

Tackling Informality

JOBS AND MIGRATION CORE COURSE

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WORLD BANK GROUP

Jobs

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Conceptual Framework, Measurement & Policy Challenges

1. What do we mean by informality?

-> informal sector...informal jobs...informal firms

-> Which occupations and sectors are most affected by informality?

-> Which types of workers tend to work informally?

2. What data and tools can be used to measure informality and assess “how big is the problem”?

3. What are the economic and welfare costs associated with informality?

4. How can we design policies to mitigate these costs?

-> formalizing...incentivizing...improving informal job quality

Which of these depict informal work and which are formal?



By what criteria do we define informal?



Break-out 1:

Discuss the ways in which informality can be defined, and how it is defined in your countries

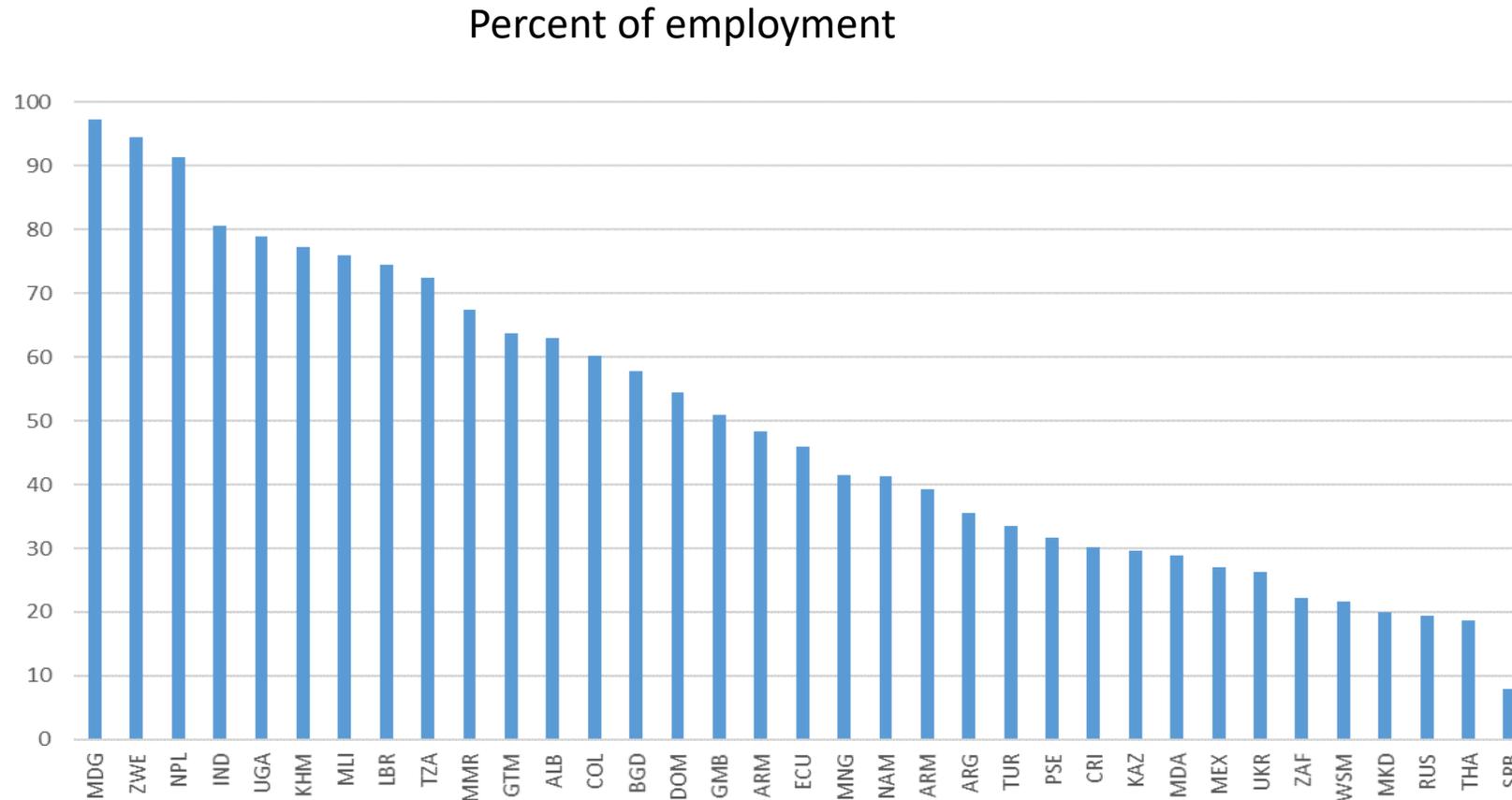
1. List definition options
2. List the most commonly used definition (within your countries)
3. Report back

Defining what we mean by “informal”

Informality Definition	Criteria	Measurement Indicator	Data Source
Registration with tax authorities	Informal if worker or firm is unregistered, or if worker works in an unregistered firm	Does not have a registration or tax ID number	Firm registry
Social insurance coverage and labor protections	Informal if not covered by social insurance. Includes undeclared employees of a registered firm; employers or self-employed not paying into social insurance for themselves; workers in part-time or fixed-term jobs that do not provide paid sick leave, mandatory holidays, or firing or freedom of association protections.	Does not make social security contributions; or does not have a right to a pension.	Administrative data: Social insurance fund list of beneficiaries; Household or labor force survey data: question on access or contribution to a pension
Firm size	Informal if worker is self-employed or small firms with less than the threshold number of employees (typically ≤ 5) (or employee of a small firm)	# of employees working at current employer	Firm census; firm registry (formal only); firm survey; some household/labor force surveys have a question on firm-size
Productivity/Output	Informal if firm has low turn-over, e.g., less than threshold level of annual output per worker, or threshold of annual firm sales	Level of output/worker or sales at current firm of employment	Administrative data from tax authority; firm census; firm surveys
Contract type	Informal if no written contract; temporary contract; some types of fixed-term contract (determines degree of informality)	Lacks a contract, non-standard terms of written contract	Household or labor force survey data
Location	Informal if no fixed work premises outside the home	Home-based work	Household survey data; informal sector/household enterprise surveys

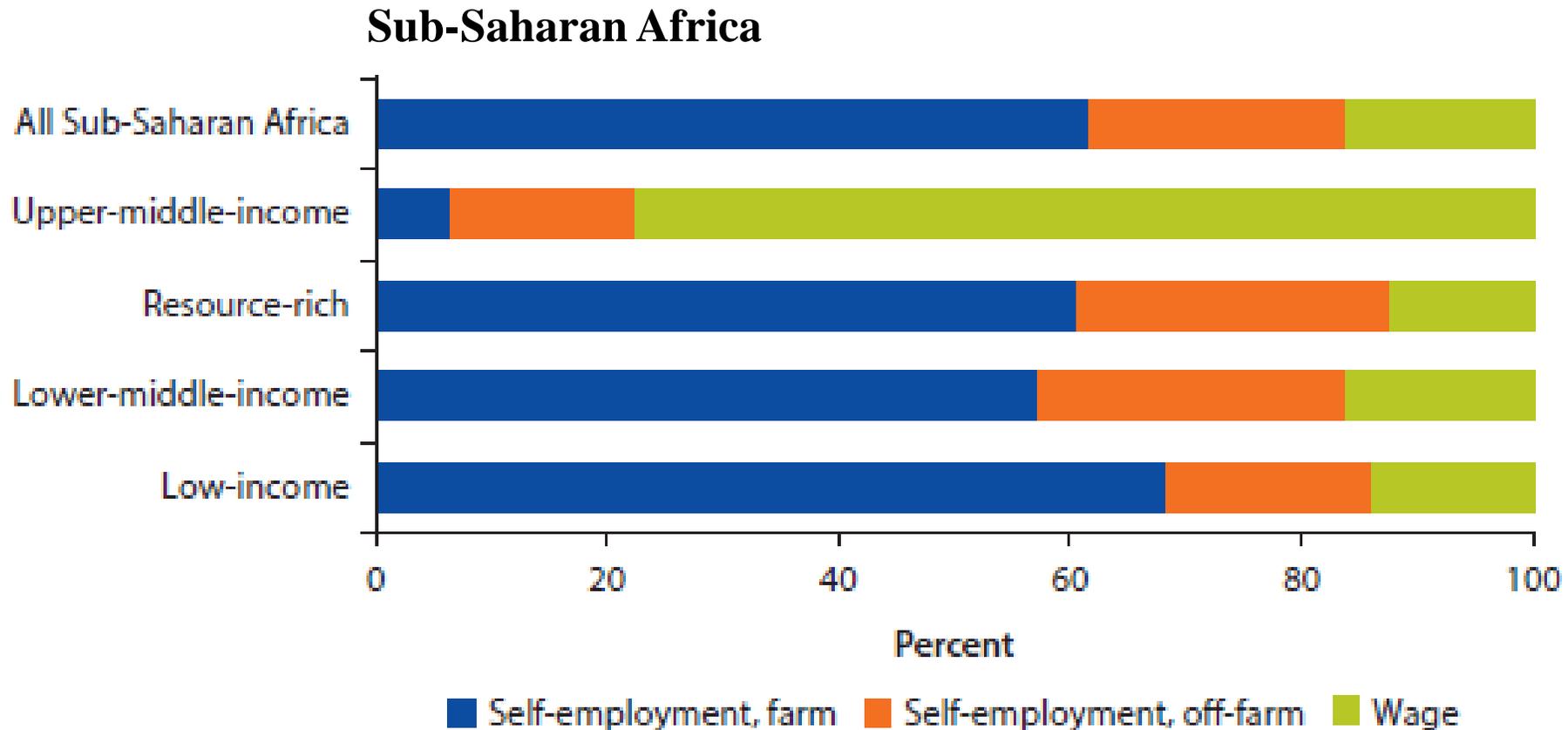
Some global estimates...

Informality is pervasive in the developing world



Source: ILOSTAT. **Informal employment comprises all workers of the informal sector (in unregistered firms) and informal workers outside the informal sector (own-account workers, and employees not contributing to social security, paying income taxes, or who lack certain benefits such as family leave or sick leave).**

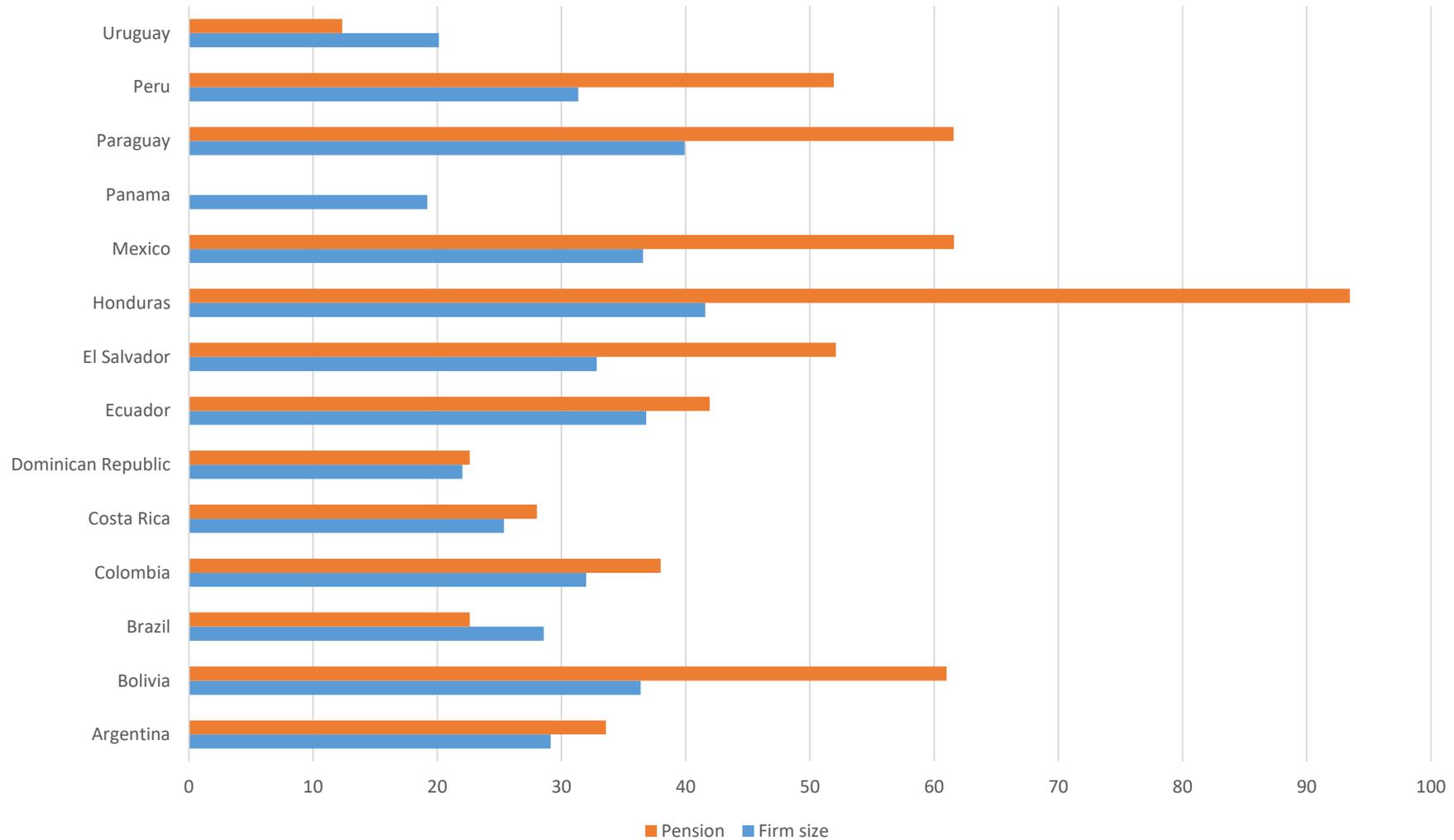
Informality rates vary by country income level, and depend on the structure of economy (and data!)



Source: Filmer and Fox et al. (2014), Honorati and Johansson de Silva (2016)

- ❖ Even economies transitioning from traditional agric. to manf. and a vibrant services sector have high shares of informal employment because many services are low-value, delivered by low-productivity micro-firms or the self-employed.

Different informality definitions yield different rates (% of wage workers, LAC)



Source: WBG estimates using SEDLAC data

Measurement challenges

(both within a country, or for comparing across countries)

- Household and labor force survey data coverage, quality (sample, implementation, data coding/recording/cleaning, timeliness)
- Differences in regulations and therefore formality definition: in a registered firm *or* access to a pension *or* contract type (open, written)
- Uniformity of questionnaires (education categories: Africa vs. LAC some tertiary vs. tertiary complete)
- Primary occupation vs. all occupations; monthly wages and hours worked vs. hourly wages
- Incomplete administrative data (NA, employment) due to under-reporting → poor estimates of labor productivity
- Easily observable: firm size, firm sales ... but evasion can distort measurement.
Moreover, where institutions are weak, evasion and data quality are worse
- Firm data that does not distinguish between different types of workers (full vs. part-time, skill vs. unskilled) and total wage bill – hard to measure firm productivity

How is informality addressed in the Jobs Diagnostics?

1. Macro structural tool

Data: employment levels over time (by sector, region, formality); national accounts data (sector, region, formality...I/O tables)

Q: Has structural transformation led to more or less informality? productivity implications?

2. Labor supply analysis: *how many informal, where are they, what characteristics, welfare implications*

Data: HH survey or LFS micro data on individual characteristics (education, gender, age) and job characteristics (earnings, work status, formality)

Q: How are labor outcomes of informal workers different from formal (productivity, quality, access)?

How is informality addressed in the Jobs Diagnostics?

3. Labor demand analysis:

Data: firm census or firm surveys including unregistered firms

- ❖ *How are firms' output levels, employment (by skill, gender), wages, inputs (K, L, training) and productivity levels linked to formality?*

Q: Which types of firms are creating jobs: young/old? small or large? formal or informal? in which sectors? more or less productive?

Which types of jobs tend to be informal?

Which types of workers tend to be informal? Which types of firms?



Break-out 2:

Discuss the characteristics of informal jobs, and the characteristics of informal workers

1. List common characteristics of informal jobs (*i.e., job attributes*)
2. List common characteristics of informal workers (*i.e., individual attributes*)
3. List common characteristics of informal firms (*i.e., firm attributes*)
4. Report back top 3 in each

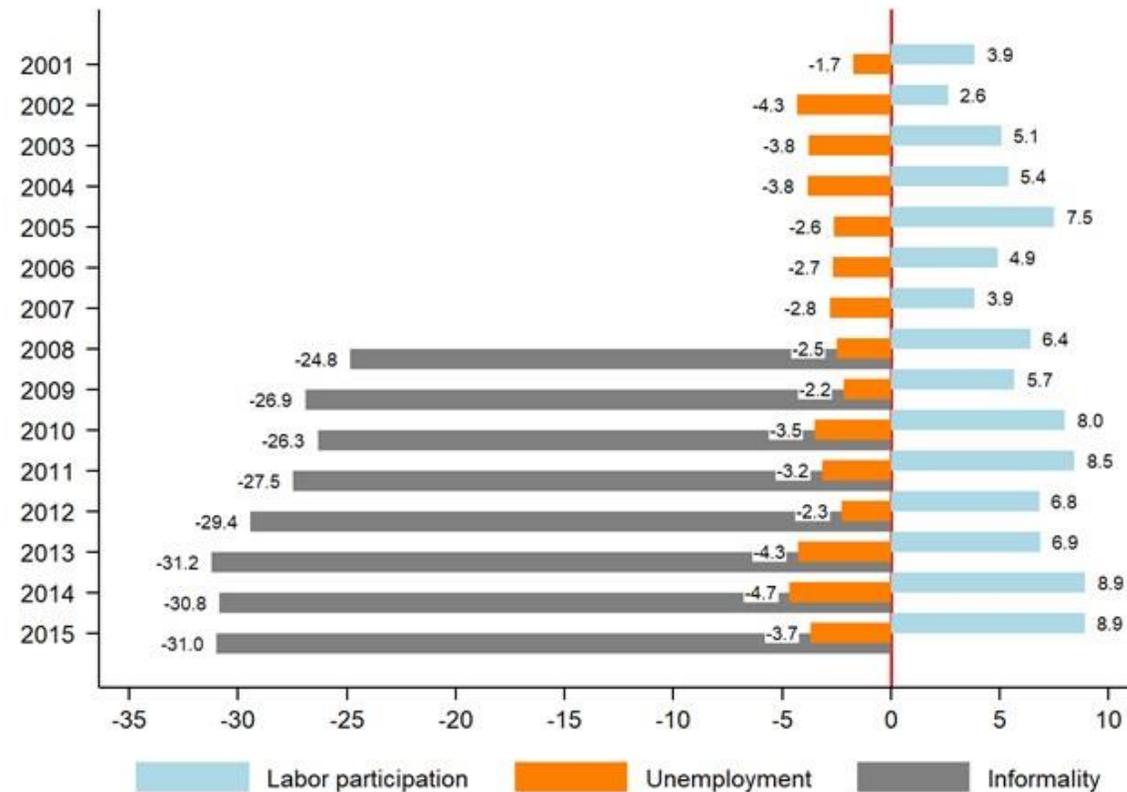
Job attributes? Individual attributes? Firm attributes?



Some evidence...

Workers in poor households have higher informality rates (Paraguay, Logit regressions)

% age point gaps in labor market outcomes: top 60% of households *minus* bottom 40% of households, Paraguay

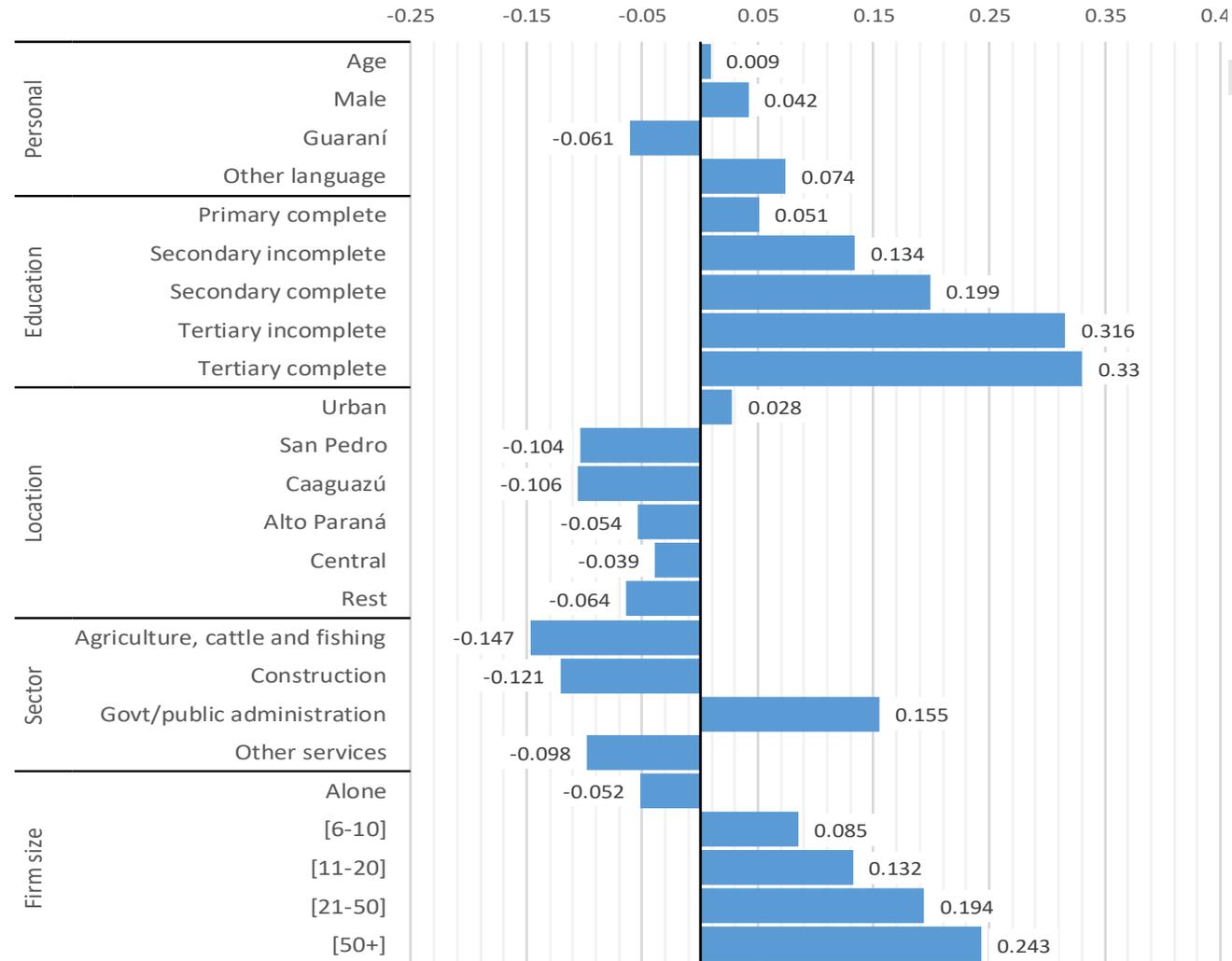


Source: Paraguay Jobs Diagnostic (Ruppert Bulmer et al. 2017)

Factors increasing the likelihood of being formal (Paraguay, Logit regressions)

More likely to be informal:

- Youth
- Women
- Indigenous
- Less educated
- Rural
- Agric, construction, services
- Self-employed



Notes: Logit regressions with weighted observations.

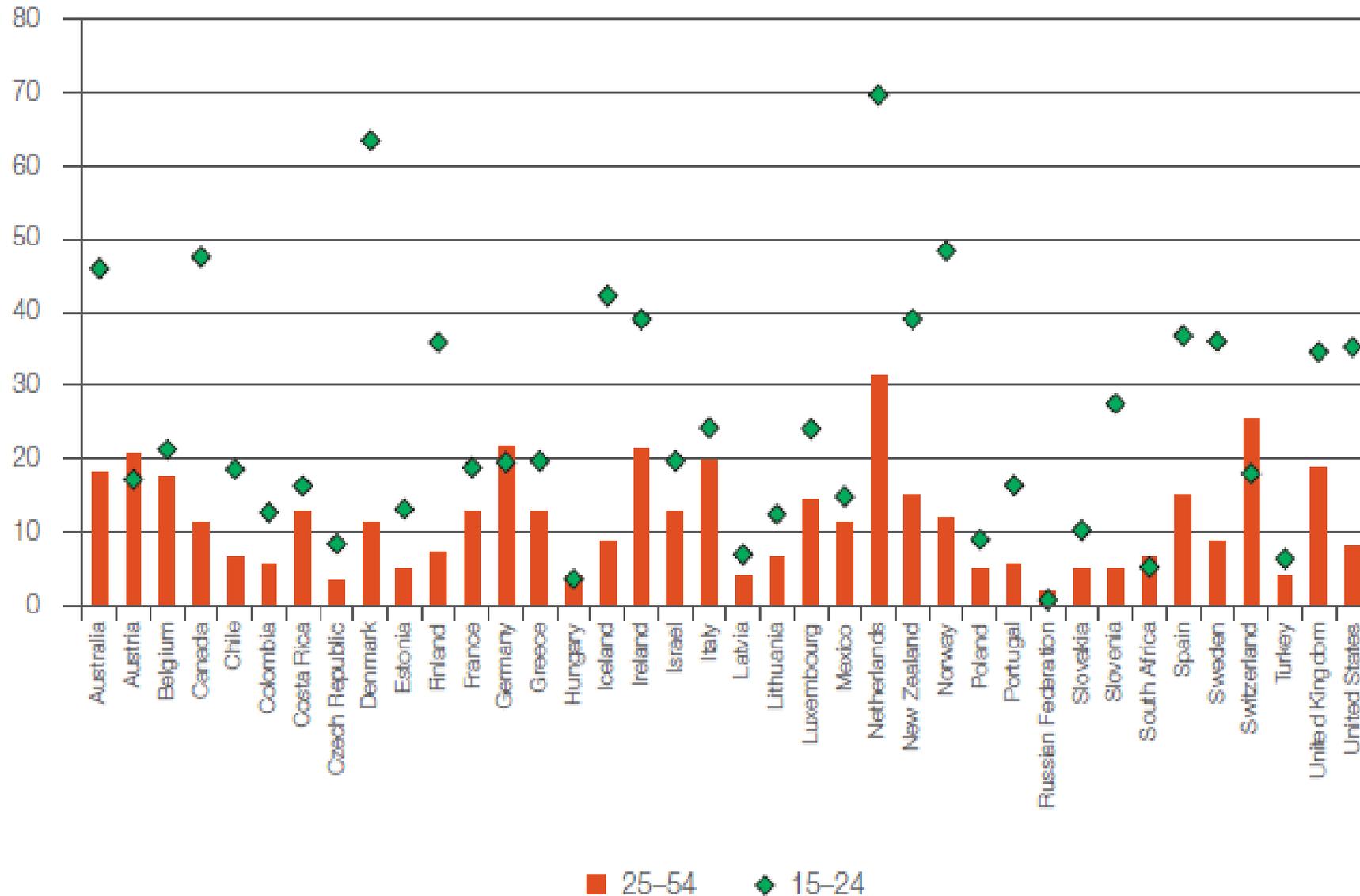
Alone category in firm size includes self-employed and domestic employees.

Source: Staff calculations based on SEDLAC data.

Reference sector: Commerce

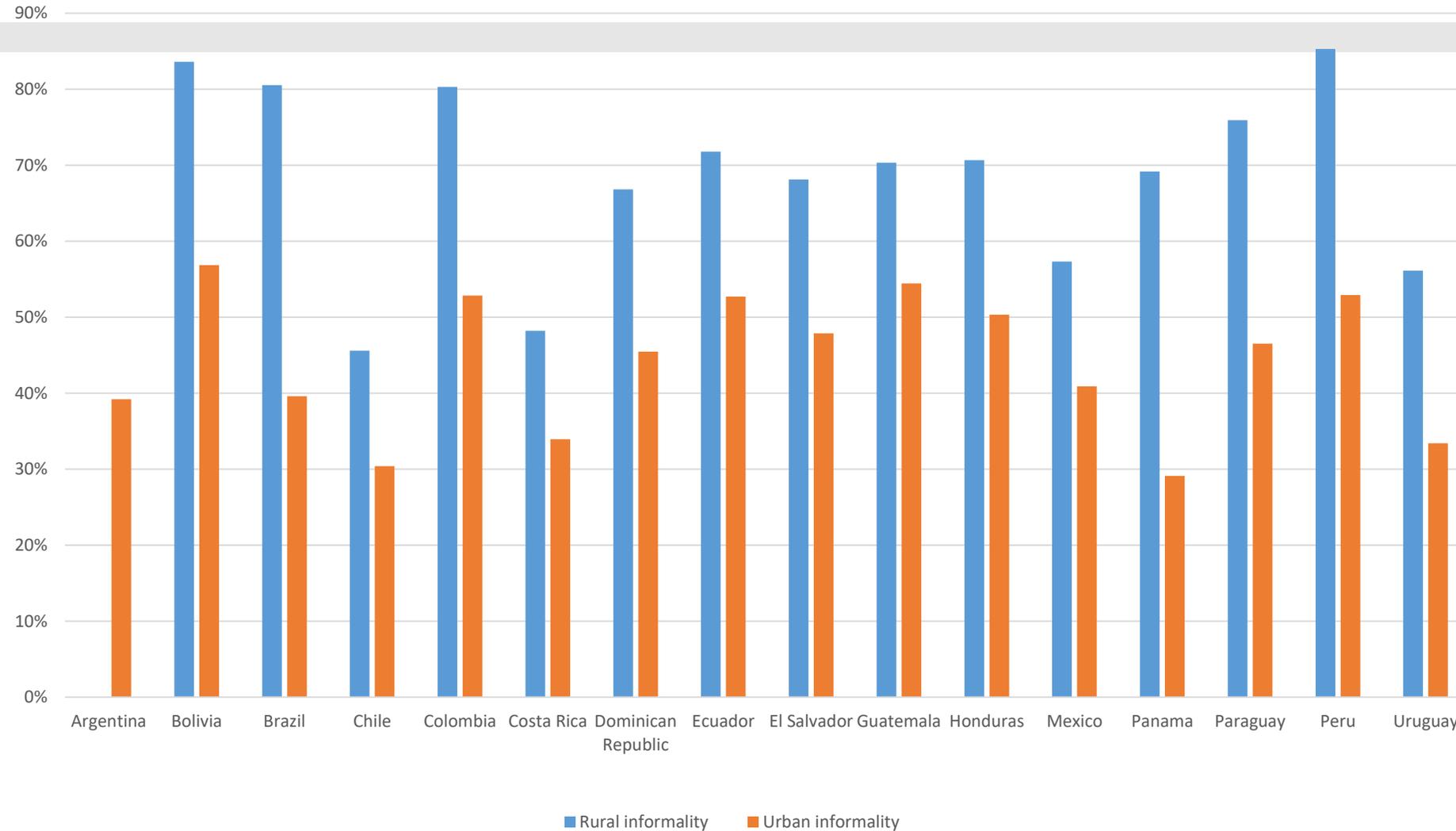
Source: WBG estimates

Global evidence: Youth Are More Likely to be Under-employed (% in part-time work)



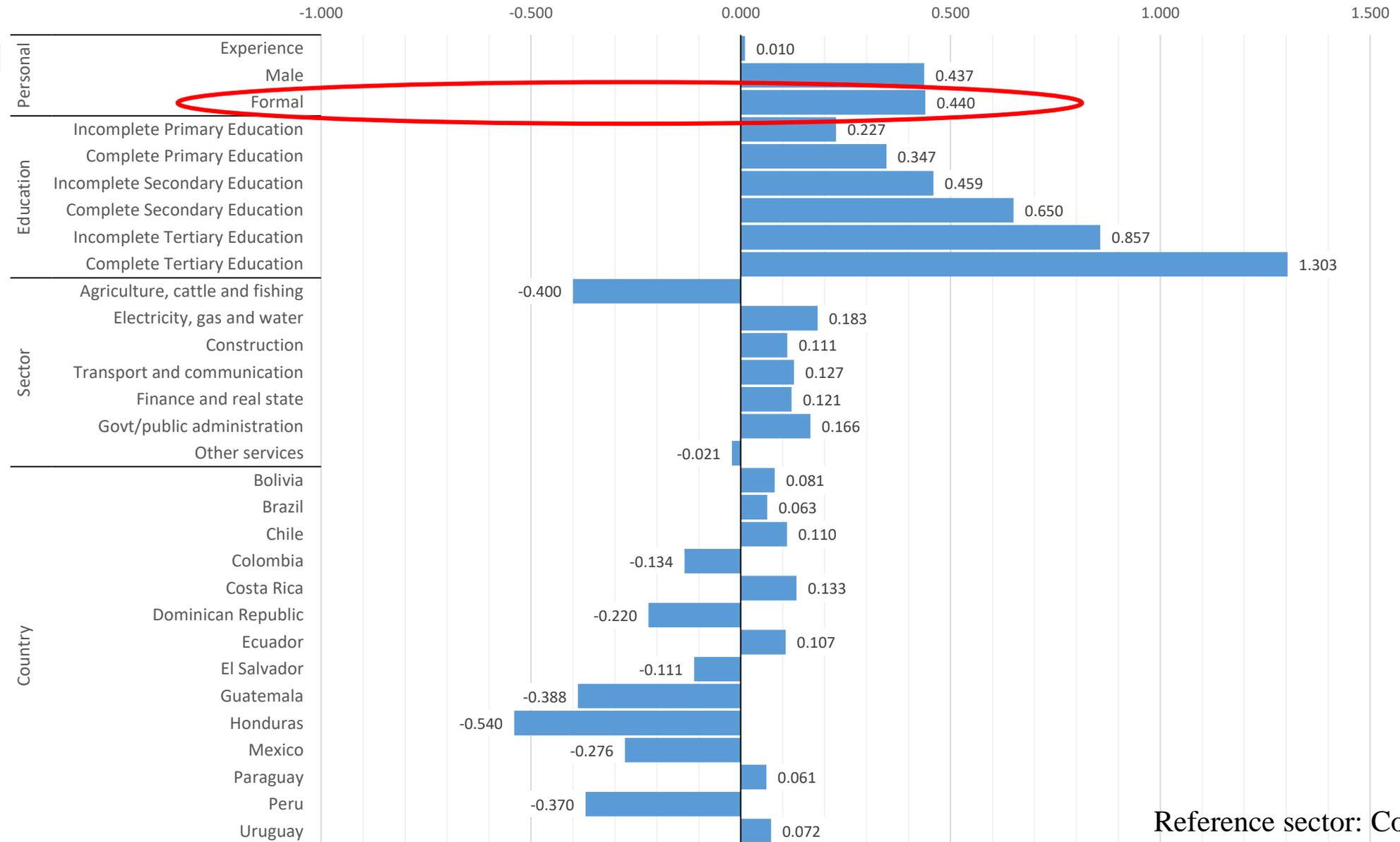
Source: ILO (2016b); computations based on OECD STAT

Rural Workers Have Higher Rates of Informality: Evidence from LAC



Source: Calculated using 2014 SEDLAC data (2013 for Chile)

Correlates of monthly wages in LAC (Mincer regressions)



Source: Paraguay Jobs Diagnostic (Ruppert Bulmer et al. 2017)

Reference sector: Commerce
Source: WBG estimates

Few workers transition from informal to formal work (data from Paraguay)

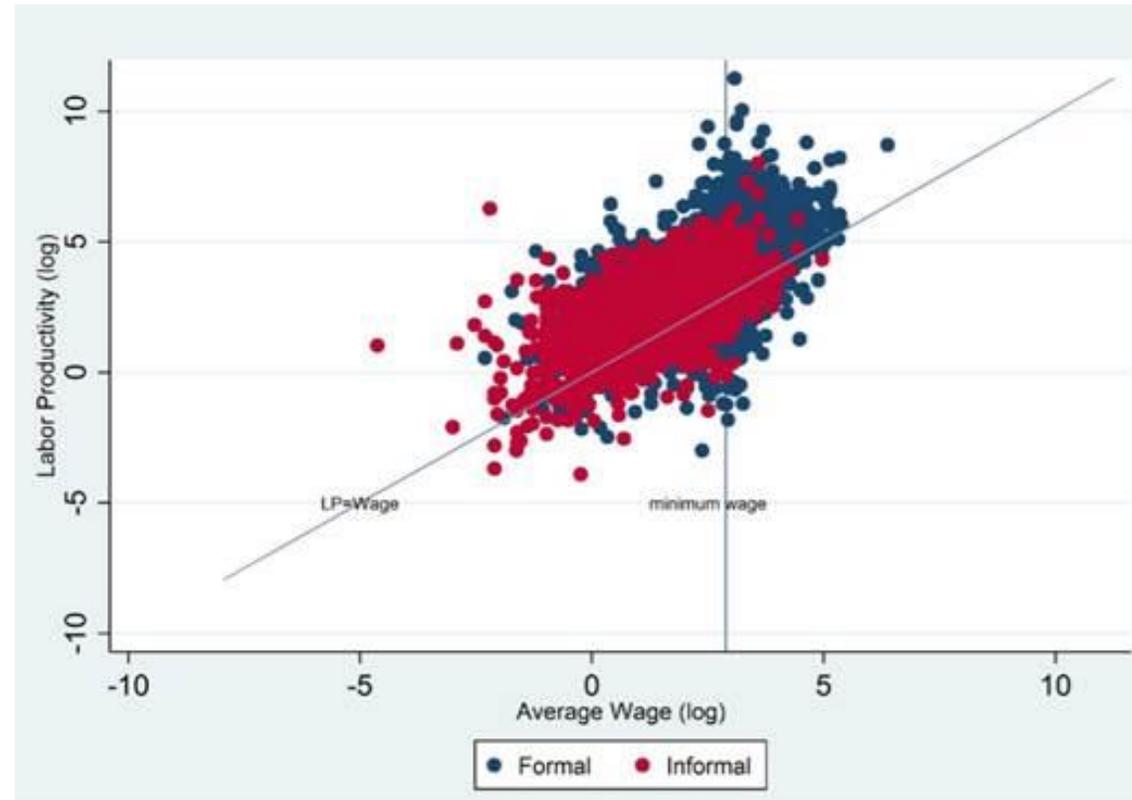
Quarterly Transitions between Labor Market States (average shares of initial work status)

Labor state at t-1	Shares									
	Labor State at t									
	Inactive	Unemployed	Unpaid	Farmer	Employer	Self-employed (non-farmer)	Informal wage	Formal wage private	Formal wage public	
Inactive	81.7	5.6	1.4	0.5	0.6	5.7	4.1	0.3	0.1	
Unemployed	27.1	34.8	1.1	0.4	1.5	10.9	21.4	2.5	0.3	
Unpaid	24.3	3.0	35.8	0.4	4.4	18.0	13.8	0.3	0.0	
Farmer	14.9	1.4	0.8	68.1	2.3	4.4	4.7	2.5	0.8	
Employer	3.8	2.3	1.3	0.4	60.2	22.5	8.1	0.7	0.8	
Self-employed (non-farmer)	12.8	3.2	2.0	0.3	7.0	65.5	8.0	0.8	0.3	
Informal wage	7.2	5.5	1.2	0.2	2.3	6.7	67.0	9.6	0.3	
Formal wage private	1.1	1.9	0.2	0.3	0.5	1.3	10.1	84.0	0.7	
Formal wage public	0.7	0.3	0.0	0.1	0.2	0.7	0.7	1.5	95.9	

Source: Paraguay Jobs Diagnostic (Ruppert Bulmer et al. 2017)

Productivity too low to afford the minimum wage

Firms in Paraguay



Source: "Firm Productivity and Firm Employment in Paraguay 2010-2014" (Ruppert Bulmer and Scutaru 2018)

Q: Why do we care?

A: Because informality leads to inequity and is costly!

- **Workers' welfare**: informal workers tend to be poor, have low and unstable earnings, and may be exposed to unsafe working conditions, lack voice and agency, and are not insured against income shocks
- **Economic and human development**: under-employed are under-utilized, and have earnings too low to invest in their children's HK (especially women)
- **Efficiency costs**: informal workers have lower productivity, lower incomes, low investment, reduced fiscal revenues and underfunded social insurance -> slower economic growth (directly and indirectly)
- **Social stability**: under-employment of youth or in vulnerable/marginal communities can have negative social externalities such as high crime/gang activity/alcohol and drug abuse
- **Governance**: trust in institutions and in government's capacity to deliver quality services and enforce regulations (high evasion undermines governance)

These factors are intertwined

Many factors contribute to informality

- **Market distortions**

E.g., labor regulations and labor taxes (too high→segmentation), business regulations

- **Institutional weaknesses**

E.g., weak enforcement, inefficient tax collection, gaps in social insurance eligibility/access

- **Market failures**

E.g., mismatch of labor supply and demand (due to constrained labor mobility, misaligned education/training curricula with private employers, inadequate labor market information systems); weak property rights (which limit access to finance); poor infrastructure (limited access to markets, electricity, public security – keeping costs high)

- **Inequality of opportunity**

E.g., low levels of HK (education/health access), constrained credit access, distance to markets, discrimination

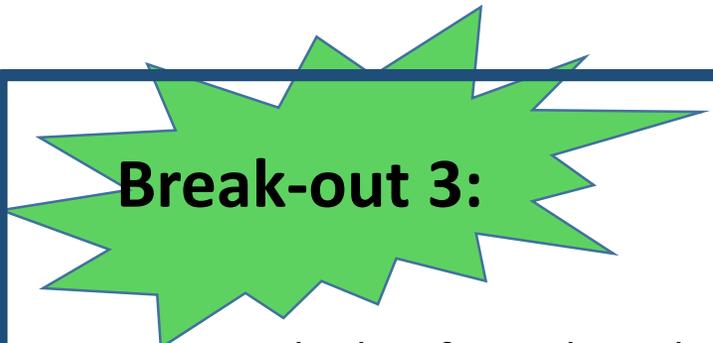
Policies need to address the root causes

Challenge: Cannot simply formalize all informal workers

Policies for addressing informality/mitigating the costs of being informal can be grouped under 5 broad objectives:

1. Reduce the regulatory gap between formal and informal	Tax wedge; de-link SI from employment contract; replace severance with Unemployment Benefits; MW; registration costs
2. Increase incentives to formalize	<u>Carrots</u> : access to credit or training; precondition for importing/exporting <u>Sticks</u> : improve enforcement, labor inspections <u>Governance</u> : confidence in the state
3. Raise the productivity of informal jobs and informal firms	Training (technical skills, management and business practices, entrepreneurship); connecting micro firms to lead firms/value chains; connecting producers to larger markets
4. Increase the quality of informal jobs	Increase worker voice through informal worker organizations and collective bargaining for better working conditions (e.g., domestic workers)
5. Improve workers' ability to access better or formal jobs	Labor mobility; labor information and matching services; education/training targeting marginal groups (e.g., rural, women)

What groups of workers are the “neediest”, and how can we design policies to reach them to formalize/improve job quality?



Break-out 3:

1. Discuss which informal workers are the neediest/highest priority in your countries, clarifying the criteria for prioritizing

[e.g., need can be defined on the basis of welfare gaps, role in economic growth, sector size or growth potential]

2. Discuss policies to improve job quality for these priority groups

3. For a selected policy, list challenges for measuring how many, targeting the policy, and incentivizing workers/firms in these groups (e.g., potential sources of failure/mis-targeting/poor incentives)

4. Each group presents one example for discussion

Policy interventions for addressing informality

	Reduce regulatory gap between formal and informal	Increase incentives to formalize	Raise productivity of informal jobs/firms	Increase quality of informal jobs	Improve workers' ability to access better/formal jobs
Causes					
Market distortions	Reduce/simplify regulations to register a firm, export/import, pay taxes (e.g., single window/electronic processing)	Increase benefits of registering, such as through:	Trade policies to increase access to better inputs and bigger markets		Review public procurement rules to accommodate small suppliers
	Reduce labor tax wedge	- access to small business grants	Trade facilitation/logistics reforms to ease trading for small producers, such as:		
	Reduce layoff requirements	- business services training	- automated customs procedures		
	Allow flexible fixed-term contracts	- export promotion services	- aggregated service delivery		
	Reduce limits on working hours (subject to overtime), night-time work	- specialized vocational training			
	Balance corporate and individual tax rates	- quality, standards accreditation services			
	Conducive macro policy	- employment or recruitment services			
	Non-distortionary trade policy	- access to wage subsidies			
	Reduce land market distortions	Increase perceived value or reliability of social security benefits			
		Increase sanctions for not registering (penalties for tax evasion, regulatory violations)			

Policy interventions for addressing informality

	Reduce regulatory gap between formal and informal	Increase incentives to formalize	Raise productivity of informal jobs/firms	Increase quality of informal jobs	Improve workers' ability to access better/formal jobs
Causes					
Weak institutions	Increase government outreach to inform the public of registration requirements, and provide accessible administrative assistance to register.	Strengthen enforcement of tax compliance		Strengthen the setting and enforcement (labor inspections) of workplace safety and labor standards appropriate to scale of informal activities	
		Increase intergovernmental coordination and cross-check VAT/customs/profit taxes		Increase dissemination and advocacy of user-friendly information on workers' rights, workplace safety, government programs targeting vulnerable groups	
		Increase government credibility to deliver future social insurance benefits			

Policy interventions for addressing informality

	Reduce regulatory gap between formal and informal	Increase incentives to formalize	Raise productivity of informal jobs/firms	Increase quality of informal jobs	Improve workers' ability to access better/formal jobs
Causes					
Market failures			Increase infrastructure access/quality (water, health services, electricity, roads) targeting informal/low-income workers/lagging regions	Extend social insurance to informal workers, and make benefits portable (i.e., de-link from employer)	Align school and TVET curricula with market demand
			Increase entrepreneurial skills training through schools and TVET programs; incorporate soft skills into standard education curriculum	Foster cooperatives of informal workers to pool assets and risk (if big enough, can offer alternative social insurance)	Increase access to training/re-training
			Increase credit access through appropriate trade credits, micro- and small enterprise financing, moveable assets registry for collateral, and farm credit	Voluntary safety standards certification programs (e.g., Fair Trade, Better Work)	Reduce labor mobility costs through:
			Insurance products targeted to small firms/farmers to facilitate sufficient risk-taking	Foster worker coordination and voice for collective bargaining for better working conditions, such as through:	- Labor market information systems
			Public support for private sector incubators	- promoting cooperatives or informal unions	- Public employment services to match job seekers to vacancies
			Phone-accessible market information platforms	- providing training to firms on the merits of worker committees	- Infrastructure for accessing urban job centers
				- create better communication channels with civil society, private sector and Government	

Policy interventions for addressing informality

	Reduce regulatory gap between formal and informal	Increase incentives to formalize	Raise productivity of informal jobs/firms	Increase quality of informal jobs	Improve workers' ability to access better/formal jobs
Causes					
Inequality of opportunity	Targeted government outreach on registration rules and process to remote areas or to certain population groups		Increase infrastructure access/quality (water, health services, electricity, roads) to raise worker productivity, especially in underserved areas	Introduce independent ombuds at the local government level to hear workers' concerns	Increase access to education, training
			Targeted infrastructure investment for informal traders		Increase quality of education/training
			Foster information links to larger markets		Extend infrastructure access/quality to lagging regions
			Foster local market development (e.g., local trading platforms)		Promote cooperatives of informal workers to harness negotiating power to insert into existing value chains or public service contracts
			Geographically targeted financial deepening, credit programs (subsidized/publicly underwritten)		Quotas for public procurement from small suppliers
			Direct support for more productive inputs for small farming communities (e.g., irrigation, farm machinery)		Legal reform (to eliminate limits on ownership, land and financial access, and/or work hours), public awareness campaigns and targeted interventions to address occupational discrimination against women/minorities/youth/older workers

EXAMPLE

Priority group	Main problem	Policy	Policy design challenges	Options for addressing
Rural women	Access to jobs	Vacancy information system	<ol style="list-style-type: none">1. Dissemination infrastructure2. Identifying labor needs of informal firms	Mobile app Survey, create local network, incentivize by providing recruiting assistance, promote private job placement services
Rural women	Inequality of opportunity	Education/Training (soft vs. hard skills, entrepreneurship)	Identifying which skills to teach, ensuring trainees are vested	Validate with local private labor demand, cost-sharing

Questions?

Thank you!

Defining a “good” job: is this the same thing as being formal?

- ❖ ILO (rights-based focus): worker protections, SI, workplace safety, voice, collective bargaining → formal or hidden formal (Non-Standard Employment report)
 - ❖ Overlap with ILO’s ***decent work*** concept: “work that is productive and delivers a fair income, security in the workplace and social protection for families, better prospects for personal development and social integration, freedom for people to express their concerns, organize and participate in the decisions that affect their lives and provide equality of opportunity and treatment for all women and men”
- ❖ Advanced economies (productivity/growth focus): ICT or high tech job
- ❖ Segmented/distorted economies: government job

Defining a “good” job from the development perspective

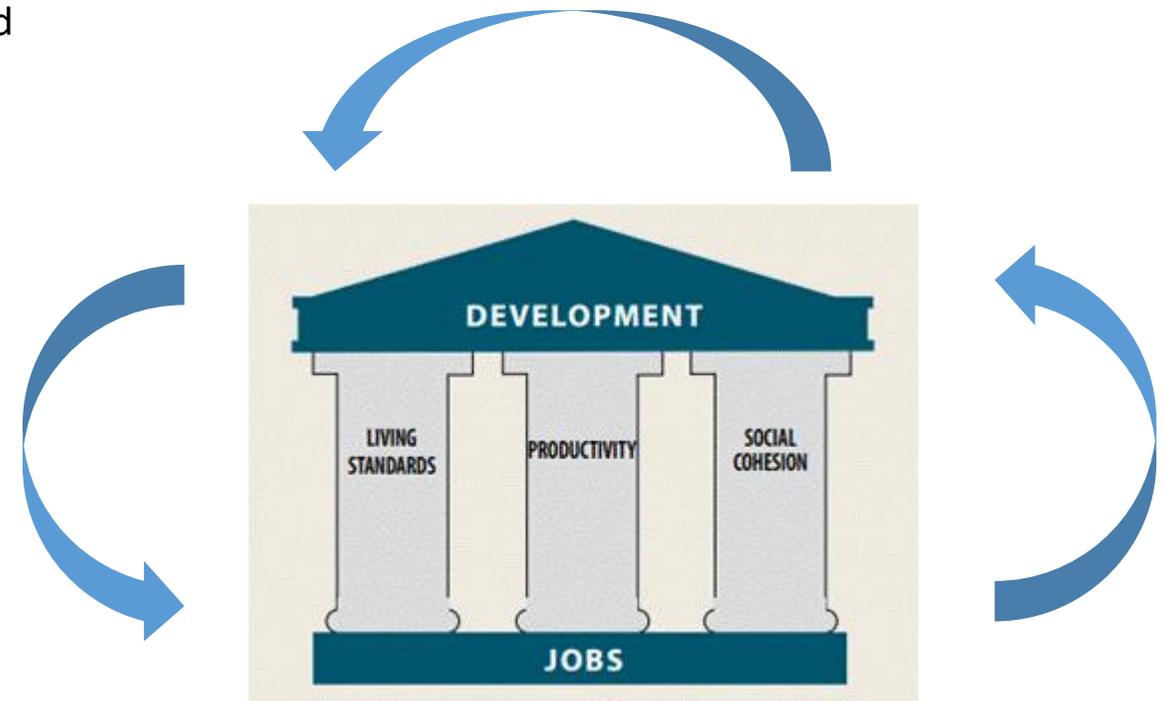
❖ World Bank Group: aims to balance social and economic development

WDR 2013 on Jobs defines good jobs in terms of : ***Good jobs for development:***

those that **raise living standards**, have **high levels of productivity**, and

improve social cohesion through positive social externalities

→ ***Virtuous cycle of higher incomes, higher productivity
and greater inclusion***



How does the more/better/inclusive jobs agenda intersect with informality?

➤ More

When economies grow, more (formal) jobs are created ↔ when more (formal) jobs are created, economies grow

- More people are working → higher incomes → increased demand for goods/services → more jobs (some of which are more productive and formal)

➤ Better

At the firm level, informal firms that can invest and upgrade/expand can increase productivity and access markets:

→ more sales, hire more workers, pay higher wages and/or offer better benefits

At the worker level, self-employed farmers and micro-entrepreneurs who raise their productivity through better market access/input quality/business management/technology:

→ higher earnings, more saving and/or investment

➤ Inclusive

When excluded groups are connected to work:

→ HH living standards rise and poverty falls, contributing to better social outcomes and stronger, more cohesive communities