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Thematic briefing note on the informal economy and decent work

1. UNDERSTANDING THE INFORMAL ECONOMY

The **informal economy** is receiving large and renewed interest from the development community as it provides for the majority of the employment opportunities in most developing countries. Despite the fact that there is not a universally accepted common definition of what the informal economy is, there is however, a broad understanding and consensus of its implications and its main components and patterns. Generally, the informal economy is understood as all activities that are performed outside the formal structures that govern taxes, workplace regulations and social protection schemes. Following the conclusions of the ILO International Labour Conference in 2002, the informal economy can be understood as comprised by **informal employment** both inside and outside informal enterprises¹.

The introduction of informal employment as the main concept of interest indicates a shift of focus from informal enterprises to informally employed individuals. For development cooperation, this is an important shift of thinking as it put the needs and concerns of the poor workers in the centre. Issues such as equity, access to employment opportunities and rights of informal workers are gaining importance on the development agenda. Earlier, a large part of the discourse was concentrated upon formalisation and issues such as registration and tax evasion of enterprises, which not necessarily are poverty-reducing.

Earlier considered as a transitional phenomenon that economic growth itself would eliminate, informal employment has become a structural feature of development that has been persistent and even increased in most of the countries of the world regardless of their level of economic development. The main reasons underlying this situation

¹ The International Labour Organisation (ILO) and the International Conference of Labour Statisticians (ICLS) have made some attempts to define informal work. Following the conclusions of the ILO International Labour Conference in 2002, the informal economy is defined as all economic activities by workers and economic units that are in law or practice not covered or insufficiently covered by formal arrangements¹. This is an update and an expansion of the definition of the **informal sector** that ICLS adopted in 1993. The informal sector was defined as all employment in unregistered micro-enterprises. The ambition of the ILO and the ICLS has been to move towards a definition that focuses on individuals informally employed rather than on informal enterprises. In 2003, ICLS defined **informal employment** as all informal jobs regardless if they are carried out in formal or informal enterprises or in households.

are the inability of economies to create sufficient numbers of formal jobs, policies leading to labour market segregation, avoidance of high taxation and social security contributions or distrust in governance of public institutions. More recently, an increase in subcontracting driven by globalisation has led to greater diversity in the forms of informal employment. The financial and economic crisis is likely to further emphasise this development.

The informal economy includes a wide variety of activities, enterprises and workers. The most visible part of the informal economy is people selling goods and providing services on the streets. Other large parts, but maybe less visible, include workers in small factories and workshops, people, often women, working with small-scale production at their homes, and casual day labourers in agriculture and construction. However, the informal economy also includes people that are fairly well off such as employers of smaller firms. **Understanding the informal economy means to recognize this diversity and to address the needs and the challenges the different parts of the informal economy are facing.**

The two main categories of informal employment, wage employment in jobs without social protection and self-employment in unregistered enterprises, can be further disaggregated into different categories of employment relationships. Self-employment consists of employers of informal enterprises who hire other workers and own-account workers. The conditions of these two categories are often very different. Wage-employment includes informal employees of both formal and informal firms, subcontracted workers, wage workers for households (domestic workers), and wage workers with no fixed employer (casual day workers).

Informal employment is often casual, irregular or seasonal implying frequent changes of workplaces and employers. Informal workers experience often poor working conditions such as long working hours, high level of health hazards and lack of social security (protection) usually accompanied with poor earnings, low productivity, lack of access to training and lack of legal protection and rights at work. Disadvantaged groups such as women, young workers, people with HIV/AIDS, disabled, indigenous people or migrants are overrepresented in the informal economy.

In recent years, a debate originating from Latin America has focused upon to which extent informal employment is based on the choice of the workers, if informality is a result of exit or exclusion from the formal economy². For some Latin American countries, data indicates that a significant share of informal workers prefers to be informal and does not wish to become formal. The preference of being informal is explained by poor governance and that formality is not associated with any substantial benefits. However, it has been argued to what extent this is a “real” choice and not related to the limited alternative options available for informal workers. This cause of informality is likely to vary very much between different country contexts.

2. TRENDS IN INFORMAL EMPLOYMENT

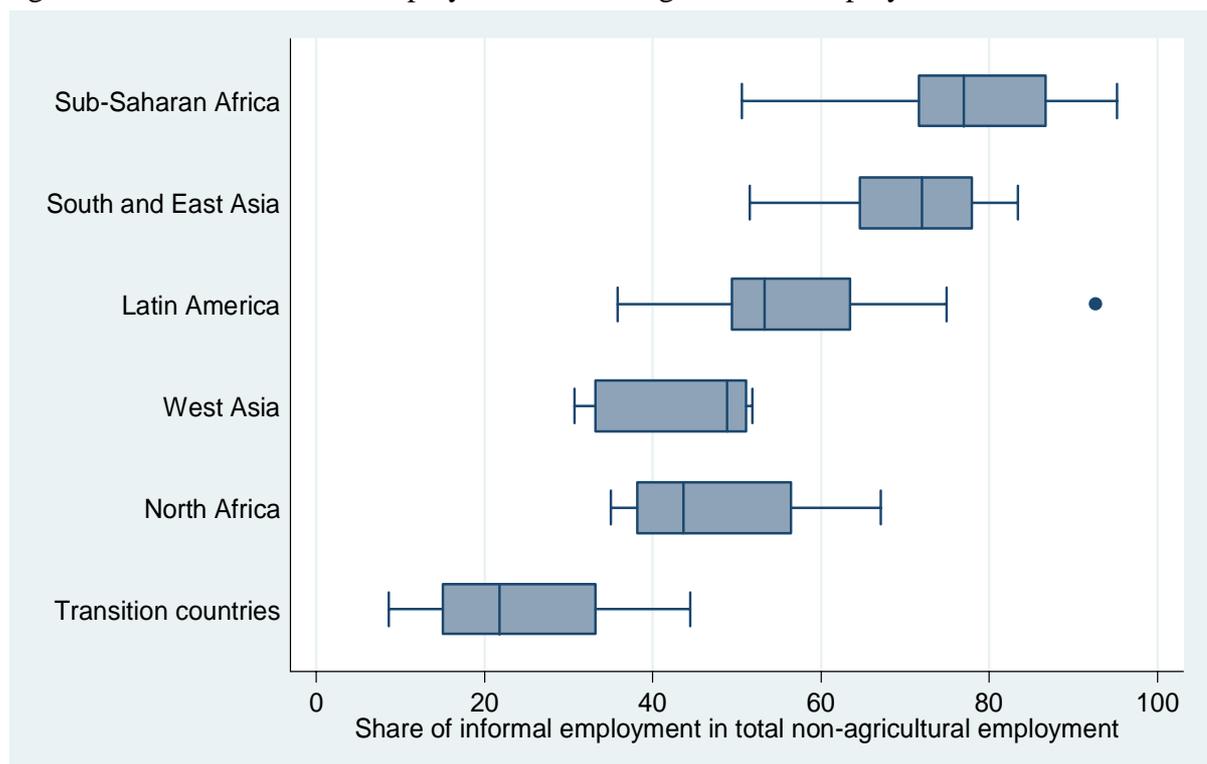
Over the world, more than half of all jobs in non-agricultural sectors in developing and emerging economies can be considered informal. In some regions, including sub-

² Perry et al. (2007) *Informality: Exit and Exclusion*, World Bank.

Saharan Africa and South Asia, this rate is as high as 80 per cent. If informal employment in agriculture is included, this share is even higher reaching 90 percent of employment in some regions. However, mapping the informal economy to understand its size, composition and evolution is a difficult and imprecise exercise given the lack of available data about many aspects surrounding informal employment. This lack of data hinders the development of policy responses and to some extent limit the focus of informal employment in national policy making. To further put emphasis on informal employment, one main priority is therefore **to strengthen the knowledge base and to develop statistics that are comparable across countries and sectors.**

The size of informal employment varies between different regions of the world (see Figure 1). Sub-Saharan Africa and South and East Asia have the highest levels of informal employment. In Latin America, the share of informal employment reaches 50 percent of total employment in most countries. Also in North Africa and in the Middle East, informal employment is a large part of the total non-agricultural employment. The size of informal employment is lower in transition and developed countries. However, informal employment shares of up to 20 percent is not uncommon also in more developed countries.

Figure 1. Share of Informal Employment in Non-Agricultural Employment



Source: Charmes, J, (2009), “Concept, Measurement and Trends”, in J. Jutting and J. de Laiglesia (eds) *Is Informal Normal? Towards more and better jobs in developing countries*, OECD Development Centre, Paris.

Note: The box chart shows the range of informal employment as share of total non-agricultural employment by region, based on the latest observation for available countries. The edges of each box correspond to the upper and lower quartiles, with the vertical line inside indicating the median value for each region. The ‘whiskers’ outside the box show the upper and lower adjacent values of the data. The outlier value in Latin America is Haiti.

Following estimates from the ILO, unemployment, working poor and vulnerable employment is expected to increase dramatically in 2009 in the current context of economic recession and global financial turmoil. The figures show that 50 million people may lose their jobs if the situation continues to deteriorate. The informal economy should not be seen as a cushion for losses of formal jobs. Instead, this will lead to larger competition for jobs in the informal economy and lower income-generating possibilities for large numbers of informal workers.

3. DECENT WORK AND THE INFORMAL ECONOMY

Originally developed by the **International Labour Organisation** and having been endorsed by a wide range of international stakeholders including the European Commission, the concept of **decent work** is based on an integrated approach of four pillars covering productive employment, rights at work, social protection and social dialogue. The 2008 ILO *Declaration on Social Justice and Fair Globalization* emphasises that these four components of decent work are “inseparable, interrelated and mutually supportive”.

In order to promote decent work within the informal economy, a comprehensive and integrated strategy cutting across a range of policy areas should be implemented. At the same time, the significant job creation and income-generation potential of the informal economy should not be destroyed. Efforts need to focus on addressing decent work deficits for workers and entrepreneurs in the informal economy with the objective to improve their productivity and working conditions, which will put them on a path towards the formal economy.

The **European Union**, in line with its international commitments, has adopted a number of documents and statements where it supports the promotion of decent work in its external and development assistance cooperation. The European Consensus on Development³ defines social cohesion and employment as one of its nine areas of priority action. It underlines that the EU is committed to promote decent work for all in line with the ILO agenda. The European Commission released a communication on promoting decent work for all in May 2006⁴ and decent work is equally an element of the internal and external dimension of the EU Lisbon strategy for growth and jobs⁵. The informal economy is a central theme of the EC Staff Working Document *Promoting Employment through EU Development Cooperation* it is emphasized that whereas the focus in the formal economy must be on creating more jobs, the centre of attention in the informal economy should be to raise earnings and productivity and improve the, very often poor, working conditions and to increase social protection coverage.

The **United Nations** has adopted declarations and resolutions committing member states to the promotion of decent work for all. In that respect, the UN Summit on the

³ See: <http://europa.eu/scadplus/leg/en/lvb/r12544.htm>

⁴ http://ec.europa.eu/employment_social/news/2006/may/com_2006_249_en.pdf

⁵ See: http://ec.europa.eu/growthandjobs/index_en.htm

Follow-up to the Millennium Declaration (MDG +5)⁶ in 2005 endorsed the need for a fair globalization and for the goals of full employment and decent work as part of the UN development agenda. A new **MDG target**, under MDG 1 *Eradication of extreme poverty and hunger*, of achieving full and productive employment and decent work for all including women and young people was added. The corresponding indicators are to a large extent designed to capture also labour market developments in the informal economy. They include the share of working-age population that is employed, the proportion of working poor, and the proportion in unstable, insecure jobs.

In May 2009, **OECD-DAC** issued a policy statement *The role of employment and social protection – making economic growth more pro-poor* that states that “policies that recognise and improve conditions in the informal economy, where most poor women and men earn their livelihoods, are critical to poverty reduction”. It stresses that measures such as skills development, the promotion of entrepreneurship and improving working conditions must be designed for delivery and impact also in the informal economy.

Similar concerns have equally been taken up at the regional level. Several regional entities such as the African Union, NEPAD, the Organisation of American States, the Andean Community or ASEAN have adopted resolutions and statements committing to the promotion of decent work.

4. DECENT WORK DEFICITS IN THE INFORMAL ECONOMY

The main challenge is to support workers and operators in informal economy to move up to the continuum to decent work through addressing and mitigating decent work deficits.

In order to do so, the wide diversity of the informal economy needs to be taken into account and special attention needs to be put on the most disadvantaged vulnerable groups, namely, women, young, people living with HIV/AIDS, disabled, indigenous people or migrants. **The policy response needs to be based on a policy mix of actions in the different pillars of decent work targeted at the specific needs of different categories of informal workers.** That is, addressing the decent work deficits of specific categories of workers, such as street vendors, home workers, small-scale entrepreneurs et cetera. The actions should not ignore the presence of child labour⁷, as it is mostly within the informal economy where we find the most hidden and hazardous forms of child work, including forced labour and slavery.

A policy agenda for the informal economy should aim at addressing the central decent work deficits within the four pillars of the decent work agenda.

PILLAR 1: Creation of decent employment opportunities

- **The legal and regulatory framework** needs to be adjusted to the constraints and realities faced by informal economy operators. Often, the existing

⁶ http://www.un.org/ga/59/hlpm_rev.2.pdf

⁷ See: ILO's International Programme on the Elimination of Child Labour (IPEC) <http://www.ilo.org/ipeclang-en/index.htm> and the ILO Global Report “The end of child labour: within reach”.

regulatory framework has been designed to cater for the needs of larger firms. The costs for the establishment and the operations of small business are often too high and the benefits of legal registration too low to make it attractive or even possible for many, or most informal operators to comply with difficult or prohibitive rules and regulations. This also includes transparency and consistent application of regulations, as harassment, bribery and extortion practiced by public authorities are common problems faced by informal operators.

- Basic literacy, employability and adaptability are critical for workers to access better jobs, improve productivity and income in the informal economy and in particular to move into formal decent jobs. Informal workers, and potential future informal workers, have little **access to education and training**, in particular development of vocational skills. Main issues to be addressed include a strengthening of the link between the formal training system and the informal economy, the scaling up of pilot initiatives targeted at informal workers, development of training needs assessments taking into consideration the opportunities and the needs of informal workers and enterprises, and recognition of skills of informal workers.
- The absence of **legal property rights for the poor**, including intellectual property, means that potential entrepreneurs are not able to use, build, recombine or exchange their assets in the most productive way in order to create added value. Without being able to convert assets into productive capital, they do not have the means for entrepreneurship, innovation, business growth or development. It is critical that sound regulations ensuring property rights for the poor are in force. It is also essential that financing can be obtained in good terms and within the reach of informal micro-entrepreneurs and potential entrepreneurs.⁸

PILLAR 2: Rights at work

Fundamental rights at work are internationally recognised human rights and apply to all workers regardless of their employment relationship or the formality status. It is important to understand and highlight that there cannot be a lower level of rights for informal workers. The fundamental principle is that all those who work have rights.

- The eight ILO conventions establishing **core labour standards** must be promoted by all means possible. The labour standards must be implemented in a way appropriate to national circumstances and capabilities. The introduction of better working conditions in the informal economy needs to be progressive. It is essential to extend basic minimum standards on matters such as conditions of work, occupational safety and health and income security, as well as basic rules of fair treatment.⁹
- A major factor in addressing the labour rights deficit in the informal economy is the constraints that the **labour administration** faces. Labour inspection

⁸ <http://www.undp.org/legalempowerment/>

⁹ See thematic briefing note on core labour standards.

services are not often properly staffed or equipped to be able to effectively enforce standards and the existing systems of labour tribunals are often very weak, lack resources and experience endemic corruption. Other constraints that informal workers face are the inaccessibility to justice or the affordability of legal services. It is also essential that informal workers are aware of their rights and entitlements and to know how to claim these rights and seek recourse as a matter of legal literacy. Since the nature of their employment is very precarious, informal workers are often reluctant to seek justice when their rights are violated.

PILLAR 3: Social protection

Social protection is an internationally recognised human right. The lack of social protection is a key characteristic of the informal economy with millions of informal workers worldwide lacking access to formal mechanisms of social protection. Paradoxically, the workforce in the informal economy is the one most in need of social protection, not only because of the precariousness of their employment and the uncertainty of their income but also because of a greater likelihood of being exposed to occupational safety and health hazards.

- **Social protection directly reduces poverty and strengthens social inclusion of the working poor in the informal economy.** It contributes to build human capital, better management of risks, promotion of investment and entrepreneurship and improve participation in labour markets. Social protection can be affordable even in the poorest countries. The ILO promotes the right to basic social protection for all. This includes basic health care benefits, income security for children, elderly and disabled, and targeted income support for poor workers¹⁰.
- Informal workers are generally very exposed to **occupational accidents, diseases and hazards**. National and local authorities do not often have adequate knowledge of the problems relating to health and safety in the informal economy. One challenge of improving occupational safety and health in the informal economy is to provide informal operators and workers with information and guidance on measures that can be taken to reduce risks. Training is a critical instrument to raise awareness and improve work practices within informal economy and should be mainstreamed through non-formal education programmes in order to reach informal workers where they live and work and respond to their real needs.

PILLAR 4: Social dialogue

Workers in the informal economy are excluded from or under-represented in social dialogue institutions and processes.

- Government policies and national legislations are key elements in determining the enabling environment for **freedom of association** of those in the informal economy. The most important role of governments in this regard is to

¹⁰ See: <http://www.ilo.org/public/english/protection/secsoc/step/about/index.htm>

guarantee the effective freedom of all workers and employers, irrespective of where and how they work, to form and join organisations of their own choosing without fear of reprisal or intimidation.

- Even if organisations of informal workers exist, they often are faced with problems of getting **recognition**. A major problem faced by informal economy organisations is their lack of defined interface with those with whom they need to dialogue. Without recognition by government authorities, informal organisations have no voice in public policy debates or access to the services and infrastructure they need to operate effectively and efficiently. This is particularly important at the local level to provide local interest groups of informal workers an avenue for voicing their concerns and priorities and take part in policy debates.
- **Capacity building** is important to further strengthen and empower interest groups in the informal economy. Some good practices exist in successful development of interest organisations of informal workers. The most famous example is the Indian trade union SEWA (Self-Employed Women's Association)¹¹ that has been a pioneer in the field of organizing and empowering workers in the informal economy. At the global level, a set of networks for sharing information and practises between interest organisations of informal workers have been established recently such StreetNet International, HomeNet South Asia and HomeNet South-East Asia that includes organisations of street vendors and home workers.

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¹¹ <http://www.sewa.org/>