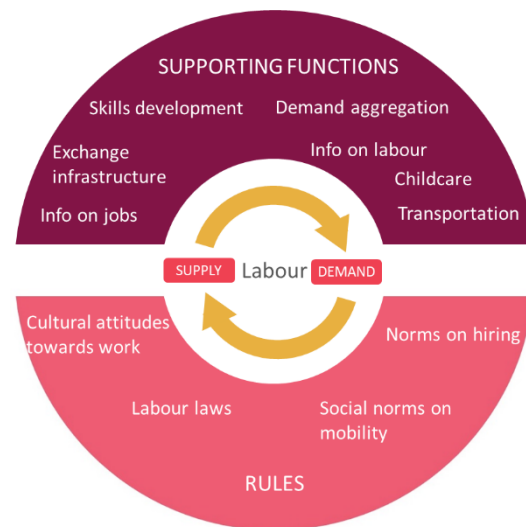
Figure 5: The Labour Market System

Causes of underperformance in the labour market related to the *supply* and *exchange* of labour are more relevant to SEP. Key supporting functions and rules here include:

Cultural attitudes towards work are of critical importance in determining the supply of labour for certain types of work. There are deficits in either the quality or quantity of supply of labour to jobs that might be considered only appropriate for people of certain castes or with certain qualifications.

Information on jobs and **information on labour** are two reciprocal functions that reduce the quantity and quality of jobs. In some cases there are suitably skilled personnel who aren't aware of available jobs, payscales, or conditions, whereas in others, there are employers who are not aware of the availability of suitably qualified labour.

Norms on hiring are an informal rule, particularly affecting the demand for labour with particular characteristics, such as persons with disability.

Social norms on mobility are an informal norm which have very formal consequences. Local migration has a distorting effect on labour markets. According to the firm survey conducted by SEP, Indian workers are ununionised and are not beholden to minimum wage laws, which means that the price, quality, and quantity of demand are all depressed.

There are also a range of supporting functions of *exchange* which impact the labour market. These include **transportation** enabling labour to access jobs and the **physical and digital infrastructure** which allows supply and demand for jobs to meet.

It is clear, however, that **skills development** is a supporting function which is of critical importance to the labour market in Nepal. As such, this is examined in detail as a support market in Section 4.

4. Analysing Nepal's Skills Development Market

4.1 How the skills development market in Nepal works and in what way is it underperforming

The skills development market in Nepal (**Figure 6**) is not adequately serving the interests of either the employers seeking qualified skilled labour or of the current and potential trainees who might look to upgrade their skills. The supply of training is performed by employers conducting in-house training, informal training by NGOs, and public and private training providers. Demand consists of employers requiring training services, as well as current and potential students. There are several interlinked problems affecting this transaction.

The quality of supply is low. Quality of human capital can always be improved and the opportunity to do so here is clear. Training by public, private, and civil society actors is not of sufficient quality to satisfy employers or trainees. It does not deliver appropriately skilled individuals nor does it provide the options attract trainees.

The quantity of supply is low. In some cases, a given type of training is simply not available in certain areas or to certain people. These access constraints affect remote regions and PWDs in particular.

The quantity of demand is low. For many courses, the potential trainees don't see the value of the training having seen their peers receive training without it resulting in a job. From employers too, having received underqualified graduates, demand for training services is low.

The quality of demand is low. Quality here refers to *who* requires training, both trainees and employers. Here, there is a quality problem. Better quality potential trainees prefer to head abroad to receive higher wages leaving the pool of candidates for training programmes in Nepal as students with lower potential. Employers too can receive better value for money by obtaining employees from overseas. Therefore, those employers seeking training services in Nepal are those paying lower wages and offering worse conditions.

The product of these flaws in the system are evident. Some estimates say that nearly 36% of the unemployed youth force in Nepal is not connected with economic production and skills (GoN, 2015). Nepal's TVET system was created to help bridge the skills gap and comprises formal, informal, and non-formal education, but despite numerous providers, an estimated 62% of youth cannot access TVET. The World Bank has estimated that if the investment-to-GDP ratio, growth of human capital, and growth of productivity stay at recent historical averages, Nepal's potential or trend rate of growth would slow to an average of just 3 percent per year from 2017 to 2030 (World Bank, 2017). This indicates that there is a need to improve the productivity of the workforce across the country.

4.2 The root causes of skills development market underperformance in Nepal

The drivers of underperformance in skills development are many. SEP's role will be in experimenting to see which of these constraints can be resolved in a sustainable way in order to ultimately improve the functioning of the labour market.
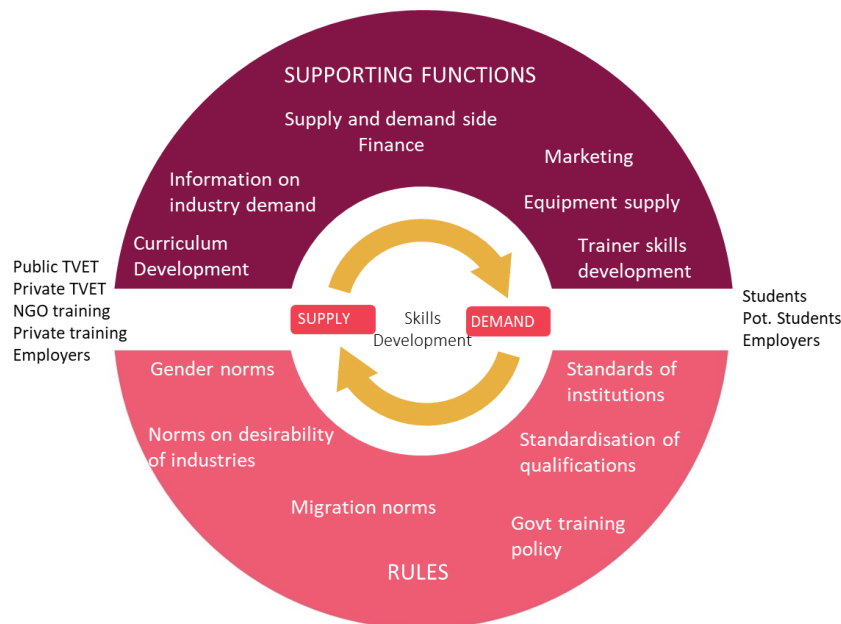
Figure 6: The Skills Market System

Critical constraints – Supporting functions

Curriculum development: The summary of underperformance in this function is that people are not being trained in the subjects or in the way that employers need. Curriculum is often focused on theory rather than practical skills meaning trainees are not ready for work when they are recruited. There are multiple ways to understand this constraint based on how these functions work when the system performs better. In some cases, training providers or government provide *training needs assessment* to provide information at an aggregate level. In other cases, there are *coordination* fora where training providers and employers coordinate to discuss needs. In either case, the results should be training institutions delivering better and more appropriate curriculum to suit the needs of employers.

Equipment supply: A constraint linked to curriculum development is equipment supply including machinery, training materials such as books, and IT applications. Training providers do not have access to high quality equipment and so cannot train students in industry relevant skills. This also affects the delivery medium as poor quality IT limits the potential for remote learning or accessing the latest information.

Supply side finance: A constraint linked to equipment supply is supply side finance. Training providers cannot access suitable equipment due to the lack of suitable financial products to allow them to purchase machinery.

Demand side finance: Students too often need to access financial services to pre-finance training costs. A lack of suitable financial products means students cannot afford the upfront costs of training.

Trainer Skills development: In addition to inappropriate curriculum, the skills of those that deliver them are often unsuitable for adult learning. The skills development market for trainers, therefore, also needs to improve if the core skills development is to improve.

Information for students on industry demand: Students don't know which courses are likely to help them obtain a job or what the conditions of that job are likely to be. Better information on industry demand would allow students to make rational choices about which courses are best suited to them.

Marketing: Training providers also need to effectively sell their services. Effective marketing involves understanding your target market (employers and students) and tailoring your product to suit their needs. This could increase both the quality and quantity of demand.

Monitoring and evaluation: This is actually a support function of many of the other support markets documented here. Training providers need to be able to effective monitor learning outcomes, graduate employment rates, wages, dropouts and other metrics which help improve curriculum development, marketing, and even finance as the development of better financial products could be improved by better information on ability to pay.

Transport: This is one way to frame the inequality of access to training for certain groups. Others include provision of accommodation or, as listed below, government training policy. Better more affordable transportation would widen the range of student who could access training.

Critical constraints – Rules

Standards of institutions: A clear, trusted, and comparable rating system for training institutions builds trust among students, that their qualifications will be of high quality and make them employable afterwards, and among employers, that graduates from particular institutions will be of a certain quality. An effective system would make it more likely that students are willing to invest in their education.

Standardisation of qualifications: Just as with institutions, qualifications themselves need to be standardised in order to improve trust in the system. If an employer cannot trust that people trained in the same subject are similarly qualified it undermines this trust as they cannot assess jobseekers in a comparative way. Similarly, students will be less likely to invest if they cannot trust the quality of the qualification they will receive.

Government training policy: The government determines investment in and, crucially, distribution of training institutions. Currently, 62% of young people cannot access TVET training, which is largely due to government policy on the distribution of training institutions.

Gender norms: This affects both access to training in general and the choice of training course. Gender norms discourage women's participation in some industries or indeed from pursuing further education. For example, women's participation in ICT is limited by the perceptions around which industries women *should* work in.

Migration norms: This affects the quantity and quality of demand for training. Potential students have the perception that migration is a far easier route to improved job opportunities and so do not wish to invest in training.

Norms on desirability of industries: Another norm which affects the quality and quantity of demand is the perception around the desirability of certain industries. Demand is low for training in some fields where there are jobs available due to the perception these jobs being for lower castes or of a lower social status.

5. Developing Interventions to Address the Systemic Constraints

Intervention aims to achieve two things, namely **sustainability** and **scale** of impact. Sustainability relies on identifying the actors with the right capabilities and incentives to deliver change in the long term. Scale relies on identifying the mechanisms by which any innovation can be replicated or scaled up without repeated programme intervention and building these mechanisms into the design.

According to the programme design, SEP has two principal intervention instruments available to the programme in order to address the systemic constraints identified here: i) a challenge fund and ii) targeted technical assistance. Given the challenge fund mechanism identified for use in SEP, the

formulation of interventions is equivalent to the definition of windows, eligibility criteria, and marketing strategies that can respond to the constraints identified above.

These intervention modalities were arrived at through diagnosis and, in part, through a detailed stakeholder analysis which examined the incentives of different actors groups to address some of these systemic constraints.

5.1 Key stakeholder analysis

Stakeholders were segmented into three key groups [refer to the deliverable (**A1.1.1**) that provides a stakeholder mapping of skills sector in Nepal], with relevance to different critical constraints (**Figure 7**).

Stakeholders at macro level: Actors contributing significantly to GoN's skills development plans.

Stakeholders at meso level: Industry organizations, training providers associations, federations of professional training and employment of Nepal, development partners and projects working in the field of skills development.

Stakeholders at micro level: Local firms and organizations, private and public training providers, business and industries including MSMEs.

Actor group	Actors	Relevant constraints	Incentive
Govt Training	CEHRD, CTEVT, MOEST	Curriculum development; government training policy	Improve educational attainment, linkage with qualification framework
Govt Industry	DCSI, MOICS, MOCTA, MOALD	Competency-based market-driven curriculum development	Increase industrial growth
Govt Labour	ESC, MOLESS	Information on jobs; information on labour	Reduce unemployment by linking with in-demand jobs
Industry Associations	CNI, FWEAN, FNCCI	Market-driven curriculum development; information for students on industry demand	Increase skills of employees
Public Training providers	Public TVET Providers, TECS, CSITC	Market-driven curriculum development; information for students on industry demand; marketing; finance; equipment supply	Increase academic attainment/ enrolment numbers, training linked with employment
Private Training providers	FPTS, FPTEN, affiliated TTPs, PABSON	Market-driven curriculum; information for students on industry demand; marketing; finance; equipment	Increase profit via fees/enrolment; training linked with employment
Development Partners	Helvetas/ENSSURE, SDC, WB, ILO, ADB, DFID, ILO, KOICA	All constraints	Reduce unemployment
Public Support service providers	NSTB, CPSC, DOFE, TITI	Standards of institutions; standards of qualifications; trainer skills development	Fulfil mandate
Private Support Providers	NAFEA	Skilled workforce meeting standards of foreign employment	Increase profit
Trainees/Target groups		Affordability, information on training opportunities and job placement	Want increased employment opportunities

Figure 7: Stakeholders, Constraints, and Incentives

5.2 How the intervention modalities respond to constraints and incentives

This sub-section highlights how the intervention modalities developed by SEP respond to the identified constraints and incentives (also see Figure 8 below).

Challenge Fund

Window 1: Employer or Industry-led Training Models

This window solicits proposals from employers or their associations who share incentives to obtain increased quality and quantity of labour for their enterprises. By offering financial contributions towards the development of replicable models for employer-led training, SEP hopes to reduce the investment cost of industry actors in discovering effective ways to produce more appropriate and skilled labour.

It is anticipated that applicants through this window will seek to experiment with sponsorship of training, apprenticeships, on-the-job-training, and certified in-house training.

Window 2: Training provider-led Training Models

This window seeks to solicit proposals from training providers who have a financial incentive to increase their training offer.

It is anticipated that applicants through this window will develop standalone or employer-run training products based on skills assessments and on-the-job training, resulting in more industry appropriate training products.

Window 3: which enhance employment opportunities for gender equality and social inclusion, people with disabilities, and other disadvantaged groups

This window seeks to solicit applications that will improve provision of training services to particularly disadvantaged groups. It is anticipated that applications here will come from non-profit organisations, civil society organisations, associations and community-based organisation who seek to realise moral and social incentives in extending training provision to these groups.

Examples from Early EOIs and Investment Applications (IAs)

From the over 45 EoIs received, 4 IAs for pilots are under consideration for the first tranche of challenge fund applications, and they showcase the relationships between the selected sectors, the constraints, and the windows identified.

Both the AI Shikshya (Fuse Machines) and Genese projects address problems in the training market system associated with **curriculum development** and **information on industry demand**, both relevant to the needs of the ICT sector. They are providing industry relevant skills with a demonstrated demand in artificial intelligence and cloud computing respectively. The curriculum is based on international best practice.

AI Shikshya also seeks to address issues with **demand side finance** by proving scholarships to key target groups.

Genese will address the critical constraint of **standardisation of qualifications** by providing a recognised certification which will build the trust of employers and trainees and make them more willing to invest their resources to seek the qualification.

Both the AI Shikshya and Rojgari projects also address constraints in the labour market with respect to **information on jobs** and **information on labour**. This is the central part of the Rojgari project which aims to extend **job matching infrastructure** to lower skill segments of the market. In the AI Shikshya project, the constraint around information is addressed by integrating a matching function which identifies the best trainees through the programme for immediate employment within Fuse.

These projects provide case studies of how the challenge fund will elicit responses that address critical constraints in both labour and skills markets.

Figure 8: Linking Constraints to SEP Challenge Fund Proposals

Open Window

This window seeks to solicit proposals which respond to any unidentified constraints and propose market-driven responses to these challenges in the skills development market.

Technical Assistance

The technical assistance component of SEP will seek to address several other systemic constraints in Nepal's labour markets relating primarily to policy change. Relevant constraints include government training policy on the distribution of resources, standardisation of institutions and of qualifications.

SEP's first six-monthly action plan for the TA component seeks to address many of the systemic constraints outlined above. Two main focal areas within this are the exchange infrastructure providing **information to employers on labour** and **information to labour on jobs**, as well as the enabling environment around public private partnerships in vocational skills development, responding to the constraint around government training policy.

In this period, SEP will provide technical assistance to GoN to help to scale the learning and successful innovations from the challenge fund. The success of the strategy depends on how successful challenge fund applications are in eliciting truly innovative models which address systemic constraints. As a theoretical example, an application might be funded through window 2 from a private training provider that seeks to provide a test to recognise work experience rather than simply taught qualifications. The model is successful. Employers are willing to pay either for the certification service or willing to pay those with certificates more money so that there is an incentive for potential employees to pay for their own certification. If this is demonstrated to have an impact by reducing the skills gap, allowing firm growth, displacing imported labour, and ultimately increasing employment, the SEP will use the evidence from this pilot to advocate to government for formal recognition of this alternative form of certification, leveraging their incentives to reduce unemployment and increase tax revenues. SEP will also employ technical assistance to help pilot and refine the introduction of a new policy, addressing capacity issues on the side of GoN.

Policy change is always an iterative process of co-creation and, as such, SEP will seek to respond to emerging learning from both the challenge fund and TA components in order to develop work plans over the period. However, the analysis contained in this document provides some key areas for reform if the labour and skills development markets are to work more effectively.

5.3 How interventions will lead to systemic change

SEP's vision for systemic change extends to both the labour and skills markets.

In skills, SEP envisages a pluralistic system of training suited to the demands of employers. This will include improved quality and availability of private training provision funded by more employers being willing to pay for a higher quality service, meeting their needs to increase the performance of their enterprise. It will also include a more pragmatic and grounded skills appraisal system including more on-the-job training and recognition of pre-existing skills, easing problems relating to the availability of skills in the labour market. Evidence and momentum built from experimenting with new models of skills development will be used to reform vocational skills structures at the national level, helping government to make more efficient use of resources to overcome some of the systemic constraints identified. This evidence-based approach will help the results from successful pilots through the challenge fund reach scale.

In the labour market, the institutional environment will adapt to changes in the skills development market to ensure that more skilled job-seekers are able to find work and help employers to grow through increased productivity, creating yet more jobs. In particular, it is anticipated that function of providing information on jobs and information on labour will be improved as a result of better training systems and record keeping, with the possible introduction of a digital system for job matching enabled through SEP.

All in all, this should reduce transaction costs for job-seekers and employers and lead to a reduction in unemployment.

The technical assistance component of SEP will be critical if the programme is to achieve systemic change in the skills and labour markets in Nepal. The challenge fund could and should encourage experimentation at the level of the firm or training provider. However, M4P as an approach relies on the examining mechanisms for scale building them into programme design.
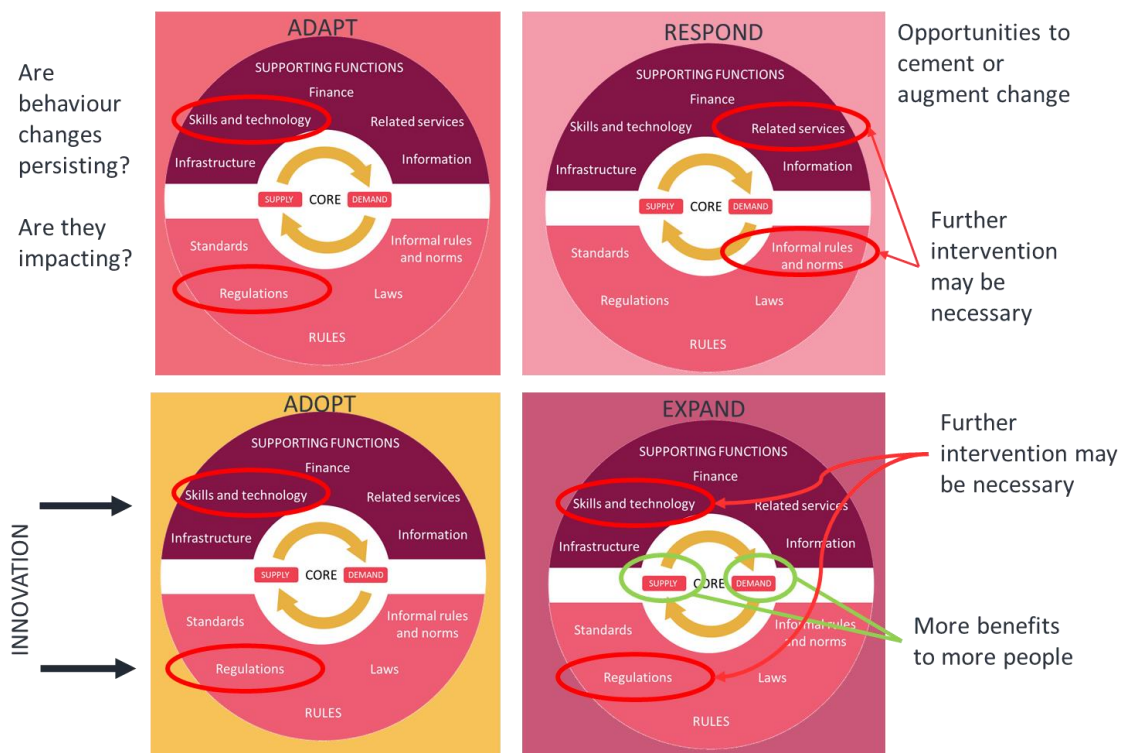

Figure 9: Systemic Change in M4P - AAER Framework[1]

Figure 9 outlines the systemic change through the M4P Adopt-Adapt-Expand-Respond (AAER) framework and **Figure 10** demonstrates how SEP envisages using this process.
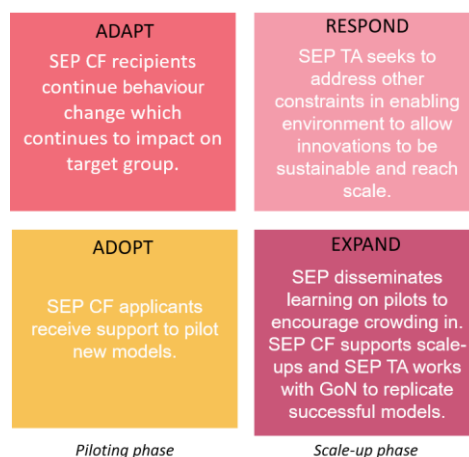

Figure 10: Systemic Change through SEP's Instruments

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[1] AAER- Adopt-Adapt-Expand-Respond (AAER) framework (also commonly referred to as *the systemic change framework*) developed by the Springfield Centre, March 2014.

5.4 Future directions

These initial interventions in defining the challenge fund windows and technical assistance workplan of SEP have emerged from diagnosis. However, they are also open to revision depending on results from the initial round of pilot interventions and in the first half of the 2nd year of the programme.

Concepts around market failures have been developed and refined through this M4P analysis and it may also be prudent, moving forward, to have the windows respond to these constraints (see **Figure 11** for an illustration).

Market Failures	Systemic Constraint	Market
Ecosystem imperfection	**Curriculum development**	Skills
Ecosystem imperfection	**Trainer skills development**	Skills
Ecosystem imperfection	**Equipment supply** and **supply side finance** limiting quality of skills development	Skills
Low Skill/ Low Technology trap	*These are symptoms rather than causes of underperformance in the skills market.*	*Skills*
Imperfect Information	**Marketing** of skills development opportunities and **monitoring and evaluation** performance of skills development	Skills
Imperfect Information	**Norms on desirability of industries** and **information for students on industry demand**	Skills
Imperfect Information	**Standards of institutions** and **standardisation of qualifications** affecting demand for and wages of trained labour	
Irrational Decision Making	*This is a symptom of underperformance in the skills market which causes employers to underinvest in training which in turn has a number of causes.*	Skills
Inequitable Access	**Demand side finance** for students to afford the real and opportunity costs of training.	Skills
Inequitable Access	**Co-location of Training infrastructure in Underserved Geographies, Transportation** and **migration** of students to training opportunities, **government training policy** affecting its distribution.	Skills
Inequitable Access	**Gender norms** on who should access what training	Skills
Irrational Decision Making	*This is a symptom of underperformance in the skills market which causes employers to underinvest in training which in turn has a number of causes.*	Skills
Inequitable Access	**Norms on hiring** affecting demand for labour	Labour
Inequitable Access	**Social norms on mobility**, **transportation**, **physical and digital infrastructure** affecting who can move to which jobs	Labour
Risk of Attrition	*This is a symptom of underperformance in the labour and skills markets related to wages, perceptions etc.*	Labour
Imperfect information	**Cultural attitudes towards work** affecting the quality and quantity of supply of labour for certain types of work	Labour
Imperfect information	**Information on jobs** and **information on labour** affecting matchmaking of supply and demand for labour	Labour

Figure 11: Mapping Market Failures to Constraints and Markets for Future Windows

One crucial area to examine for success is the quality and relevance of applications to the challenge fund. SEP will reflect (as part of MEL assessments) after the first round of applications on two key questions:

1. To what extent are these applications addressing the systemic constraints to the better functioning of labour and skills development markets in Nepal?
2. Is it clear how these applications will lead to sustainability and scale of impact?

It is quite possible that the answers to one or both of these questions will be no. As such, SEP will seek to modify interventions to achieve these objectives. One possible way to address question 1 is to refine the windows to more closely reflect the diagnosis, to ensure that SEP is supporting innovation that affects the system rather than only firm level constraints. If applications are not suitably addressing the second question, SEP may seek either to redirect resources towards the TA facility or to introduce new intervention modalities that work more flexibly on the mechanisms to achieve scale. There are also options to tweak the challenge fund conditions to make sustainability and scale more likely. For example, refining eligible costs for applicants to ensure commitment to cover all recurrent costs can drive sustainability, while building in information sharing and dissemination components to the agreement can drive scale. These options will all be assessed (as part of SEP MEL Framework) following the conclusion of the pilots before the windows are refined for scaling up.