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Informal Employment: Can We Tame the Beast?

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- ◆ Informal employment persists, even when the economy is growing
- ◆ Understanding the phenomenon is necessary to “tame the beast” of informality
- ◆ Coherent policies are needed to create decent jobs and provide social protection

Informal Employment: Why Bother?

Shoe shine workers in Cairo, street vendors in Calcutta, badly-paid public officials driving their taxis at night in the streets of Moscow – these are all examples of the phenomenon called informal employment. Defining and measuring informal employment is a huge and daunting task, but ignoring it does not help. As Hernando de Soto puts it, “The informal sector is like an elephant: we may not be able to define it precisely, but we know it when we see it”. Indeed, defining the beast has not been easy. But why should we care about the beast in the first place?

For three reasons. *First*, if you care about jobs and social security, you cannot overlook informal employment. All over the world, the majority of work performed outside of the formal structures that govern taxes, workplace regulations and social protection schemes.

Second, informal employment is not declining: as the table shows, we have witnessed persistent and sometimes even rising informal employment despite growth! The beast is here, perhaps to stay.

Third, it causes important problems for individuals as well as for societies. Informal employment often functions as a last resort for people that cannot find a formal job – actually most of the poor people in the world work “informally”, either in self-employment or as wage earners. Many of these people lack basic social protection, and

Table 1. Informal Employment*

Region	Informal sector as percentage of non-agricultural employment	
	1980-89	1990-99
North Africa	38.8	43.3
Sub-Saharan Africa	68.1	74.8
Latin America	52.3	56.9
Asia	53.0	63.0

* Informal sector employment includes “all non-agricultural unincorporated enterprises owned by households” and micro-enterprises as well as professional, domestic workers, and home-based workers; it also includes family labour and “employees on an occasional basis” (Beneria, 2001)

Source: Charmes 2000, quoted in Beneria 2001, Table 6.

are locked in low productivity activities, with fewer opportunities to climb the social ladder. Widespread informality, meanwhile, weakens tax revenues and governments’ capacity to address important social problems. At the same time, quite a few working people actively choose to “go informal” – partly to avoid paying taxes and complying with regulations, but also to opt out of social insurance schemes and other public services that they deem low in quality. Hence, being informally employed does not automatically mean being poor, low in productivity and excluded from services and social security. This is the heart of the dilemma in which policy trade-offs arise: how can societies go ahead taming the beast without actually accidentally feeding it?

How (Not) To Do It

Law and order measures that aim to ban informal activities have done more harm than good. One crucial issue behind this is governments' capacity to enforce regulations – people are very good at circumventing them. More importantly, repressive measures harm the livelihood of those who depend on incomes from informal activities. In the mid-1990s, when the authorities of Mexico City sought to ban all informal street vending in the historical centre, only a fraction of those vendors actually switched to a formal market setting; a large proportion simply continued their informal trading in other areas of the city or had to close their business, becoming even more vulnerable. A more promising approach: improve the quality of social services, discontinuing services and programmes that people don't value. In Latin America, for example, formal workers often pay for a mandatory bundle of programmes, some of which they don't want. Likewise, there is often much to be gained from scrapping red tape related to business registration and social security administration. Finally, as the example of South Africa demonstrates, the nurturing of a "culture of compliance" regarding tax payments helps keep public revenues viable.

Towards Coherent Policies for Taming the Beast

Any credible approach should start with an honest assessment of the status quo. To measure the size and characteristics of informal employment better, as well as the motivation of the different groups working informally, more and better data are badly needed. We need a two-pronged strategy to deal with informal employment that takes into account its dualistic structure. For those people for whom it is a last resort, government actions should improve opportunities to engage in productive work with decent social protection, through training, access to credit and universal coverage of the most basic needs. When it comes to the segment of informal workers or entrepreneurs who voluntarily opt out of public sector schemes, efforts

should focus on the improvement of such services and the provision of appropriate incentives for operating formally. In this respect, there is often much to be gained from mere simplification of registration procedures of both labour and businesses.

Furthermore, policies governing private-sector employment and social development must provide compatible incentives to workers and employers. Policies can work at cross purposes. Increasing social protection to those who are uncovered is a valuable policy goal; however, as the debate surrounding Mexico's *Segura Popular* shows, universal protection may discourage those joining the scheme from entering the formal system. Worse still, some people might even drop out of the formal statutory social security system to join those programmes initially intended for the marginalised. Careful screening, selection of beneficiaries and an appropriate governance structure are crucial. In general, a more holistic vision for business promotion, job creation and social protection is needed. This new vision might come at a higher cost – for increased co-operation and exchange between different ministries and layers of government. But if we want to slake the appetite of the beast, there is no alternative.

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