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Social Protection and the Informal Sector in Developing Countries: Challenges and Opportunities

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Preface

There is a renewed concern for social protection in recent years in both the developed and developing world, in part due to the growing trend toward informalization in the labor markets, but more importantly due to a rise in the level of poverty in several countries. Globalization, reflected in increasing trade and capital flows between countries, combined with changes in technologies also seems to have aggravated this concern. Countries in transition toward a market economy are also faced with a similar problem owing to changes in institutions, and the consequent difficulties in adaptation at the firm and household level. Public schemes like 'social safety net' have sought to minimize the insecurity confronting the population, at least in the short term, with limited success. Labor standards have likewise sought to improve income security for workers in the long run through a variety of measures ranging from unemployment benefits to health and old age security. With an increasing share of the labor force outside the formal labor markets, such protective security is not available or accessible to all workers. The need for more effective approaches and instruments toward social protection is therefore evident.

This paper consists of two parts. The first part identifies the sources of income insecurity and vulnerability among workers in the so called informal sector in developing countries, all of whom, by definition, are excluded from the formal labor market, and hence ineligible to the conventional forms of protection. This sector accounts for an increasing proportion of employment in these countries. Since there is a strong overlap between poverty among households and employment in this sector, measures to provide social protection to these workers would also benefit large sections of population in these countries. This paper examines alternative approaches to social protection for the informal sector. It is argued that attempts to extend orthodox social protection measures to those in the informal sector in developing countries are unlikely to succeed in providing effective protection, and a more comprehensive approach is required because much of the income insecurity for them is derived from their informality.

The second part deals with the challenge of developing a comprehensive approach to social protection for the informal sector. Arguing that the narrow constructs that characterize

many current programs that “target” the informal sector need to be broadened, this part of the paper uses two recent comprehensive approaches that have been put forward by the World Bank to assist the poor and excluded – namely World Development Report (WDR) 2000/1 on “Attacking Poverty” and Social Protection Sector Strategy Paper on “Social Risk Management”. It discusses in detail what it means to move towards this broader approach and explains how various policies, programs and regulations which have hitherto not treated the informal sector needs can indeed be used to provide effective social protection for the informal sector. It then discusses what such a broader perspective entails for the World Bank and other donors and explores how World Bank’s lending and non-lending instruments can be used to provide comprehensive social protection for those in the informal sector. This paper not only highlights the challenges but also the opportunities for extending social protection on a sustainable basis.

The authors wish to thank the participants of a seminar at the World Bank in which a draft version of the paper was discussed in May 2002. They would also like to acknowledge with thanks the constructive suggestions received from Marty Chen of WIEGO and Vijay Kalavakonda of the World Bank. The comments revealed that there is a need to extend the ideas contained in this paper to specific target groups within the informal sector as the structural causes of risks and opportunities facing them differed considerably. It also became clear that there are a number of stakeholders in extending social protection to those in the informal sector who play a critical role. Given the exploratory nature of this paper, these issues will be the object of future work in this area.

This paper is the outcome of a collaborative work between Mr. Sudharshan Canagarajah of the Social Protection Unit of the World Bank and Mr. S.V. Sethuraman (Consultant) funded by the Professional Development Grant of the World Bank. Mr. S.V. Sethuraman was responsible for the first part of the paper, and Mr. Sudharshan Canagarajah, for the second. In view of the exploratory nature of the paper, it is intended primarily to stimulate discussion and invite comments.

Social Protection for the Informal Sector: The Issues

Sudharshan Canagarajah and S.V. Sethuraman*

PART I

1. Introduction

Ever since the emergence of a market economy during the 19th century, providing social protection to workers has remained a major concern among the developed countries. In recent years this has become an area of concern in the developing world too, presumably due to a rise in the level of poverty in several countries, attributed to a variety of factors including poor economic performance in these countries. The proximate causes behind this increased concern for social protection is however believed to lie in the changes in the labor market. The quality of employment, measured in terms of wages and conditions of work, is believed to have worsened in most countries. The rate of unemployment has not only been significant but may have worsened too in several countries, in part due to growth and change in the structure of labor force, attributable to demographic factors.¹ Underemployment, as reflected in either part-time and casual work, or as measured in terms of income, appears to have risen too.² Further, firms are believed to be relying increasingly on labor outside the factory premises i.e., homeworkers who operate on a sub-contracting basis, and hence without protection envisaged in the labor laws.³ This trend toward "informalization" in the labor market viz., increasing proportion of "poor quality" employment, in both developed and developing countries, explains the increasing concern for both job and income insecurity among workers. Informalization in the labor market is in part derived from the increasing competitive pressure in the global markets, which has forced firms to minimize costs, especially labor, by avoiding high payroll taxes and social security contributions. This has been made possible in part by the weakening power of trade unions in

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¹ ILO (2000)

² Standing (1999), pp.105-106

³ In the European member countries, for example, "over 12 percent of the employed usually or sometimes worked from home...". Standing (1999), p.109

most countries. Greater capital mobility across countries in recent years, besides contributing to greater volatility in investment and production, and hence employment, is also believed to have aided this process. New technologies have also played a role because they made more flexible forms of work possible. Labor regulations, because they constrained the freedom to shed redundant workers, have also encouraged firms to avoid hiring them on a regular basis; by keeping them as contract workers outside the firm they have greater flexibility. Changes in trade and technology, accompanied by greater global linkages between nations, are thus seen as posing a threat to workers' income and social security, especially in the developing world.

Perhaps a more important reason behind the renewed concern for social protection, especially in the developing countries, is not the informalization of the formal labor market, but the rapid expansion of what is known as the "informal" economy or sector, which implied low income and poor conditions of work, as the discussion later will show. This is in part the result of weak growth in "good quality" jobs. Formal employment in the organized private sector and in the government, which by definition is of 'good' quality because they respect the labor standards, failed to grow rapidly in most developing countries; in fact it stagnated or declined in many. Diminishing role of the state, reflected in the falling share of public sector employment, also no doubt contributed to this trend. This, combined with labor force growth and poverty in these countries, led many new entrants to create jobs on their own, either by establishing small and micro enterprises, or as independent service workers i.e., the informal economy. To be sure, growth of such 'informal employment' in these countries is also in part *demand* driven. The substantial presence of low-income population in these countries provided a market for goods and services albeit of poor quality, and hence at low cost. In other words, many individuals have found it profitable to engage in their production and distribution in spite of fierce competition, even though they had little capability.

The net result of the above trend has been an increase in employment but of a poor quality i.e., lacking both income and social security that are characteristic of the formal economy. This is because the informal economy functioned mostly *outside the accepted institutional framework*, and hence beyond the reach of most conventional social

protection schemes. Because most of the poor households in these countries depend on this sector for income and employment their income security depends on that of these workers.⁴ The need for social protection however varied within the informal sector because some worker categories (e.g., women) are exposed to greater risks and insecurity than others. Lacking access to *formal* social protection measures, these workers had no choice but to develop their own informal or indigenous mechanisms of social protection. The challenge in extending formal social protection schemes to these workers is therefore evident. As a recent publication of the ILO - *World Labor Report 2000: Income security and social protection in a changing world* pointed out, designing effective social protection measures for workers in the informal economy does indeed pose a formidable challenge to policy makers in these countries.⁵

This paper explores the question of social protection to workers in the informal economy mainly in the developing country context, though its conclusions are likely to have wider relevance. Since the issue is sometimes clouded by ideological or emotional overtones the paper attempts to clarify the issues and put the debate in its proper perspective. It is intended primarily to stimulate discussion on what constitutes social protection for these workers, which hopefully will shed some light on how to go about in addressing the problem. The section below briefly discusses the terminology 'informal sector' in these countries, and identifies the sources of income insecurity for its workers. The meaning and significance of social protection as well as current attempts to extend it to workers in the informal sector are examined in section three. The fourth section presents a critical appraisal of the current thinking and approach toward social protection, especially their relevance and adequacy for the informal sector. The last section raises issues for reflection in shaping a strategy for the future.

2. The Informal Sector in the Developing World: A Selective Review

A distinguishing feature of employment in the developing countries is that it varies enormously in terms of quality and other characteristics, compared with the developed countries. A substantial proportion of the labor force in these countries is in the rural areas, engaged primarily in agriculture, which is dominated by small and subsistence farming.⁶ Due to low and

⁴ Though there is a strong overlap between poverty and the informal sector not all those in the latter are necessarily poor; nor are all the poor in these countries in this sector.

⁵ ILO (2000)

⁶ See for example ILO (1998), Statistical annex, Table 3

unpredictable incomes many are also employed as wage labor. Most of such employment occurs outside the regulatory framework, with little control over the conditions of work and remuneration. Outside agriculture, the bulk of the employment is not created by economic agents that operate within the framework of law as in the developed countries. A substantial part of production and distribution occurs in the informal economy⁷ where enterprises (or agents of production and distribution) remain outside the *recognized institutional framework*.

What is the informal economy?⁸

The informal economy consists of all economic activities that remain outside the official institutional framework. Consequently the governments have little *control* over the quality of employment.⁹ In fact they do not even have statistics on them. For purposes of the present paper the term ‘informal economy’ is defined to exclude agriculture mainly because it requires a somewhat different analytical treatment (see below). There are a variety of reasons why these activities fail to conform with the institutional framework. A vast majority of the enterprises that engage in production and distribution in these countries tends to be very small, as the individuals who start them are often ill-equipped in terms of education and skills, and possess few resources for significant physical investment such as premises and equipment, and machinery. Consequently they are either unaware about the regulations and the procedures for compliance, or are unable to comply with them owing to resource constraints. Low incomes, for instance, oblige these small producers to avoid compliance with the existing institutional framework because full compliance with all the regulations involve significant cost, reducing their income substantially. Besides direct financial cost, it also involves time and effort in overcoming the bureaucratic and administrative obstacles. More importantly, many are not sure about the benefits that they would get in return. Ambiguity in the regulations as well as in their enforcement, derived from weak institutional capacity, also no doubt explains non-compliance in these countries.

⁷ For an estimate of the size of the informal economy in selected countries see ILO (2000), Statistical annex, Table 7

⁸ The terms informal economy and informal sector are used in this paper interchangeably.

⁹ The institutional framework is generally defined to include not only regulations that govern the establishment and functioning of enterprises but also a host of other regulations such as labor, fiscal, and environmental, that they are expected to comply with. Typically it requires enterprises to be registered and licensed, which in turn bind them to respect other obligations.

Compliance with the regulations, one could argue, would have been better if these enterprises had access to resources and markets such as land and credit. Because of the frequent absence of organized markets, or due to imperfections in existing markets, these individuals who own and operate small and micro enterprises often find it difficult to access non-labor resources, especially credit, and land in large urban locations. Government policies and institutions have also frequently exacerbated the situation by rendering the access difficult, either due to interventions in the market or control over resources. Access depended sometimes on the enterprise scale. These enterprises, unlike their counterparts in the formal economy, also frequently faced *discrimination* in various markets; access is determined *not* by the characteristics of *enterprises* such as their economic activity and viability, but by the traits of *individuals* who own and operate them. This is unique to the informal economy as a large majority of small and micro enterprises is owned and operated by single individuals. Women, for instance, faced discrimination due to certain institutional practices derived from cultural, ethnic or religious considerations. Generally speaking age, sex, education, and ethnicity of individuals seem important determinants of access to credit and other resources. These constraints imply that they have to rely more on their own labor and personal savings, which explains their small scale and low revenue from business. Because of land related regulations these enterprises also have unclear title to land or premises on which they are located, making them *ineligible* for legal status.

Despite their informality i.e., remaining outside the institutionalized part of the economy, they are nevertheless able to exploit profitable production opportunities, which arise, as noted earlier, due to the existence of a market for a variety of products and services of low quality and low price - derived from the substantial presence of low-income households in these countries, and the resulting constraints on purchasing power. The markets these small scale activities try to reach are also such that they do not often warrant a larger scale of operation. These enterprises therefore choose technologies appropriate to keep the costs low viz., intensive in labor and other indigenous resources. Constraints on access to resources mean that they are not operating on an efficient scale, nor utilizing optimum technologies that would minimize the costs. Since there are few entry barriers, competition has also kept their income at the minimum, most of which being essentially returns to their own labor. These small and micro enterprises constitute

the "informal" economy or sector. Informality among these enterprises is thus derived from two basic criteria: *absence of legal recognition and the absence of access to organized markets and resources*.¹⁰

It would however be incorrect to conclude from the above that *formal* institutions alone are responsible for the emergence of an informal economy. Besides government regulations, customary laws have also played a role as they constrained operation of these enterprises; in some countries they determined land allocation, inheritance and succession, and property rights in general. In Zambia, for example, women are reluctant to expand their business for fear of losing their property to relatives after the husband's death. Women in sub-Saharan Africa lack title to land they cultivate; they often lack control over their income e.g., from cash crops; to obtain credit they are forced to rely on informal means like ROSCA (rotating savings and credit associations or the equivalent e.g., *tontine*, *susu*, etc.). In Zaire, for instance, women need the husband's consent and signature to open a bank account.¹¹ Clearly such "informal constraints" have also hindered the performance of small and micro enterprises in a significant way because of their exclusion from certain markets. Informal economy is in short the result of both formal and informal institutional constraints.

Heterogeneity of the informal economy

The foregoing discussion implies the existence of a dichotomy, formal and informal economy. Studies on the informal economy in developing countries over the last three decades have shown that such a characterization viz., dichotomy does not in fact correspond to the reality. According to the available evidence, most of the small and micro enterprises in these countries are neither formal nor totally informal by the criteria mentioned above; rather they are in between the two. This is because they often have "partial" recognition, and enjoy "partial" access to resources and markets. Legal status of an enterprise, for instance, is not determined by a single or *unique* criterion, but by a variety of regulations ranging from purely administrative rules to labor, fiscal and other laws governing business operation. It has been found that small and micro enterprises tend to comply with only some of them and not others, which assures

¹⁰It should also be noted that a small proportion of small enterprises that are quite capable of assuring wages and social protection to their workers as envisaged in the labor standards also "hide" in this sector mainly in order to gain pecuniary advantages.

¹¹ Sethuraman (2000), Chapter 2

them partial recognition by the authorities.¹² This choice of selective compliance can be explained by the *risk minimizing* strategies of the poor; where non-compliance threatens their very survival as a business they often choose to comply only with those regulations that matter viz., that improve their income and security. For example, enterprises with significant investment, and engaged in non-traditional activities, often find it costly to remain totally informal (i.e., invisible) because they require backward and forward linkages with the rest of the economy for efficient operation.

Likewise, the extent to which enterprises have *access to organized factor and product markets, public resources, information and opportunities* has been found to vary considerably, reflecting the extent of market imperfections including fragmentation and discrimination; some tend to enjoy greater access than others. Unequal access is also in part the result of ambiguous legal status i.e., institutional constraints, and a function of initial endowments of these individuals. Because of their *exclusion* from formal or organized markets they have to rely more often on "informal" markets e.g., credit and skills. Even access to informal markets is not easy as it frequently depends on the individual's access to 'social networks' (i.e., social capital) and other non-economic factors. Women for example have difficult access to certain networks and therefore have developed alternative networks of their own. These findings imply that there is no single criterion by which an enterprise can be classified as formal or informal. Instead, enterprises vary in their "*degree of informality*".¹³

There is thus considerable heterogeneity within the informal economy depending on the *incidence of informality* in enterprises. Those that are very small, owned and operated by individuals with little or no schooling, by women, and by the poor tend to be more informal.¹⁴ In other words there is a whole range of enterprises with varying degrees of informality, with informal economy at one end of the spectrum, and formal at the other. This means one can define the informal economy as narrowly or broadly as one wishes. This also implies that the *cost* of remaining informal (discussed below) is relatively higher for certain categories of

¹² For evidence on this from sub-Saharan Africa see for example Sethuraman (2000), Chapter 3; and Maldonado et al., (1999)

¹³ It is not possible to classify the degree of informality as the extent of formality or informality among enterprises varies continuously in terms of a number of indicators. They may be visualized as lying on a spectrum varying from formal at one end to informal on the other.

¹⁴ See Sethuraman (2000), Chapter 2 for more details.

workers; risks, constraints and opportunities facing those in the informal economy thus vary. *Insecurity defined in terms of insufficient income and vulnerability seems to be greater for certain categories of workers.* Since income insecurity and vulnerability vary directly with the extent of informality (see later discussion), the *need* for social protection varies too.

Increasing importance of the informal economy

These activities in the informal sector account for a substantial share of total employment in the developing countries - ranging from a third to two thirds or more, particularly in urban areas.¹⁵ They also make a significant contribution to the GDP. National level data on employment and income generated in the informal economy is generally not available. India is one of the few exceptions where it has recently been estimated that the informal sector (including agriculture) accounted for 80 percent of all male and 92 percent of all female employment, and 68 percent of the net domestic product.¹⁶ In Ahmedabad city (India), for example, 77 percent of all employment and 47 percent of all valued added are estimated to originate from the informal economy.¹⁷ The informal economy is also believed to be rising rapidly, partly due to poor performance in the rest of the economy, especially in sub-Saharan Africa.

Globalization measured in terms of trade and capital flows between countries, and technological change is believed to have played an important role in the process, as already noted. They may have intensified competition among firms, driving down labor costs. Since these costs are lower in the informal economy, as they generally do not comply with labor regulations such as legal minimum wage, social security contributions and other provisions, an increasing proportion of employment in these countries is believed to be informal. In South Africa, for example, women retrenched by textile and garment industries are now in the informal sector, as petty traders.¹⁸ Increasing international trade likewise appears to have created more employment for women especially in Asia and Latin America, but mostly in the informal sector. Many of them are engaged as homeworkers, operating on a sub-contracting basis - without adequate social protection.¹⁹ Improvements in technology are also believed to have contributed

¹⁵ For a recent estimate of the size of the informal sector and its contribution to GDP in selected countries see Charmes (1998)

¹⁶ Sudharshan (2000)

¹⁷ Unni (2000)

¹⁸ Lund et al., (2000)

¹⁹ ILO (1994)

to such informalization of employment as it opened up new possibilities for increased division of labor.²⁰ Poor economic performance, resulting from poor management, especially in sub-Saharan Africa, has also led to a rise in informal employment following the implementation of structural adjustment programs and retrenchment in the public sector and the organized private sector.²¹ Rising poverty in several countries has encouraged women participation in the labor force, especially in the informal economy, which is also partly due to discrimination in the formal labor market. These trends implied a relatively higher growth of female employment in the informal sector.²²

Scope of the informal economy

Before proceeding with further discussion on the salient features of the informal economy and its significance for policy as it concerns social protection, it seems necessary to clarify the scope of these activities. The term informal economy, though applied in principle to all branches of economic activity, has in practice been applied in the empirical literature mostly to the non-agricultural sector. This is because there is no evidence to suggest that formal institutions have been a source of hindrance, obliging farms to operate outside the framework of law, even though numerous subsistence farms co-exist along with large commercial farms. Unlike the non-agricultural sector where enterprises are expected to be registered and licensed, and comply with a host of regulations, there are no such obligations in agriculture because they have always formed part of the traditional economy and recognized as such. All farming activities enjoy equal legal status in these countries even though there is considerable heterogeneity in terms of size, organization and access to markets. Informal institutions on the other hand have sometimes imposed costs on certain farms due to discrimination. In sub-Saharan Africa, for example, small farms operated by women are known to be subjected to *informal* constraints. Even though government regulations have not discriminated between farms in terms of their legal status - because they generally have a clear title to land that they cultivate and hence are not 'informal' i.e., outside the law, most small farmers in the

²⁰ See for example Sethuraman (1998), pp.17-18. Indeed there is a vast literature supporting this view.

²¹ Sethuraman (2000)

²² For more on this see Sethuraman (1998)

developing countries are known to have difficulties in accessing resources such as credit and inputs.²³ Since market institutions have tended to discriminate between farms based on scale or other considerations (e.g., subsistence farms), one could argue that informality exists in agriculture too. The scope of the informal economy is however defined to exclude agriculture in this paper for reasons already mentioned.²⁴ By virtue of the fact that most non-agricultural activities tend to be concentrated in urban locations, it follows that the informal economy, as defined in this paper, is essentially an urban phenomenon.²⁵

Another caveat applies to the work force. The discussion above may have oversimplified the situation in that the informal economy is defined as consisting of only small and micro enterprises. This implies that its work force comprised those who own and operate these enterprises viz., heads or micro entrepreneurs, hired workers and apprentices, and unpaid family workers engaged in them. In practice there is a fifth category - known as independent service workers - consisting of those who neither have fixed activity nor work for a fixed enterprise or employer such as domestic servants, porters and other similar footloose workers, sometimes labeled as casual workers. Since their work is largely outside the recognized institutional framework in these countries, they are also considered as part of the informal sector. In some cases it also includes workers who are engaged not by enterprises but by households, as such employment remains unrecognized by governments in most countries. In Latin America for instance this is an important category. To illustrate, in urban Mexico in 1988, informal sector employment was distributed as follows: individuals operating an enterprise on own account, 37 percent; heads of micro enterprise who engaged workers, 8 percent; wage workers, 23 percent, unpaid family workers, 13 percent; domestic servants, 13 percent; and casual workers,

²³ See for example Tendulkar (1992) on India.

²⁴ Clearly there is a need to address the social protection concerns of those engaged in agriculture, which however is not attempted in this paper owing to time and resource constraints. Issues pertaining to this topic would have to deal with the institutional, structural, policy environment (as well as those derived from geographical / climate and ecological factors) and the risks they impose on workers. But based on the issues discussed in this paper one can draw an analogy.

²⁵ Arguments somewhat similar to those for agriculture also apply to rural non-farm activities. Institutions do not appear to have played a discriminating role because regulations enforcement in rural areas are generally weak; also few have a problem with access to land.

5 percent.²⁶ In discussing the social protection needs of the informal sector clearly all these worker categories matter.²⁷

A further distinction is often made within the informal sector between those who operate from their residence, and other micro enterprises. Not all those operating from their residence or home are truly independent enterprises, taking risks and making decisions; many, especially women, are paid for their work by "the employer, subcontractor, agent or middlemen" and hence considered as "homeworkers" or 'disguised wage workers'. In other words those who operate from residences consist of both home-based and homeworkers. In Ahmedabad city (India) in 1998-99, for example, of the total *female* employment in the informal sector, 32 percent belonged to home-based, and 24 percent to homemaker categories; corresponding figures for *men* were 3.3 and 2.5 percent respectively.²⁸ This also illustrates the *invisibility* and heavy dependence on sub-contracting, and hence the *increased vulnerability and insecurity*, of women, as they remain beyond the reach of the regulatory authorities. Since homeworkers do not interact directly with the market, they differ from other 'home-based' enterprises; and the sources of income insecurity and vulnerability are different. For homeworkers, their income and conditions of work are determined by the terms of contract with their 'employer' (or contractor), which is not governed by any labor standards or regulations in most developing countries. However, the ILO Conference in 1996 adopted a Convention and a Recommendation to protect homeworkers, which provides a basis for countries to develop new national guidelines or standards.²⁹ This tendency to engage workers outside the factory premises on a sub-contracting basis is widely seen, as already mentioned, as a process of "informalization", and interpreted as a means by which employers disown responsibility for their welfare envisaged in the labor standards.

²⁶ Sethuraman (1998), p.28

²⁷ From the point of view of social protection one should also consider those workers engaged by the large private firms that operate within the framework of law viz., the formal sector, but who are denied protection through the labor standards on the pretext of temporary, part-time or casual labor. Normally such violations should not exist, but in practice they do as many formal firms take advantage of the weak law enforcement capacity in these countries; they are able to get away from non-compliance because of the travesty of law.

²⁸ Unni (2000)

²⁹ Home Work Convention 1996 and Home Work Recommendation 1996

Informal economy: Some empirical magnitudes

There is a vast literature on the empirical magnitudes of the informal economy, a discussion of which is outside the scope of this paper. But one may summarize some salient features that are pertinent to the question of social protection. First, it is obvious that these enterprises are quite small, mostly below ten workers per establishment, the cut-off line commonly used for licensing and registration requirement viz., legal recognition in most countries.³⁰ In fact a vast majority of the enterprises (not employment) - anywhere between 65 and 85 percent - is owned and operated by single individuals, and hence quite small, with little or no capital investment, and hence low productivity and income. Second, a large majority are engaged in tertiary activities consisting of petty trade and service activities, though the proportion varies between the poor, medium and high income developing countries. In the poorest African countries for example they often tend to account for almost 90 percent. This concentration in low productive activities is in part a reflection of entry barriers to other more lucrative activities, which require not only more capital but also significant technical and entrepreneurial skills - which incidentally are also the ones that provide much of the wage employment in this sector. Conversely, it is the heavy transaction costs resulting from poor institutions that seem to explain this phenomenon. The concentration is also partly due to the *risk aversion behavior of the poor* as institutions in these countries have tended to enhance the risks and uncertainties in non-trade activities. Third, most of those who own and operate enterprises with significant amount of capital, funded through personal savings or informal credit mechanisms, have an income, according to the evidence, above the legal minimum wage mainly because of returns from capital, in addition to returns to labor. This means that a vast majority of those operating on own account with very little capital, or even without a premises, and those who are engaged as wage labor, earn below the legal minimum wage, and hence the most deprived, needing social protection. To the extent legal minimum wage reflects the minimum or subsistence income in the country concerned, distribution of workers by earnings or income provides an indication of the extent of income insecurity for workers. In many sub-Saharan African countries, for instance, the legal minimum wage has fallen in real terms in recent years, and hence such data may not

³⁰ This choice of ten may seem arbitrary; it could be any number that signifies the inclusion or exclusion from the institutionalised part of the economy, which no doubt varies from country to country.

reveal the true extent of income insecurity. These findings have a significant bearing on the design of social protection schemes for these workers.

Fourth, because they are mostly urban, these enterprises face serious constraints in accessing land or space; where land markets exist and function, few can afford to own or rent because of land scarcity. Zoning and other land related regulations may have further aggravated the situation by limiting the space available, or by imposing heavy transaction costs. Many are therefore driven to operate businesses out of their residence, or in the residential neighborhoods, or in other invisible locations including slums, and other marginal areas e.g., in the fringes of urban areas like hill slopes, beside train tracks, garbage dumps and so on. This implies that they lacked direct contacts with markets, as they were obliged to rely on intermediaries. Finally, the activities also differ in their objectives; some seek to maximize current income while others focus on the long-term goal of maximizing business assets through enterprise development. Women for instance are believed to engage more frequently in petty trade or services in order to supplement household income, and hence are considered as part of the *survival* economy - as opposed to the more productive activities like manufacturing that have a potential to grow. This however contradicts the finding that a rising proportion of women are also the main bread-winners in these economies.

Consequences of informality

Scarcity of land (or space) for business, besides pushing individuals to marginal locations and condemning them to 'invisibility' (i.e., operating from residence), has also induced them to violate property rights through encroachment of public and private property and assume the attendant risks - encouraged in part by the ambiguities in the law. It would seem in retrospect that such action has paid off, even though they may have become more vulnerable in the process, exposed to bribery and threats of eviction from regulating authorities. Their success is in part due to the weak law enforcement capacity in these countries. In many African countries it is explained by the absence of a land market and unclear property rights. These survival or coping strategies of the poor have helped them to avoid starvation, if not earn income above the poverty line. Another implication is of course that those who managed to acquire space earlier derive a substantial part of their income in the form of rent, and therefore relatively well off. These imperfections in land markets have no doubt significant efficiency and welfare costs.

Perhaps the most significant consequence of lack of access to land on a legal basis has been that a substantial proportion of these activities are *ineligible* for legal status and hence recognition by the state, as mentioned earlier. It is one of the major deterrents to becoming formal.

This has a cascading negative effect on these enterprises because, without a clear title to land or space they occupy, they are also denied access to credit from banks as well as assistance schemes funded by the government. In several sub-Saharan African countries, for example, it also implied lack of access to other key inputs including those imported, and other raw materials (e.g., products from forests and mines) as their supply was often controlled by the state directly or indirectly. *In other words, informality compounded by market imperfection, not only rendered these activities less viable but also their participants more vulnerable.* Their ability to compete in the market is diminished, especially against some products and services of the formal sector, which tends to enjoy a favored treatment in the policy framework in many countries, or against imports that are made artificially cheap by overvalued exchange rates. They are unable to minimize the cost; nor are they able to diversify their output. They have few incentives to accumulate capital, acquire skills, and improve technology.

This also raises questions about some of the current efforts that have tried to promote investment in human capital like skills and education. Can they succeed, in the absence of a more favorable environment facing these activities i.e., low returns to investment in skills and assets? In other words it is not always the deficiencies in the supply mechanisms that is holding back investment in this sector. It is also a question of adequate returns to such investment that matters.³¹ The need to make the environment facing these informal producers more friendly is therefore evident.

Lack of access to resources has often forced individuals to turn to ‘informal markets’ or seek employment based on sub-contracting relationship. Often they have to borrow at exorbitant rates of interest from money lenders or merchants though some have relied on informal mechanisms such as ROSCA mentioned earlier. Others have resorted to sub-contracting work because the contractor advances the inputs and markets the output, but at a

³¹ See for instance Bigsten et al., (2000) for evidence on factors constraining returns to human capital in manufacturing sector in selected sub-Saharan African countries.

price - unfair terms and conditions, derived from unequal bargaining strength. These and other consequences of being informal (see discussion in the next section for more on the consequences) obviously increased the income insecurity of individuals as well as their vulnerability. This suggests that measures to improve social protection should be concerned with ways to eliminate informality. But should they be aimed at the most vulnerable groups only, or all those participating in this sector?

3. Social Protection and the Informal Sector

Background

Although it was not defined in those terms, the origins of social protection can be traced back to the Poor Law of 1601 in England, which aimed at providing work to every able bodied person; and it was the responsibility of the parish to provide such work, which was empowered to mobilize the necessary resources through 'taxes or rates' on land and other property. This, together with other statutes pertaining to labor, known as the Code of Labor, provided the framework for social protection in England, though it placed restrictions on labor mobility and wage determination. In the modern sense of the term it however made its appearance only in the early 19th century when the laws protecting labor hitherto were abolished, and labor assumed the character of a commodity, freely bought and sold in the market - which implied, as Karl Polanyi put it, that human beings were deprived of their "protective cover" derived from their social and cultural institutions. Though labor was now free to move, it also lost the guarantee to employment and minimum income, or the 'right to live' as it was sometimes called, provided by the earlier laws. This change towards a 'market' economy, necessitated by the Industrial Revolution and the ensuing expansion of industry, exposed labor to new risks in terms of labor mobility and wage flexibility, which a variety of new social and labor legislation sought to minimize. Doubtless such a change also provided workers new opportunities for higher wages in the urban setting.

Social protection in the developed countries, which has evolved over years, thus consisted of measures that gave workers *freedom to organize themselves into trade unions* to safeguard, defend and advance their interests, especially through increased bargaining strength, leading to better wages and working conditions. They also included *factory laws* to ensure worker safety, and *labor regulations* that defined not only the conditions of work such

as limitations on hours of work, rules regarding dismissal, maternity benefits and legal minimum wage but also the employers' liability with regard to employment related injury caused to workers, and responsibility for old-age security in the form of social security contributions and for insurance against unemployment or *social insurance*. These measures, which aimed at safeguarding the human character of labor, laid the foundation for extending social protection to workers in the formal or organized sector consisting of enterprises that functioned within the framework of law, or the legal institutional framework. Notwithstanding their comprehensive nature, they did little to reduce the risk derived from increased instability of earnings resulting from changes in trade, or from mass unemployment caused by business cycle.

Over the years, however, a variety of other policies have complemented the specific measures noted above, which have sought to reinforce social protection for workers in these countries. For example, a variety of proactive policies such as health care, and public policies toward training and education have tended to reduce income insecurity by minimizing the risks of unemployment and earning incapacity. These policies and measures, which involved significant financial transfers from the government to the needy, currently amounting to about a quarter of the GDP, are believed to have contributed to a significant reduction in poverty in these countries during the last 50 years.³² Last but not the least, there is little doubt that favorable macro economic policy environment that is friendly to employment creation has also played a vital role in reducing the insecurity facing workers.

What is social protection ?

There seems to be a broad consensus now that the insecurity facing workers in both the developed and developing world is largely derived from income *inadequacy* and income *variability*, though they may manifest themselves in different forms. The goal of social protection has once again come to be regarded as one of *assuring minimum and stable income* to workers, without of course the *guarantee* by the state as in the earlier period. As a recent ILO report noted, the aim of social protection is not only *alleviating poverty*, but also *minimizing the risk* that, "through no fault of their own, individuals fall into poverty".³³ This is indeed a much broader goal, more ambitious than what was originally envisaged under social protection through

³² ILO (2000), p.2

³³ ILO (2000), p.2

labor standards, as it calls for action on a much wider front, well beyond the immediate working environment of workers; but it falls well short of providing a 'social safety net', with a minimum income defined in absolute or relative terms.

Broadening of the objective of social protection in recent years is in part explained, and perhaps justified, by the fact that a vast majority of workers in the developing countries - probably around 90 percent of the workforce - is in the informal economy that is outside the institutional framework, and consequently beyond the reach of conventional social protection measures, by definition. They have neither an 'employer' who can share the cost burden that these measures entail, nor can their enforcement be monitored by the government as these activities remain unrecorded and unregistered. But it is unclear who should take responsibility for minimizing the risks. Achieving the broader goals of social protection underscores not only the need to *prevent a fall in incomes* of workers, but also how to *improve* incomes. It also implies the need for *innovative* mechanisms of social protection that would *reduce the risks* contributing to income insecurity - innovative because these risks are different from those facing workers in the formal sector (see later discussion for more on this). They need to be innovative also because the burden of implementing the new protective measures has to be borne largely by the workers themselves, most of whom are known to have only a limited earnings. The challenge is therefore evident.

The ILO approach

Derived from the above considerations, and based on the 1952 Convention 102 - the Social Security (Minimum Standards) Convention - the ILO, which recently undertook a global review of issues pertaining to social protection, has defined *social security* "as the protection which society provides for its members through a series of public measures:

- to offset the absence or substantial reduction of income from work resulting from various contingencies (notably sickness, maternity, employment injury, unemployment, invalidity, old age and death of the breadwinner)
- to provide people with health care; and
- to provide benefits for families with children."³⁴

³⁴ ILO (2000), p.29

It is noteworthy that the definition does not mention explicitly the need to raise workers' incomes. Social protection is defined "to include not only public social security schemes but also private or non-statutory schemes³⁵ with a similar objective, such as mutual benefit societies and occupational pension schemes." The various social protection mechanisms for workers, identified and assessed by the ILO report, fall essentially into two categories: a) schemes that aimed at maintaining the earning capacity of the worker during the working career; and b) schemes that provided income security to the worker and his/her family after the end of the working career, and thereby minimizing the risk of falling below the poverty line. Schemes aimed at maintaining the earning capacity of workers broadly consist of:

- Health care - as access to it enables the worker to maintain health and hence the earning capacity. It may be provided by the government or through voluntary schemes including what are known as micro-insurance schemes for health care.
- Social protection during periods of incapacity - which enables workers to avoid a loss in income either due to sickness, or disability resulting from employment injury or other unforeseen events, both in the short and long term through income replacement benefits. It may be provided through a social security scheme, the cost of which is shared by both the employer and / or the government; or through occupational health services and rehabilitation systems. Clearly this also covers benefits to workers who retire prematurely owing to disability. Long-term disability benefits are typically provided by social insurance pension schemes.
- Maternity protection schemes for working women, a social security scheme whose cost is shared by both male and female workers as well as employers and the government.
- Unemployment insurance, provided by the state, mostly in developed countries, funded in part by employer contributions, whose benefits may however be only for a limited duration; and other *ad hoc* employment generating schemes such as public works mainly in poor countries.

Social protection schemes that aim at maintaining the living standards of workers and the survivors of his/her family beyond the working career include:

³⁵ Excludes schemes where contributions are wholly determined by market forces. (p.30)

- old-age and survivors' pension schemes - which includes government schemes that provide minimum income or pensions for the elderly;
- contributory social security schemes, widely known as social insurance;
- mandatory retirement savings schemes such as the provident funds;
- complementary voluntary retirement schemes; and
- social assistance schemes, tax financed benefits mainly for the poor who receive little or no benefits from other forms of social protection (or universal benefits).

A variety of other supportive measures such as child care services are also seen as contributing to income security, though indirectly, by helping women to participate in the market more effectively. Similarly, education and insurance schemes that minimize the risks to health of workers resulting from occupational accidents and exposure to hazardous substances also form part of the package.

Current approaches to extending social protection: A critique

Social protection schemes listed above vary not only in their *coverage*, funding and administration but also in terms of the *level* of protection. It is also obvious that these measures address only the risks faced by workers as individuals, and thus exclude *collective* (or covariate) risks such as natural disasters and unforeseen political events including wars. Many of the above schemes are not in general available to workers in the informal sector for reasons already cited viz., not having an employer, and not operating within the recognized institutional framework. Even in the developed countries many workers face the threat of losing access to the above measures because employers are increasingly resorting to informal forms of employment, avoiding compliance with labor regulations; high social security contributions or payroll taxes are often seen by them as a hurdle to extending social protection in the conventional sense of the term viz., formal schemes funded by the government and employers because they raise labor costs significantly.³⁶ This means the burden of social protection rests increasingly on the workers themselves. Given the limited financial capacity of workers who bear much of the cost burden, especially in the developing countries, these schemes necessarily tend to limit the package of benefits commensurate with lower contributions. Both the range and level

³⁶ In the industrialized countries non-wage labor costs as a share of total labor costs varied between 13 and 30 percent in 1995. Standing (1999), p.99

of protection tend to be limited.³⁷ Further it is not clear if they possess the tools necessary to manage the risks on their own.

The emerging response to the problem has been one of 'maximum benefits at minimum cost'. For example, increasing emphasis is being placed on organizations of workers (or small producers) in the informal economy in order to pool risks, and thereby lower the cost of insurance e.g., group insurance schemes; they have also led to cost reduction, especially administrative and managerial, through participatory management at the grassroot level. Such *informal* mechanisms are still in an experimental stage. Despite innovations and adaptations few schemes seem to reach workers in the informal sector as the discussion below shows.

A number of developing countries have designed schemes that provide access to health care for the general population; but very few social protection schemes in operation are either comprehensive, as suggested in the ILO approach, or focus exclusively or mainly on workers in the informal sector. In Africa, social health insurance schemes in at least 13 countries are believed to provide benefits to a substantial proportion of the population. Similarly several Asian and Latin American countries are believed to have social health insurance schemes.³⁸ In Bolivia, the Instituto Politecnico Tomas Katari (IPTK) has instituted a mutual health insurance scheme in 1996 which, among others, also serves the informal sector workers. A similar scheme is in its early stages of operation in West Africa.³⁹ Women have access to maternal and child health services but it has been found to be uneven, depending on the level of education and rural/urban status, according to the evidence from Bolivia, Egypt and Kenya in 1988.⁴⁰ Among the few countries that focus on the informal sector is Mexico where workers now have access to social health insurance protection in exchange for a nominal annual payment.⁴¹ But difficulties in "disseminating information about the scheme and bureaucratic obstacles" are believed to have limited the outreach, especially among the more vulnerable groups.

Likewise in Africa, Tanzania has recently started a scheme of micro insurance for health care - under the auspices of UMASIDA (an acronym for Mutual Society for Health

³⁷ ILO (2000), Chapter 10

³⁸ ILO (2000), p.85

³⁹ ILO/WIEGO (2000)

⁴⁰ ILO (2000), p.80

⁴¹ ILO (2000), p.80

Care in the Informal sector) - in Dar es Salaam since 1995 for workers in the informal sector.⁴² It is still too early to say the extent to which these schemes have been successful, taking into account their financial sustainability. A major hurdle to universal access to health care has been the income disparity among potential beneficiaries. Another example is the case of Self-employed Women's Association (SEWA) in India, which is currently implementing an Integrated Social Security Program covering some 32000 women workers in the informal sector in Ahmedabad city and elsewhere. "The scheme covers health insurance (including small maternity benefit component), life insurance (death and disability) and asset insurance (loss of or damage to housing or work equipment)."⁴³ Similar examples can be found in Bangladesh, the Philippines, Colombia and South Africa though in some cases the coverage goes beyond health care to include asset and life insurance, and pensions. These are frequently community-based mechanisms, though some are formal insurance schemes and transfers.⁴⁴ Micro-finance institutions have also contributed to increased social protection for informal sector workers mainly through the provision of loans though some have provided other services such as insurance. They seem to have yielded only modest results partly because the beneficiaries tend to divert loans intended for business to other purposes; in part it seems to be the result of these institutions pursuing multiple objectives including "mobilizing the poor, building on social capital, and empowering women".⁴⁵

In the case of sickness benefits, though there are social security and labor legislation that protect employees, mostly in developed countries, they tend to provide little coverage for the self-employed. Similarly social insurance pension schemes rarely provide long-term disability benefits to self-employed, even in the developed countries. There have been some isolated small scale experiments with regard to insurance against employment injury and occupation related diseases in the informal sector. Similarly with regard to old-age security and survivor benefits, "the governance of social security schemes in many developing countries has been so weak that satisfactory compliance rates have often not been achieved, even among the limited groups of

⁴² ILO (2000), p.89

⁴³ ILO (2000), Box 10.3, p.201

⁴⁴ These include: Grameen Kalyan in Bangladesh, CLIMBS and SHINE schemes in the Philippines, AMUANDES in Colombia, and the South African Old Age Pension Schemes in South Africa. See Lund and Srinivas (2000)

⁴⁵ Lund and Srinivas (2000), p.91

workers who should legally be covered by the scheme."⁴⁶ Consequently informal sector workers in developing countries can expect no more than small financial transfers from the government, under the social assistance schemes, based on a means-test. About ten countries in Latin America and the Caribbean have apparently legally established social assistance pensions for the poor but their effect seems to be negligible.⁴⁷ Finally, the only type of insurance against unemployment that informal sector workers in some countries can aspire for is employment through labor-intensive public works schemes e.g., the Maharashtra employment guarantee scheme in India.⁴⁸ The cost is shared equally between the beneficiaries, external donors and corporations (public and private insurance). These compromise solutions, as the ILO report warns, should not be seen as a way for the governments to escape from their responsibility in the field of social protection; instead, they should be considered as complementing the efforts by the government.⁴⁹

In sum, the "new" mechanisms, most of which are still in their early stage of operation, are fraught with a number of difficulties. Though some of them hold promise for the future, given the problems of 'scaling up' and the doubtful financial sustainability, quite apart from the problems of institutional capacity and governance, it seems fair to conclude that they still have a long way to go, and far from assuring a rapid and satisfactory resolution of the problem. Given the sheer magnitude of workers who need social protection, this means that it could indeed take a very long time before any visible impact. This gives added reason to look for alternative solutions. Before doing so it seems necessary to discuss the relevance and adequacy of the various schemes mentioned above for protecting the workers in the informal sector.

Income insecurity and vulnerability of workers in the informal sector

Social protection for workers in the informal sector in developing countries must address at least two types of risks: first, risks that are faced by any worker at the work place, or the immediate working environment, namely, a *potential* fall in income resulting from various contingencies stipulated in the ILO definition above; and second, risks that are unique to workers in this sector, derived from their status of informality - briefly discussed in the last

⁴⁶ ILO (2000), p.119

⁴⁷ ILO (2000), p.181

⁴⁸ ILO (2000), p.165

⁴⁹ ILO (2000), p.15

section, and elaborated below in greater detail. It must also address the needs of at least four distinct categories of workers, noted earlier:

- those who are self-employed, operating a business either on own account, with or without family labor, or as a micro enterprise, with few hired workers and apprentices
- homeworkers
- wage workers and apprentices in the micro enterprises
- independent service workers, who neither have a fixed business activity nor a fixed employer.

Unpaid family labor is not treated as a separate category since they essentially share the revenue as well as the risks with those who own and operate the activities in which they are engaged.⁵⁰ Following the ILO approach, the aim of social protection may be assumed to be the provision of income security; and the measures therefore consist of schemes that contribute to maintenance of current and future income of workers, as well as those that minimize the risks of insecurity. What are the factors that threaten the income security of workers in the informal sector? And to what extent do the various measures designed to provide income security to workers in the formal sector are also adequate for workers in this sector? These are discussed below, focusing first on individuals who operate their own business in the informal sector.

Protecting investment in human capital:

Considering the first category viz., individuals who own and operate their small business (either as own account workers or as heads of micro enterprises), it is clear that any *risk to their health* could threaten their income security, both in the short and the long term, as their ability to run business would be compromised. Measures such as those discussed earlier could therefore help, as they either prevent or minimize health related risks (including occupation related accidents and health hazards). To the extent they are comprehensive and complete, they help these individuals maintain the level of human capital investment, and thereby ensure flow of returns from such investment. And in the case of women, health care that includes maternity benefits can prevent a fall in income and thus provide some security. Maternity benefits are particularly important due to the disproportionate presence of women in the informal economy.

⁵⁰ Formal sector workers who are denied adequate protection through labor standards are not considered here as their insecurity is primarily derived from the weakness in the institutional capacity; elimination of ambiguities in the law and stricter enforcement of standards should take care of this problem.

These measures however assure income security only partially because they compensate for health related costs but not *the income loss* derived from sickness and disability; some insurance schemes no doubt cover, at least partially, the *loss* of income due to long term disability. *Such health insurance schemes thus provide only partial protection to these workers.* It is also evident that the workers have to bear part or all of the cost burden involved in such insurance schemes since these workers do not have access to the statutory schemes, and they have to rely mostly on social health insurance schemes funded partly by the state, or on micro-insurance schemes (such as those mentioned earlier) that are typically offered by micro-finance institutions but also by other community-based organizations. In fact most of these workers lack access even to such minimal protective schemes and are obliged to borrow or deplete their accumulated assets or savings to meet such contingencies. Thus micro credit often serves a protective role.

With regard to risks derived from occupational accidents and health hazards, isolated attempts have been made by donor funded projects to sensitize workers in specific activities in a few countries, which are thus preventive in character. Given the *risky environment* in which these workers operate, and their low capacity to pay, it is not surprising that the private sector has little interest in insuring such risks.⁵¹ How should these work-related risks be addressed? Because of the externalities involved, there is a strong case for state involvement in developing suitable schemes, but lack of legal status and organization among enterprises appear to be a major deterrent.

Protecting investment in physical capital:

These micro entrepreneurs are also frequently exposed to the threat of loss of income *due to damage to physical assets* utilized in their business. These risks are unique to the informal sector as part of the workers' income is derived from such assets - unlike in the formal sector. Such losses are in addition to the losses they may incur with regard to their non-business assets such as dwelling, which also contribute to income insecurity. Their assets are exposed not only to risks such as flood and other natural disasters, but also other man-made contingencies like civil disturbances and fire leading to destruction of property or theft viz., failure of the state

to protect property. Frequently such losses also result from law enforcement i.e., arbitrary action by the regulating authorities (e.g., police) leading to confiscation of assets, and eviction - a risk derived from the informal status of the activity. In many cities of the developing world it is not uncommon to find poor traders being not only chased away but also their merchandise and equipment like carts taken away; and many are also bulldozed on the ground of unauthorized construction. This risk can be attributed largely to the *failure of state to protect their property rights* because of their informality i.e., lack of legal recognition.⁵²

Clearly such risks are disproportionately large for those in the informal sector, partly because of their inaccess to infrastructure but also derived from institutional constraints i.e., *ambiguous* property rights. (See the discussion on access to land below). Though such risks are not addressed explicitly by the social protection measures mentioned earlier, they are in practice sometimes covered through a composite insurance mechanism such as those in operation under SEWA in India which includes a component for asset loss. Such schemes mostly cover losses due to theft, fire and other unforeseen risks but not those resulting from enforcement of regulations. Since the 'market' for such insurance services is mostly absent in the developing countries (presumably because the private sector does not find it attractive), these individuals have often no choice except to face the loss and eventually replace the asset through new loans, which of course is not easily accessible. Their incomes are consequently reduced. It is also clear such risks strike more severely those enterprises that do possess physical assets for business purposes, especially the ones with insecure premises or none at all. In other words, it may be a less important factor of income insecurity for the very small business such as petty trade and services who possess little inventory or equipment, who however are faced with a different set of risks (see below). Satisfactory management of these risks therefore seems to depend on a change in the institutional environment.

Assuring minimum income:

Unlike workers in the formal sector who are protected by legal minimum wage legislation, workers in the informal sector have no comparable protection. As noted earlier,

⁵¹ Employment injury is most frequent in informal construction work; tuberculosis, silicosis and other respiratory diseases affect weavers, beedi workers in India, quarry workers, etc.; exposure to lead poisoning, other toxic substances, hazardous chemicals, etc. are also frequent.

those who own and operate their own enterprise are more likely to earn above the legal minimum mainly because their income includes not only returns to labor but also own resources invested in the business as well as rewards to entrepreneurial tasks. Since a vast majority lacks such non-labor assets their earnings are below the *legal minimum income*, which means that measures to protect physical assets are of little help in reducing their income insecurity. In the absence of other measures they can realize higher income either by accumulating assets i.e., physical capital including land, and skills, or by finding wage employment in the formal sector. Social assistance measures in some countries perhaps assure some of these workers with a minimum subsistence allowance.

Preventing income fluctuations:

As in the case of formal sector workers, these micro entrepreneurs are also exposed to the *risk of unemployment*, and hence income insecurity. This can happen when the physical and human capital assets at their disposal, even if they are maintained, fail to generate income owing to market related risks and uncertainties i.e., either the assets remain under-utilized, or they are unable to realize optimal returns. As in the case of agriculture where farmers often suffer from income losses due to draught, the resources owned by an enterprise can remain under-utilized and fail to generate adequate returns for a variety of reasons: high transaction costs (poor institutions), price distortions (often policy induced), non-availability of complementary inputs (market imperfections). Demand fluctuations, either seasonal, or due to *unforeseen* events including natural disasters, political disturbances (civil unrest and crises), abrupt changes in the macro economic environment (e.g., structural adjustment programs), and business cycles also often precipitate a fall in revenue. Unlike wage workers in the formal sector whose employment and wages are largely protected by the employers and the state, these enterprises are often exposed to the threat of unemployment in an indirect manner via under-utilized capital. As these enterprises command few resources, they cannot, like their formal sector counterparts, overcome such risks through the use of 'political capital' (i.e., privileged access to decision makers in the government), output diversification, or other buffer mechanisms. What they can do, in the event of prolonged threat, is to deploy the resources they own into alternative

⁵² In South Africa, 55 percent of the street traders in Johannesburg were reportedly robbed, and 10 percent were assaulted. Lund et al. (2000), p.38

ventures. But this is not always easy owing to constraints on mobility (e.g., shifting the business location) and market access e.g., inability to acquire new skills, credit and know-how. Consequently, they *lack effective mechanisms to protect themselves against such contingencies*.

This is a risk that is endemic in most developing countries which can be overcome only in the long run with the development of institutions and improved economic management that reduces uncertainties. It should also be noted that these small producers face greater difficulties in adjusting to *change* partly because of their low level of education but also due to other constraints. Since these risks are quite serious, the most common response has been for these entrepreneurs to choose those activities that are least risky e.g., trade, especially in basic need items where they are assured of stable demand among others, even though returns are low; clearly these are also the activities where there is little scope for productivity increase. They prefer to engage in activities where there are less uncertainties and lower likelihood of unforeseen changes. This then seems to explain, partially, why many in the informal sector have inadequate incomes, not only present but also future. The various social protection measures listed earlier totally ignore these risks. These risks can only be addressed through institutional and policy reforms that reduce such uncertainties and hence transaction costs, making it worthwhile to undertake investment.

Old age security:

All categories of workers in this sector, it is obvious, are exposed to the risk of falling below the poverty line once their working career comes to an end as they do not have access to either statutory or non-statutory pension schemes, though in some countries they may have access to social assistance. In other words they have to develop their own mechanisms for protection, or assure old age security through private savings and insurance schemes such as those discussed earlier. Since these workers lose, when they cease to work, only the income derived from human capital investment, one may assume that the non-labor assets they own still remain intact and represents an important source of accumulated savings, which can provide a basis for designing a social security scheme. But in most cases this would be meager. With institutional reforms enabling these enterprises to accumulate capital, they could become an important source.

Income insecurity and informality

It was noted earlier (section II) that informality constraints prevent these enterprises from generating higher income, and thus contribute to income insecurity of workers. Lack of legal recognition, one of the two criteria of informality, implies access to non-labor resources, in particular land and formal credit is constrained, either due to government control or regulations. They are often unable to expand and reap gains through economies of scale, or diversify their output; neither can they compete effectively in the market, especially against comparable output from larger firms, or imports, that tend to enjoy 'protection' due to price distortions or other incentives. In fact these constraints are believed to have prevented many small and micro enterprises from entering into more lucrative activities because of entry barriers, which few are able to overcome. This is most evident, as noted earlier, in the concentration of petty trade and service activities within the informal sector. Productivity and income are not only low but also under constant threat owing to the absence of entry barriers, suggesting that much of the insecurity for workers in the informal sector is derived from institutional constraints. In sub-Saharan Africa, for example, these activities have grown at a phenomenal rate during the last two decades or more, with a corresponding fall in real incomes. It is this *involutionary* development that has been at the root of income insecurity and vulnerability for a majority of workers in Africa. It is in this context that *access to credit* assumes particular significance; easier access to credit can result in improved productive capacity and help these producers move into more productive lines, if accompanied by a change in the business environment that ensures adequate incentives.

Unfortunately, under conditions of informality, these workers have *few incentives to invest either in themselves or in physical assets or to improve technology* - quite apart from the question of access to resources. This means that there are few prospects for raising the level of human capital investment in the informal sector, which is already quite low. There is some evidence from Latin America which suggest that the returns to investment in education are lower for workers in the informal sector.⁵³ In Africa, though education and training increases incomes

⁵³ Expected return to schooling for self employed men was 13.8 percent compared to 14.7 percent for employees in Brazil; for men in informal sector, 9.2 percent compared to 10.1 percent for men in formal and informal sectors in Costa Rica; for men self employed, 8.8 percent compared to 12 percent for men in formal sector in Honduras; in Peru in contrast self employed men had a higher return, 9.4 percent compared to 9.1

of workers in the informal sector, the extent of the increase is limited owing to the non-availability of complementary capital inputs.⁵⁴ To the extent income insecurity is inversely related to the level of investment, the prospects of improving income security for these workers seem bleak, unless the environment for investment is made more attractive, and access to markets improved. Incidentally, improved access to credit, even in the absence of such institutional reforms, contributes to improved social protection for workers in the informal sector as it helps them to overcome the problems of uneven cash flows. This is evident from the experience of micro level credit schemes in several countries, which also show that the poor need banking facilities i.e., access to markets.⁵⁵

Not being able to access land in a *legal* manner, likewise, also contributes to increased insecurity, as many individuals are driven to violate the laws, especially those pertaining to land and property rights, which explains the wide spread "invasion" of land by the poor in many cities of the developing world. This has been made possible no doubt by the acquiescent law enforcement capacity in these countries. Ambiguities in the laws and regulations have also no doubt played a role. There is overwhelming evidence to suggest that a majority of informal activities lack premises with a proper legal title. This has increased the risk of losing their assets (already mentioned), besides loss of income in the form of penalties for violating the law. Another consequence of poor access to resources has been that these small producers have little choice but to remain invisible, cut off from direct links with the markets, by operating out of the residence, which however exposes them to different sort of risks (see discussion on homeworkers below). Finally, lack of access to non-labor resources also pushes these enterprises to use labor at their disposal more intensively, often resulting in self-exploitation. Not only those who own and operate the small scale activities but also the unpaid family labor are exposed to long hours of work under deplorable conditions for meager returns.

percent for men in wage and salary employment. No similar evidence is available for Asia and Africa. Sethuraman (1998), Table 4.3, p.109

⁵⁴ Birks et al., (1994) As mentioned earlier returns to human capital investment in manufacturing in selected African countries are indeed quite low owing to low level of physical capital at the enterprise level. See Bigsten et al. (2000)

⁵⁵ Many studies show that one of the reasons why the poor borrow is to smoothen the uneven cash flows; often they need to borrow in order to meet lumpsum expenditures for birth, wedding, funeral, etc.

Institutions have constrained *maximization of revenue* in these enterprises not only through restricted access to resources, but also through price distortions resulting from government interventions and poor functioning of markets i.e., segmentation and

fragmentation. and imperfect market structure. In fact many markets in developing countries are either absent, or characterized by monopolies; the state for example assumed the allocative function, often on a discretionary basis, giving room for discrimination based on legal status or other grounds. Imperfections in markets have been a source of insecurity to the extent they raise production costs above the potential minimum, and lower revenue in these enterprises. These imperfections reflect in part the governments' failure to organize markets and assure lower transaction costs through efficient functioning. Since the very existence of the informal sector is predicated on the existence of markets, where individuals interact directly with the markets in generating value added, the consequences of such imperfections is obvious. Besides land which is often under state control and heavily regulated, access to training and credit is restricted either because of regulations or due to the absence of private training systems and few commercial banks. In sub-Saharan Africa, for instance, virtually all non-labor inputs (including imported items such as spare parts and equipment) that the micro enterprises require, were either under state monopoly or control; and their availability subjected to uncertainty, raising the transaction costs. Frequently they were also under private monopolies. The informal sector is consequently obliged to turn to parallel or informal mechanisms, which however alleviate only some of the constraints. Small *scale* units also imply higher input prices due to reliance on intermediaries and retail buying. These inefficiencies are often compounded by discrimination in the markets based on gender or other individual characteristics such as age, education, caste, ethnicity and so on. This is most evident in accessing credit. Such discrimination have no doubt contributed to increased income insecurity among specific worker categories. In the case of women, informal constraints derived from social, cultural and religious considerations have also prevented them from improving their income security.

A variety of local government policies and regulations have also placed restrictions on vending activity in most cities of the developing world which, as one would expect, has increased the income insecurity and vulnerability, especially of women vendors. This has led women vendors to organize themselves in several countries. In part this has been inspired by the creation of International Alliance of Street Vendors, founded in Bellagio (Italy) in 1995, consisting of representatives from eleven countries, created in order to promote and protect the *rights* of street vendors. Since then it has evolved into what is known as 'street net' with more

countries joining the net; and is currently endeavoring to improve the policy and regulatory environment facing street vendors, and thereby reduce their vulnerability and income insecurity.⁵⁶ Similar restrictions (on routes, licensing and other regulations) on informal transport operators (mostly three wheeler *rickshaws*, motorized and non-motorized) in several Asian (e.g., Indonesia, Philippines, India, and Bangladesh) and African countries (e.g., Kenya, Senegal, Ivory Coast) have contributed to their vulnerability and income insecurity. Besides increasing the vulnerability, institutions in developing countries have also threatened the income security of workers because of the financial cost of non-compliance with regulations. A deeper analysis thus suggests that institutions have contributed to workers' income insecurity and vulnerability both *directly and indirectly*. Elimination of informality can therefore have a double impact on income security: not only can it reduce the risk of a fall in income, but also improve the chances of realizing higher incomes.

Homeworkers:

Turning to other worker categories, homeworkers, as noted earlier, are mostly women and employed on a sub-contracting basis, and hence differ from other enterprises in the informal sector in several respects. Problems relating to accessing inputs or disposal of output are virtually absent as they are generally taken care of by the contractors; but they risk receiving lower remuneration for the work they do, besides being exposed to contractual risks.⁵⁷ Though they have a choice of operating independently, assuming the attendant risks derived from markets (such as those described earlier), they seem to prefer working on a *sub-contracting* basis despite the lower income it entails, and the risk of being exploited by contractors through unfair terms and conditions. This is evident from the fact that several millions are actually operating as homeworkers. This choice is presumably explained by their risk minimizing strategies; the risks associated with contract work seem to be less, in their estimation, compared with those derived from direct exposure to markets, which in addition also requires management skills. Higher transaction costs also perhaps explain this preference as independent businesses have to

⁵⁶ This is one of the program elements of WIEGO. Research-cum-action is currently in progress in Kenya, and nearly completed in South Africa. Other countries are to follow.

⁵⁷ See ILO (1994) for a detailed discussion on the importance of homework and the problems facing homeworkers.

incur significant costs in terms of time and money e.g., searching for input supply sources, transport cost, and the need for working capital. Home-based workers, on the other hand, face the risk of lower income partly due to constraints in accessing resources discussed earlier, but more importantly due to their weak linkages with markets resulting from their *invisibility* i.e., lack of information and knowledge about the markets or their competitors. *Because these activities are small, scattered, and invisible they are highly vulnerable to exploitation; this vulnerability is also in part derived from market imperfections.* Often they have to rely on only a single or a handful of traders or intermediaries to dispose of their output, who naturally exercise their monopsony power.

The concentration of women in homebased work and homework is explained by several factors. The choice of operating from home is in part dictated by the informal constraints (Section II), especially access to land, credit and other resources, to which women are often subjected to. Such a choice also avoids potential conflicts between market participation and respecting socio-cultural norms that oblige women to remain invisible. For many it also represents a way of obtaining labor market flexibility i.e., combining gainful work with household and child care responsibilities.

Women homebased workers, in some instances, have been able to overcome the vulnerability noted above by organizing themselves (e.g., SEWA in India), leading to an improved bargaining strength, and hence better prices for their output. Homeworkers too appear to have used similar strategies to improve the terms and conditions of their contract. But the general absence of protective labor standards have deprived women of these gains. The ILO Convention on Homework (1996) cited earlier appears to have improved the prospects for their social protection. But much remains to be done as countries have yet to formulate legislation and implement them, which means they have to build the relevant institutional capacity. This also implies that these workers need to be identified and recognized. The need for protecting women is evident from the fact that they are frequently the sole earners or breadwinners in the family.

Wage workers:

Turning to wage workers in the informal sector, their number is relatively small as very few enterprises in this sector are big enough to have hired workers; and most of them are in manufacturing, transport and services according to the available evidence. Given the lack of legal

recognition of the enterprise, and the absence of formal wage contracts, their income is generally below the legal minimum wage. Workers are also exposed to unemployment risks, as there are no employment contracts. Like their employers, they have virtually no access to the different statutory or voluntary social protection schemes. Many however do enjoy a degree of security in the event of threat to their health, as their employers often provide at least partial financial assistance, depending on the number of years of service and other factors, which however can not be claimed as a matter of right. They are particularly vulnerable because of their exposure to risks derived from their work (occupational health hazards, exposure to hazardous materials, inadequate safety measures at work place, accidents, absence of emergency aid). To some extent their plight is also explained by discrimination in the labor market. Since they can not expect any significant improvement in their employment and working condition, most of them tend to leave and set up their own small scale activity once they have accumulated sufficient savings and gained access to the business and market network. Though they can improve their income security in this manner the process is no doubt hindered by the different constraints noted earlier.

Independent service workers:

Finally, with regard to independent service workers such as domestic servants, porters and the like, who are not attached to any single employer, the evidence shows that their income tends to be the lowest. Because these workers lack any specialized skills, and are mostly paid on a piece rate basis, they are constantly exposed to competition, driving down their wages. More importantly they are faced with discrimination in the labor market. Women in particular earn much lower wage than men; they are also more likely to be in dead-end jobs with few prospects of learning new skills. But there have been isolated cases where they have been able to organize themselves into unions, and impose self-discipline, which has brought them not only gains in income and greater job security, but also improvements in working conditions such as holidays, sick benefits and partial insurance against simple contingencies. A few seem to have successfully converted themselves into service companies. These cases are yet to be carefully documented and their experience analyzed, but they seem to hold promise for the future. But most governments seem to be either unaware of such experiences, or indifferent to the plight of

these workers. It seems fair to conclude that these workers would lack social protection as long as they remain unorganized.

Insecurity facing workers in this sector has often been overshadowed by the risks derived from poor macro economic environment prevailing in many countries, and there is very little recognition of this fact. Where the economic performance has been poor, workers are faced with greater insecurity it seems, because of the sharp conflicts of interests. In many sub-Saharan African countries, for instance, worker insecurity appears to have worsened over years significantly, judged by the phenomenal expansion of the informal sector and the rise in poverty, which is largely explained by the poor macro economic performance, exacerbated in part by the structural adjustment programs.

It is evident from the foregoing discussion that nothing short of a *comprehensive* set of measures, well beyond those under debate currently, aimed at eliminating informality, can improve social protection for workers in the informal sector on a sustainable basis. What are they ? The section below looks at these issues.

4. Social Protection at Crossroads ?

The risks facing workers in the informal sector in developing countries are indeed overwhelming; they contributed not only to income insecurity but also their vulnerability. These workers, it should be recalled, had little choice but to *assume greater risks* mainly because of their *exclusion* from formal labor markets. They appear to be far more serious compared with the situation facing workers in England in the 19th century because of the presence of informality in the developing world today. It also differed in another respect: transition toward a market economy in the earlier period, though it created new risks for workers, was also accompanied by a significant *rise* in both employment and wages due to a rapid expansion in world trade and improvements in technology. In contrast, workers in the informal sector today seem to have benefited little from globalization and technological change. In fact income insecurity may have worsened for many, because global competition has tended to lower labor costs. Relative abundance of labor in these countries, and *the presence of an informal economy* have also no doubt aggravated this trend. These risks are mostly derived from their *informal* status including their low initial endowments (reflected in low schooling and skills, as well as poverty), and not from the immediate working environment viz., the various work related contingencies. This

means that the threat to income security for these workers is far greater, compared with workers in the formal sector. The need for social protection to workers in the informal sector is therefore obvious. Can the current attempts to extend social protection to workers in the informal sector eliminate these risks ? This is discussed below.

It should be noted at the outset that the very existence of the informal economy in these countries can be interpreted *as a mechanism of protection* through which individuals attempt to overcome income insecurity on their own, notwithstanding the risks that such effort entails.⁵⁸ As already pointed out, this involves more intensive utilization of the resources at their disposal (including self-exploitation sometimes), accessing private or public property through illegal means (assuming the attendant risk), resorting to the use of common resources and recycled waste materials at little or no expense, and adapting technologies.⁵⁹ In the process, they have also assumed significant health related risks. Some of them have improved their income by gaining access to credit and other resources either by organizing themselves (e.g., ROSCA or mutual credit and savings societies) or by exploiting the various social networks successfully i.e., by building up 'social capital', which in turn has enabled them to realize higher returns to resources owned by them.

In recent years, they have even attempted to alter the environment in which they are obliged to function, an important source of insecurity. There is an increasing tendency among informal producers to *organize* themselves and create their own network, not only to improve their access to land and other resources, but also to obtain other concessions (e.g., fiscal), to reach wider markets, and even to exert pressure on the authorities to bring about a change in the regulatory environment, though not always successfully, all of which seem to have reduced the extent of their insecurity and vulnerability. This is evident from the various grassroot experiences such as StreetNet (network of vendors), HomeNet (network of homeworkers), and other informal sector organizations (artisan associations, transport operators' organizations, women's groups, etc.) cited earlier, though many more still remain undocumented. In other words they are attempting to overcome the constraints derived from informality. These efforts are more

⁵⁸ Some would like to interpret the emergence of the informal sector as a response to "the lack of protection.

⁵⁹ Maldonado and Sethuraman (1992)

successful in some countries than others, partly due to the differences in the macro economic policy environment i.e., the presence or absence of economic growth.

Notwithstanding these efforts, the risks, and hence the insecurity, remain. The *process* by which these individuals seek to improve their security thus appears to be *inefficient* in the sense that it has been slow to produce visible results measured in terms of income security. More importantly they have been able to overcome only some of the constraints because others require major reforms, which the state alone can initiate (discussed later). In the absence of such reforms they have essentially resorted to *coping* strategies. *In short, they still require an effective social protection mechanism.* Governments in developing countries, in contrast, have generally adopted an attitude of benign neglect, if not total indifference, to the phenomenon of informal economy. There is little awareness of the need, or concern, for social protection in the informal sector. How can they be motivated or persuaded to adopt a strategy of social protection? What should such a strategy consist of? Before answering these questions it seems necessary to examine the extent to which current approaches and measures for social protection respond to the needs of the informal sector.

Can Orthodox Social Protection Schemes Help?

The gap between those who have social protection and those who don't in the developing countries is indeed large, not only because of the vast number of workers in the informal sector but also due to the enormous differences in the quality of employment. Extending social protection to workers in the informal sector in the developing world poses formidable challenges not only because of the vast number of workers involved, but more importantly due to their *exclusion* from the recognized institutional framework, and hence the organized markets - unlike in England during the 19th century. Further, the number requiring protection has been *rising* because of demographic changes as well as the trends in globalization and technological change.

Capacity to pay: It was noted earlier that incomes of workers vary enormously, with a large majority earning below the equivalent of legal minimum wage because they have few non-labor assets. In several sub-Saharan countries for instance not only the level of income has been

low, but it is also believed to be falling.⁶⁰ As long as the workers are expected to participate in the cost of providing social protection, its level is determined *inter alia* by their income, within the framework of utility maximization. Clearly such a

⁶⁰ Employment in the “irregular and independent marginal workers” or the precarious category increased more rapidly than in the salaried workers category in Burkina Faso, Cameroon, Ivory Coast and Mali in recent years. See Sethuraman (2000), Chapter 1.

level may not be adequate to assure income insecurity. For the poorest, for example, there could be a conflict between satisfying current consumption needs versus buying security for the future. The poor for instance may choose not to participate in a scheme if it improves their income security only marginally. If this is true these protection measures will not make any *real* difference to their income security. In fact this low capacity of beneficiaries to pay for the cost seems to explain why social protection schemes have failed to develop in the private sector even though there is a considerable *need*. In other words, income constraint, besides making social protection inaccessible to many, is also likely to limit the scope and level of protection.

Government subsidy: There is some confusion in the literature between 'need' and 'demand' for social protection. Social protection is generally considered as a need, implying that the society (or the state) has an *obligation* to provide it. Given the considerable number of poor workers in the informal sector, the cost burden on the state is evident. The state is therefore likely to provide a *minimum* level of social protection, irrespective of the ability of the worker to pay, implying subsidies for the poor. These subsidies can be justified, quite apart from other considerations like equity, on the ground that *social benefits* will exceed social costs owing to the presence of positive externalities such as higher productivity in the economy and investment in health. Frequently they are justified on the ground that such measures provide 'social insurance' i.e., benefits to all members of the society. Even though one can justify state involvement, to what extent is it realistic to expect governments in the developing countries to devote resources for social protection for the informal sector, especially when they have adopted an attitude of 'benign neglect' if not indifference toward these activities?

Can the schemes reach the informal sector?: There is little doubt that even a *minimum* level of social protection, designed "to offset the absence or substantial reduction of income from work resulting from various contingencies", as suggested by the ILO, could bring considerable relief to these workers by protecting them from *some* if not all of the contingencies noted earlier (assuming that the shortcomings noted below can be removed). The key issue is however whether these schemes can *reach* workers in the informal sector as long as it remains *invisible*, outside the institutional framework - except indirectly through general schemes that aim at covering the poor or low income population as a whole. In fact many of the current schemes address the poor or low income population in general, and *not*

specifically the workers in the informal sector. The limited evidence from India regarding social assistance to the elderly - ‘means’ tested old-age pensions - which has been in operation in several states and financed by the government, suggests that less than a fifth of the old people under the poverty line benefited from it because of lack of information on the part of eligible beneficiaries and restrictive qualifying conditions, along with corruption and procedural delays limiting the effective access.⁶¹

Shortcomings in the schemes: Among the many schemes envisaged, health care and micro savings and insurance schemes are perhaps the only ones that respond to the security needs of these workers to some extent. Currently, life insurance schemes for the poor are more often oriented to protecting credit institutions from potential financial losses rather than persons, though they could be linked to savings. Schemes to protect assets, for example, may not necessarily reduce income insecurity because the *returns* from them are still open to fluctuations and not protected, and could cause a fall in income. Further, asset insurance in many current schemes is believed to cover only the loss of assets *financed by credit*, and that too for the outstanding loan amount only. In other words the insecurity will remain unless social protection measures also include appropriate initiatives that would *guarantee adequate returns to investment* in these small scale activities. For this to happen, clearly the institutional and policy environment in which these informal activities are carried out need to be improved.

Supply mechanisms: Though the schemes currently being experimented have sought to lower the cost through risk pooling and sharing of management and administrative costs to improve the outreach, the problem of ‘scaling up’ micro level initiatives remain. Some of these issues are beginning to be addressed.⁶² What about private sector involvement? Private health insurance is not considered as a valid option for full population coverage by some, because of high transaction costs, derived from the need to undertake risk-rating, which requires detailed information and analysis. But some private insurance schemes seem to hold promise. In other words, it is still unclear if these schemes can be effectively managed to reach all potential beneficiaries in the informal sector, and to assure delivery without cumbersome procedures.

⁶¹ Guhan (1992), pp.287-289; See also van Ginneken (1998)

⁶² Brown and Churchill (2000)

It would thus seem that the various innovative approaches to extend social protection viz., '*protective security*' to the informal sector, which have been identified in recent years, either fail to respond adequately to the security needs of workers, or are beyond their reach. Perhaps the most important drawback of the orthodox schemes is that they fail to address the fundamental causes of income insecurity and vulnerability facing workers in the informal sector because they were not so designed. These schemes are but an "extension" of the measures designed to protect workers in the formal sector, more specifically in the industrialized countries context. As Guhan puts it, "In the developed countries, the origins of modern social security were based on an empirical diagnosis of want, which postulated that much of poverty in these countries could be related to the interruption, reduction, or loss of earnings [of workers] from contingencies such as temporary unemployment, sickness, disability, old age, death of main earners in the family, and large household sizes."⁶³ While such contingencies, and the insecurity derived there from, apply to workers in the informal sector too, they are relatively a less important source, compared with the insecurity derived from *structural* factors such as those discussed in this paper. Risks to income security for workers in the informal sector in developing countries are more often derived from the *conditions governing their employment and income generation* viz., *informality*. Orthodox measures to social protection thus imply a 'Band-Aid approach' to the problem because they respond only to the symptoms rather than the disease; they are more in the nature of *coping* with risks from various contingencies through remedial measures, and fail to address the fundamental causes of insecurity and vulnerability.

How does one then explain the current emphasis on protective security based on orthodox measures? It may reflect the existence of a 'professional' bias, which takes a narrow view of social protection, based on historical experience. Alternatively, since the removal of fundamental causes of insecurity and vulnerability among workers in the informal sector hinges on economy-wide reforms, many probably consider them as extraneous to conventional social protection instruments. Or perhaps they take a pessimistic view of reforms because of the difficulties in implementing them, which by definition is a long-term political undertaking. Perhaps a simpler explanation is that current attempts to social protection have simply overlooked the structural causes of income insecurity in the informal sector. Practical considerations such as

⁶³ Guhan (1992), p. 291

limited resources and implementability of well-defined and time-bound schemes may have also influenced this choice.

An Alternative Approach

Do the arguments above then imply that the emphasis should be exclusively on ‘preventive’ and ‘promotional’ aspect of social protection i.e., addressing the *structural* causes underlying insecurity?⁶⁴ Or should it also include ‘protective’ security? Should social protection also include elimination of *vulnerability* of workers in this sector besides improving income security? There are several reasons why the approach toward social protection, as far as the informal sector is concerned, should be *comprehensive*, aimed at not only protecting against various contingencies implied in the orthodox approach, but also promoting income security through the *elimination* of risks. Even if the emphasis is placed on the promotional aspect the need for protective security will continue to exist because a certain proportion of these workers or their families will always experience income shortfalls, as the experience of industrialized countries show.

Broadening the goal of social protection - from risk ‘minimization’ or ‘alleviation’ to risk ‘elimination’ - would however imply a *shift* in the strategy - from *preventing* a fall in income or *minimizing* its fluctuation, to *raising* the level of income.⁶⁵ Instead of designing schemes to cope with, or mitigate the consequences of risks, the focus will shift to more fundamental *reforms* that attempt to modify the institutional environment in which the informal sector functions. This is inevitable as much of the risks facing these workers is derived from their ‘informality’, and hence rooted in the institutions. Instruments of social protection, it is also evident, would then become indistinguishable from those aimed at poverty reduction.

What are these reforms? Since income insecurity and vulnerability of workers in the informal sector are largely derived from their informality viz., lack of legal recognition, reforms aimed at eliminating such discrimination seem essential. In many sub-Saharan African countries, for example, vulnerability of informal workers is mainly derived from the refusal of local authorities to provide legal recognition as many of them were considered ‘vagabonds’, depriving them access to resources and opportunities. Apart from discrimination based on legal status,

⁶⁴ Following Marty Chen’s suggestion, promotional measures may be defined to include also preventive measures.

high transaction costs derived from poor institutions including market deficiencies also explain their exclusion from organised markets. They could include not only regulatory reforms pertaining to business registration and licensing, labor, fiscal and other administrative requirements, but also land related regulations as they render many informal producers ineligible to legal status. Ambiguities both in the regulations and in their enforcement need to be eliminated as well, since they contribute to informality. Informal constraints derived from social and cultural practices would also need to be reviewed.

Similarly, reforms aimed at improved functioning of markets and improved access to them by those in the informal sector could help not only in raising the income of workers but also in reducing their vulnerability and improving equity. These market related reforms are important because the essential characteristic of informal sector is that individual producers attempt to gain income by interacting with various markets directly; outcomes in terms of employment and income critically depend on how well they function. They would also enable them to enhance their capabilities in the long run, resulting in productivity improvements. These reforms could include measures that not only eliminate market fragmentation and discrimination but also reduce the risks and uncertainties leading to lower transactions costs and higher returns to investment. One of the reasons why developing country governments have failed to place adequate emphasis on this aspect in the past has been the strong presence of the public sector in the provision of resources or their allocation.

In addition to the above, other reforms that protect property rights of the poor (especially women) and improved access to law and justice would also seem necessary to ensure social protection. These need to be complemented by policy reforms as they also seem to matter, to the extent inappropriate policy environment including negative policy bias and distortions discriminate against the informal sector and exacerbate the risks. This is most evident in sub-Saharan Africa where structural adjustment programs seem to have increased the income insecurity facing workers, especially in petty trading and services, as noted in the last section.

These reforms, it is clear, address various kinds of deprivations confronting the workers in the informal sector and thus emphasize the link between social protection and the *rights* of

⁶⁵ This is mentioned in Lund and Srinivas (2000), p.43 but not pursued through.

individuals as argued by Sen.⁶⁶ They underscore the importance of right to access organized markets and resources, to access land with a proper legal title, legal recognition as well as right to access various public social protection measures including labor standards. They also raise questions about street vendors' right to access space, and trade in public places, and protection from harassment by the regulating authorities.

Social protection based on such a broad strategy would no doubt have far reaching implications; and they also pose a number of formidable challenges. But it also offers a number of advantages. Institutional reforms could have a positive effect on the economy as a whole and thus improve employment prospects in the formal sector, leading to a *reduction in the size of the informal sector*. With increased incomes, workers in the informal sector could afford a *higher level of social protection* offered by various schemes, reducing the need for state subsidy. This is important since several micro level health insurance schemes in operation are believed to be financially unsustainable, though some recent examples show promise. Such a strategy would also open the prospects for greater government involvement in the provision of social protection as it would allay their fears on resource commitment. It should be recalled that many governments are reluctant to commit themselves to extending social protection to the informal sector because its size has been expanding inexorably. It would also encourage private sector involvement. Risks facing workers in the informal sector would become more *manageable*. In fact many of the risks facing workers in this sector, especially those derived from the market, are not susceptible to management by individuals through conventional tools, making it necessary to place emphasis on promotional aspect of security. In other words it is likely to ensure sustainability, as it reduces the dependence on external financial support.

Perhaps the most important argument why social protection for the informal sector should place emphasis on such reforms is that it would bring the informal activities *within the institutional fold*, making it possible for the government to extend existing schemes. *As long as they remain outside the institutional framework, invisible, the workers' chances of accessing social protection schemes will remain bleak*. Legislation incorporating new labor standards intended to protect workers in the informal sector (e.g., ILO Convention on Homeworkers), for example, can contribute to social protection but only if these small scale

⁶⁶ Sen (1999)

activities are brought within the institutional fold so that they can be effectively enforced and monitored. *It is therefore an illusion to think that there is a choice between protective and promotional security.* Successful implementation of the former critically depends on reforms that eliminate informality. Thus a comprehensive approach to social protection seems inevitable if it is intended to provide income security and eliminate vulnerability of workers in the informal sector in developing countries on a *sustainable* basis.

It should be noted that the above reforms may not be as radical or far-fetched as they may sound because a careful analysis of the recent experience in these countries suggests that informal producers are already attempting to improve the institutional environment in which they function, and gain access to various rights. This is evident in the existence of StreetNet, HomeNet and other self-help organizations which are manifestations of increased *empowerment* of workers. What they could not achieve individually, they are able to achieve collectively, though only a few governments are yielding to such pressures grudgingly, in part due to its political implications.

Turning to the issue of implementation, it is evident that the prospects for reforms, and their success vary between countries because of the challenges they pose. Though certain bureaucratic reforms may be easier to implement, this may not be the case with others. Some reforms are likely to involve trade-offs between equity and efficiency which may not be easy to resolve; with appropriate analysis and research, it may be possible to minimize such conflicts. Measures to compensate any financial loss in the short term, for instance, could pave the way for certain reforms where loss of government revenue is the sticking point. Regulations governing business for instance have generally been used in these countries to raise local government revenue (and encourage rent seeking) rather than lower the transaction costs, and consequently their reform could meet with some resistance. Similarly, in the Latin American context, labor regulations have played a more important role in separating informal from formal enterprises. Reforms in this area are no doubt fraught with difficulties because of the well entrenched trade union interest. Once the authorities are convinced of the benefits, and a popular support can be developed, they are however more likely to support them.

Certain reforms, such as those aimed at strengthening the markets and making access to them more equitable (i.e., eliminating discrimination) may not meet with much resistance though they will face hurdles in terms of institutional capacity. But reforms such as those related to law and justice, or to land regulations, may however prove to be difficult because of political obstacles, and partly due to the need for extensive consultation and legislation. In many African countries, for example, the land market is often absent, making reforms in this area more complex and difficult. It may be possible to overcome opposition to reforms through education aimed at creating awareness of the potential benefits. But these difficulties should not be underestimated.

It is precisely for this reason that a strategy for social protection should place emphasis on *empowerment* and *participation* of those in the informal sector. Given the 'benign neglect' attitude toward the informal sector in most countries, it would be unrealistic to expect governments to take the necessary initiatives in the direction of reforms unless there is pressure from the grassroot organizations. It is in this context that the emerging experience of informal organizations assumes particular significance. These organizations are not just helping their members to overcome various scale - related disadvantages (lower input prices through bulk-buying, better output prices through collective bargaining) and market imperfections (improved access to credit and other resources); they have also been instrumental in obtaining legal recognition, and in creating indigenous or informal social protection mechanisms. They remain the potential, and perhaps the most important, watch-dog that can make the governments accountable, and ensure the effective delivery of social protection

5. Conclusions

Informal sector in the developing countries is essentially a *manifestation* of the protection mechanism by which workers have sought to gain access to income, and hence security, by integrating themselves with the mainstream economy through whatever means. It is also in part a reflection of the failure of governments to assure formal employment i.e., jobs with adequate wage and social protection. By failing to adapt institutions they also seem to have caused the expansion of the informal economy. In other words the number of individuals requiring 'social protection' would have been considerably smaller if appropriate institutions including well functioning markets had

been put in place. What is surprising is that they have shown little concern for the income security of workers in the informal economy. They have generally assumed that these workers would *somehow* assure their security needs on their own. Few governments seem to be aware of either the extent of income insecurity facing these workers, or the fact that their own action (or inaction) is the principal cause of such insecurity.

Without access to organized markets, basic infrastructure and legal recognition, it is not surprising that workers in this sector, despite their best efforts, have been able to improve their income security only *partially*. In fact a vast majority of them is exposed to considerable insecurity and vulnerability, though the extent varies between countries. Besides low initial endowments of these individuals in terms of schooling, skills and physical capital, institutional constraints and poor macro economic environment also seem to explain why they have been unable to overcome income insecurity and vulnerability on their own. These distinguishing features explain why workers in the informal sector are faced with greater need for social protection, compared with those in the formal sector. What has perhaps aggravated the concern for social protection in the informal sector in developing countries in recent years is the rate of its expansion. The need to protect workers in the informal sector is therefore not in doubt.

Evidence emerging from countries suggest that *as long as they are subjected to informality constraints, few can either overcome income insecurity or vulnerability*. In other words provision of social protection to these workers hinges critically on the elimination of such constraints, and making the sector more “visible”. They seem to be a far more serious source of threat than the risks derived from various work related contingencies, which many orthodox social protection schemes have attempted to address. What is needed is a more *comprehensive* approach toward social protection than has been attempted hitherto, that includes not only short-term measures to cope with risks i.e., ‘protective security’, but also a long-term strategy to *eliminate* them, especially those derived from institutional constraints i.e., measures to promote security. Since macro economic policy environment has also been an important source of insecurity for these workers, both institutional and policy reforms should form an integral part of such a strategy.

Such reforms would help informal producers in these countries in many ways. Improved access to resources partly through lower transaction costs would provide incentives for

investment and productivity improvement, as well as encourage them to engage in more lucrative activities through greater mobility. Since failure to protect the rights of these individuals has often been an important source of insecurity and vulnerability, these reforms, by assuring them their *rights*, could contribute to their social protection. In short a comprehensive approach is likely to not only diminish the need for social protection through risk and cost reduction, but also enhance their capacity to pay for a higher level of protection owing to its positive effect on workers incomes. It is not only desirable but also seems necessary to assure *effective* protection and its *sustainability*; unless these activities are brought within the institutional fold, workers in them have little chance of gaining access to social protection of any kind. Such a strategy is also likely to encourage state involvement in the provision of social protection because it implies smaller public outlays. Needless to add these reforms, because they lower transaction costs, will also have a salutary effect on economic growth; in fact they are likely to help the growth of employment in the formal sector, and thereby reduce the size of informal economy in these countries. These reforms, by removing the veil of informality, hold the promise of contributing significantly to social protection in the informal sector. Evidence from countries suggest that it is easier to implement such reforms in a growth context as it minimizes potential conflicts and trade-offs, and eases the tension.

It should be recalled that workers in this sector are already attempting to overcome various constraints along the directions mentioned above. They have attempted to modify the institutional environment through collective effort, mostly by organizing themselves into a visible force, with or without the help of other non-governmental organizations committed to their advancement. But such attempts are still few and in the early stages, and the extent of their success is limited. Notwithstanding this, these initiatives have demonstrated the potential for bringing about a positive change in the environment through *empowerment* and *participation* of those in the informal sector. The proposed reforms could build on this experience. By encouraging such grassroot organizations, and hence people's participation, it would seem possible to bring the issue of institutional reforms into the development agenda.

Besides reforms, there may also be scope for improving conventional social protection measures to make them more efficient and accessible. Some attempts are already being made in this direction. For instance, innovative measures to cover the risk could help micro finance

institutions extend their services. By linking insurance premium to savings (such as those being implemented by SEWA in India) these schemes could provide incentives for workers to join. Where micro health insurance schemes are not possible owing to the absence of grassroots organizations, it may be worth considering the franchising approach, whereby a network of small scale private initiatives could be encouraged and supported to develop a supply mechanism. Such an approach holds the promise for 'scaling up' the supply of health services, besides the prospects of lowering the cost. Such innovative measures remain to be discovered and documented based on actual experiences on the ground. In certain cases it may be possible to improve social protection of particular groups of workers through new initiatives. For example, in India, it has been proposed that by levying premia on contractors, the construction workers engaged by them can gain access to injury, disability and death benefits; by collecting premia through taxes on the final output, social protection schemes can be designed to reach specific occupational groups in the informal sector (e.g., weavers, *beedi* workers, quarry workers, etc.).⁶⁷ Similarly, in the context of globalization, governments in developing countries could consider constituting a 'social security fund' designed to benefit homeworkers engaged on a subcontracting basis, especially in manufactured exports, financed out of the gains from trade. These illustrations can be multiplied through a careful analysis; but obviously they need to be experimented on a pilot scale before wider application. Finally, other promotional measures such as improved access to schooling and skills could also complement the above in order to build 'capabilities', especially among the poorest.

Since the conclusions presented above are generic in nature, they need to be adapted to the specific country context, especially because of the variations in the size and structure of the informal sector. The scope for, and the nature of, action will no doubt depend on the realities on the ground. Thus the agenda for action will consist of further research to verify the underlying assumptions. The main thrust of the arguments developed in this paper viz., the need for a more comprehensive framework toward social protection including institutional and policy reforms, underscores the importance of institutions in economic growth. The earlier efforts during the 1970s to promote "growth with redistribution", it would seem in retrospect, failed to yield the expected results partly because they ignored the role of institutions. The time is perhaps ripe to

⁶⁷ Guhan (1992), p. 295

consider promoting “growth with social protection”, with particular emphasis on empowerment and participation.

Part II

Social Protection for the Informal Sector: Towards a Comprehensive Framework

1. Background

It is clear from the discussions in Part I that approaches to social protection (SP) for the informal sector are currently inadequate to address the complex risks and uncertainties that affect this sector. The existing approaches to social protection have been very narrow and selective and have treated the informal sector as a “target group”, without acknowledging its inherent heterogeneity.⁶⁸ Indeed, rather than talking about the informal sector, one may rightly talk about several informal sectors or, even better, the informal economy.⁶⁹ Most of the social protection programs to date have been mainly concerned with developing coping strategies for risks as they appear on the scene. Naturally, this approach is very limited and in the long term unsustainable, because it is better to address risks at their source rather than develop coping strategies to deal with the myriad of consequences of each risk. Some of the early approaches of informal sector were naturally based on a narrow view of the informal sector: early development economic theories expected that with sustained economic growth the informal sector would shrink and ultimately disappear (i.e., become formalized). Evidence over time has proved this is not true and very unlikely to be even anywhere near the reality⁷⁰. Thus, the approaches to social protection also need to move away from the traditional narrow view of the informal sector to a more inclusive and comprehensive one where informal sector workers and their households are active partakers in the growth process. This part of the paper tries to precisely do this, with the help of some recent development frameworks which have been proposed to assist practitioners move away from the narrow constructs of traditional economic theories to a more inclusive and comprehensive socio-economic framework as we address the

⁶⁸ Sethuraman (1998) discusses this point to show how historically the international donor community adapted the “target group” approach to the informal sector as economic policy reforms and “trickle down” approach failed to benefit the informal sector and the poor.

⁶⁹ ILO Director-General Juan Somavia (ILO, 1999) first used the phrase “informal economy” to refer to the informal sector in his paper “Decent Work for All” in his address to the 87th session of International Labor Session.

⁷⁰ Castells and Portes (1989) give quite a few examples of the way in which informal sector has grown over the years in many countries including United States. Tokman (1989) also shows figures for Latin America. Charms (1998) Table 1 shows figures for Sub Saharan Africa, North Africa, Latin America and Asia to

future welfare of those in the informal sector. In addition, recent risk management approaches enable us to develop a framework within which risks and *ex ante* and *ex post* risk management approaches can be discussed as they relate to the informal sector.

The next section discusses the traditional approach to social protection of the informal sector and the need to broaden that approach not least to account for the inherent dynamism in the productive informal sector. The section that follows briefly describes the three frameworks which have appeared recently and are relevant for broadening the social protection approach to the informal sector. Section 4 discusses the World Development Report (WDR) 2000/1 by the World Bank as a basis for expanding the framework for social protection, while section 5 supplements this same theme with the Social Risk Management (SRM) framework developed by the Social Protection Unit of the Bank, both of which complement each other as a development paradigm. The subsequent section argues how this broader approach is consistent and congruent with the objectives of international donor community and especially the World Bank and sketches some options towards addressing informal sector needs through its policy and lending activities. The final section concludes with a summary and agenda for further research.

2. Moving Towards a Comprehensive Approach to Social Protection

The traditional approach to social protection is quite narrow. It consists of targeted programs which primarily address risks “*ex post*”. Thus, many of the social protection programs are risk coping in nature, although some tend to also steer towards risk mitigation. Because many social protection programs pursue the “*ex post*” approach they could not deal with risk prevention. Risk prevention or an *ex ante* approach is a cost effective way of addressing the consequences of risk at its source. *Ex ante* approaches will reduce the need for plethora of *ex post* programs which can be extremely expensive. Hence a broader approach for SP requires that risk management interventions be also “*ex ante*”. For example, economic and other government policy reforms which could be aimed at reducing vulnerability and income variability of the informal sector has not been considered part of a social protection strategy for the informal sector. Thus, the informal sector in the past was viewed as a residual sector which

highlight the point that independent of level of growth the share of employment in the informal sector has increased.

benefited more by chance than by design from broad macro policy reforms.⁷¹ However, it is clear from part I of this paper that the varied and complex set of risks that the informal sector faces require a broader approach which includes policy reforms and program interventions.⁷² This will ensure that social protection is not just risk coping but also includes risk reduction and mitigation under a comprehensive risk management framework. This means that social protection is not a short term or interim strategy to assist the informal sector but a long term strategy for eliciting efficiency gains central to economic development. Therefore, social protection needs to adopt a more coherent approach than the few ad hoc measures which fill the space of social protection schemes currently in many countries. SP needs to be seen as a central element of any national government policy and should underline all government policies and programs – whether they be economic or social or political for that matter.

In addition, social protection needs to move away from top down approaches by the state to a more inclusive and bottom up approach, especially in terms of design and implementation of social protection programs. Most commonly, the lack of understanding of risks has resulted in public or state-run social protection programs being ineffective in assisting the informal sector risks. Literature also discusses how various programs and policies of the government are in conflict with each other. To avoid this, the informal sector should be a central stakeholder in the design of social protection measures such that social protection policies and programs are equitable, accountable, transparent and cognizant of institutional capacity issues. Apart from ensuring that social protection is more comprehensive such an approach will also ensure that the informal sector constituency is an equal partner in implementing social protection measures together with the state. Definitely, this will increase the efficiency and effectiveness of social protection programs.

⁷¹ To our knowledge there is not much evidence of economic policies being treated as part of a comprehensive SP strategy. This is because, we believe, that economic policies have not been seen as measures which include social protection among other things as important in their objective function. We believe this is wrong for two reasons. One it perpetuates a wrong view as economic policy by definition is meant to address overall welfare – including economic and social. Second it encourages economic policy not to be concerned with social protection and social welfare despite absorbing large amount of financial and institutional resources. Unless this trend is reversed, most government programs will not be accountable to most welfare needs of the population and we will need a plethora of special programs, which unfortunately is the reality in many developing countries.

Redefining Social Protection - Narrow versus Broad Approach

Broad SP leads to a comprehensive risk management framework which includes risk prevention and risk mitigation while narrow or targeted SP mainly leads to risk coping. Broad SP leads to new opportunities and through that leads to empowerment and enhanced security, while narrow SP mainly strives for greater security and lowering exposure to vulnerability, although in a few cases can also deal with facilitating empowerment and promoting opportunity.

Broad SP includes macro economic policy reform, regulatory and legal reform, social sector reform and a myriad of special programs targeted at the vulnerable and excluded.

Macro Policy reform includes trade reform, price reform, exchange rate reform, pension and social security reform which directly and indirectly will influence the opportunity set of the informal economy. Different policies may derive different levels of weight in the way they relate to the informal sector. It can also include reforms related to expanding market opportunities for informal sector.

Regulatory reform here means laws and regulations which apply to the legal status and registration of informal sector activities and workers. These measures will seek to define the rights and responsibilities of informal sector clearly. Some of the measures can be self enforcing or can be left to the respective occupation group or trade association relieving local government officials of the responsibility of regulating this sector. Legal reform will ensure that informal sector has clear litigation process and build their confidence in the judicial system of the country as it relates to them.

Social sector reform deals with measures the government adopts to increase access and improve quality of health, education and social welfare services. This can also include broader public service provision issues which deal with infrastructure – namely roads, water supply, sanitation, etc. – which has an important bearing on the activities of the poor in general and the informal sector activities in particular.

Pension and Social Security reforms are becoming important aspects in addressing worker welfare and old age issues. Although these reforms have been concerned mainly with efficient management of existing programs for those currently covered; in some cases, coverage for those in the informal sector who are currently not covered by these programs are also being addressed.

Narrow SP includes targeted programs – training, safety nets, social assistance, unemployment assistance, social security, micro credit, and micro insurance schemes. Descriptions of some of the narrow approaches to SP can be found in Holzmann and Jorgensen (1999), Lund and Srinivas (2000). Many other World Bank, ILO, WIEGO publications on the informal sector have details of the narrow SP approaches and hence they are not expounded here.

⁷² Lund and Srinivas (2000) in Table 4.2 provide a list of risks that the informal sector faces which are different in character and intensity from those of the formal sector.

The fiscal outlay of social protection programs can be substantial and one needs to ensure the sustainability and long term benefits of programs implemented. Hence one needs to move away from just consumption smoothing approaches to social protection (although they are important in many cases) to an investment approach which seeks to address risk at its source. This will ensure programs are not “band aid” solutions as they currently tend to be, but are complete cures to the root sources of risks and uncertainty that the informal sector faces. This would also mean a move away from risk coping strategies to ensuring risks are prevented or their harmful effects reduced when they are non-preventable. Such a broad approach would ensure that the informal sector is empowered and strengthened such that it has at its disposal effective means of managing risks common to the sector. In the absence of a comprehensive and broad approach to social protection we will have a multitude of ad hoc measures.

3. Frameworks for a Broader SP Strategy for the Informal Sector

Given the limitations in the existing (narrow) approaches to social protection, especially to the informal sector, we want to highlight here the frameworks that could be useful in broadening our view of SP and ensuring the proposed strategy is comprehensive enough to deal with the limitations of past approaches.

In the recent past, three frameworks have emerged which have been useful in highlighting the limitations of current approaches to development broadly and social protection in particular. The first of these is the ILO Director General’s “Decent Work Agenda.”⁷³ This perspective having revolutionized previous narrow views of providing assistance to workers has implied substantive revisions of the objectives and scope of activities in SP. This has also naturally started to change the ILO’s approach to worker welfare and broadened the scope of social protection for workers. However, this paper will not deal with the implications of this framework extensively, although many issues we address in relation to the other frameworks will be relevant. The second and third frameworks that we want to discuss here are recent additions from the World Bank – namely World Development Report (WDR) 2000/1 and Social Risk Management (SRM) framework. They complement each other in the way they relate to SP. The WDR 2000/1 on “Attacking Poverty” provides a very broad view of development that has not

⁷³ This was presented by ILO Director General Juan Somavia as his address in the 87th session of the International Labor Conference in 1999.

hitherto been emphasized in a coherent framework. The three pillars presented – promoting opportunity, facilitating empowerment and enhancing security – thought not mutually exclusive, are very timely and relevant concepts not only for understanding how to eliminate poverty but also how to bring out the full potential of the informal sector. The SRM framework also has three elements for managing risks individuals and households face – namely risk prevention, risk mitigation and risk coping. The SRM approach neatly complements the WDR and ILO approaches in critically evaluating current approaches to social protection and ensuring that new comprehensive approaches are developed to address all three aspects of risk management. The next two sections that follow will discuss how the WDR and SRM approaches, respectively, enable us to develop the broad and comprehensive approach to social protection which we promote in this paper as opposed to the current narrow view and see how such an approach is consistent with the objectives of reducing poverty and managing risks of the poor in the developing world.

4. Informal Sector and the WDR 2000/1

The objective of this section is to develop a broader framework for addressing the needs of those in the informal sector using WDR. The informal sector is currently under a lot of strain as a consequence of wrong macro-economic policies and absence of specific policies or programs to assist the informal sector. Thus, we explore here the issues that need addressing to ensure those in the informal sector are able to realize their full potential as a result of the reform programs that are being adopted in these economies. We use the WDR 2000/1 framework of promoting opportunities, facilitating empowerment and enhancing security and analyze the implications for the informal sector from these three angles.⁷⁴

4.1 Promoting Opportunities

The literature has several examples and extensive evidence as to how the lack of productive employment opportunities in the overall economy leads people to join the informal

⁷⁴ It is worth emphasizing again that the heterogeneity of the informal sector. This implies that all programs and policies discussed here may not apply in the same way to all working groups – e.g. micro-entrepreneurs, self-employed, home-based workers, unpaid workers, apprentices and wage workers. Wherever necessary, we will highlight the exclusive relevance of some instruments only for a smaller segment of the informal sector.

sector and how those in the informal sector are deprived of access to many opportunities.⁷⁵ This lack of opportunities does not enable those in the informal sector to attain the full potential in the activities they are involved in due to various constraints. Thus, as part of any comprehensive SP strategy, it is important to ensure that their opportunity sets are expanded through a variety of measures. In this context, government should focus on measures which increase employment and income opportunities through jobs, roads, power, and markets for products and inputs. Also schools, water supply, sanitation and health aspects which seek to enhance human capital can expand the opportunities for a large part of the informal sector. Government policies should strive to increase lucrative job opportunities for those in the informal sector micro-entrepreneurs so that they can apply their skills and entrepreneurship to activities where returns are high. Thus the government has to focus on removing the policy biases such that they can augment the productive capacity of the informal sector. This, apart from enabling them to involve in high return activities, will also provide incentives for them to grow out of poverty and expand their business opportunities.

Access to Credit

In addition, many studies have consistently revealed that the informal sector is curtailed by the lack of access to formal credit sources. It is clear that most individuals involved in the informal economy are “asset” poor and hence can not provide the required collateral for credit, except their limited human capital, skills or household asset base. Thus, financial institutions which serve this segment of the credit market should be encouraged and incentives should be given for their sustainability.⁷⁶ This problem has been identified as even more crucial in the case of women whose entry into informal sector is limited by the lack of titles to assets by women in most societies.⁷⁷ Hence, until measures can be designed to remove such discriminatory practices the future of women in the informal sector will be limited due to pre-existing conditions.

⁷⁵ Tokman (1989) and Bromley (1978) among others argue that lack of opportunities as an important concern for the informal sector. Others (e.g. Sethuraman, 1998) highlight the public sector contraction and lack of private sector growth as important issues in understanding the growth and trends in informal sector.

⁷⁶ As Tokman (1989) puts it credit is an important part of “productive assistance package” to informal sector.

⁷⁷ See Sethuraman (1998), Ela Bhatt (1999) among others argue that women have limited access to credit which affects their informal sector activities.

Government and donors have in a small way addressed these credit market constraints through expanding micro credit services to poor areas and informal sector activities.⁷⁸

Access to Markets

Most of the informal sector activities (especially micro-enterprises and home based workers) thrive on a very thin profit margin due to exorbitant costs of production, out of which transport accounts for a large share. In some Sub-Saharan African (SSA) countries it is claimed that a very large proportion (some times up to 30 – 70%) of the difference between cost of production and price received for sale of final product goes to take care of transport costs (including actual costs and bribes). Hence, reducing the transport costs and overall transaction costs by improving infrastructure and information technology in linking with markets can increase the profit margin and income of informal sector households. There are also many examples of the existence of primitive or outmoded production technologies in the informal sector. Some of these are due to lack of information and know-how while others are also due to lack of electricity and supporting infrastructure. Naturally, these inefficient production technologies lead in some cases to substantial reduction in productivity and profit in the informal sector. Thus, measures which ensure a steady supply and access to electricity and dissemination of information on improved production techniques will lead to a greater use of machinery, such that productivity and profits will be enhanced.

One of the perennial problems for the informal sector has been their limited access to potential markets. For instance, because the markets are not accessible, many informal sector producers are not able to achieve their full potential in terms of sales or profits. There are also instances where the informal sector does not have strong knowledge of the markets for which they could cater their products. This limits the potential set of activities of the informal sector and limits the potential for higher earnings. These issues clearly indicate the need for linking markets to people and ensuring that information regarding untapped markets are made known to the informal sector, an area in which the state could play a meaningful role, and indirectly lead to the upliftment of the informal sector. For instance, in many countries in SSA and Asia, the

⁷⁸ CGAP review shows that there has been substantial progress in micro finance institutions enabling poor access credit. See also ILO-STEP, WIEGO, USAID publications.

improvement in infrastructure – including access to water, electricity, roads – has opened up many more market opportunities to the informal sector than existed previously.

In this context, in addition to domestic markets one also need to focus on international markets. There are many examples where opening the economy has generated demand for many local products, especially for home workers, which were not realized hitherto. However, it is also important to mention that opening borders are not always favorable to the informal sector.⁷⁹ As we had already observed the thin profit margins in the informal sector make participants very susceptible to international competition and can adversely affect certain activities. But on the whole, the lack of opportunities for the informal sector micro-enterprises is definitely an area where opening new markets can help future trade and industrial policy reforms and should be the focus of future interventions.

Access to Human Capital

In addition to those constraints which limit the earning potential of those in the informal there are issues which impinge directly on the part of the population that depends on informal activities. Due to lack of recognition by institutions, difficulty in complying with regulations and sometimes scare tactics of state officials or the organized sector, the informal sector tries to be invisible to the rest of the economy and institutions.⁸⁰ One of the implications of this is that the informal sector population (especially women and marginalized groups) is cut off from many services, especially social services provided by the state and is unable to realize the full potential benefit from those services critical to enhancing their limited human capital. For instance, education, water, sanitation and health are services provided by the government in most cases but not very well implemented to reach those in the informal sector, especially the women in the urban slums of big cities and rural areas. Thus, to ensure that the informal sector benefits from these services the state should make a special effort to target programs such that those in the informal sector are able to benefit from them. It has been observed that because those in the informal sector are less educated and low on skills, they tend to value

⁷⁹ Lee (1997, 1998) indicates that the research community and policy arena has both positive and negative examples of opening trade barriers for the prospects of the informal sector.

⁸⁰ As Sethuraman (1998) points out informal sector can save up to 50 % savings by non-compliance of regulations and going underground, which also indicate the incentive for “invisibility”.

education less and also do not pay adequate attention to the human capital needs of their children.⁸¹ Hence awareness and advocacy campaign programs should be developed to inform the mothers of the benefits of education and provide special assistance to encourage the enrollment and learning of children from informal sector households. This will also ensure that the future generation of the informal sector will have a higher level of education and better able to reap the benefits of increased human capital. The development literature clearly indicate that this is a sure way to a world of unlimited opportunities.⁸²

Health Needs

The lack of access to water and sanitation also has an impact on the health of the adults and children in such households. Thus, in urban and rural areas where informal sector activities are concentrated, government programs should seek to improve water and sanitation needs. It is essential that a special effort is made to target health services for those in the informal sector communities such that they can benefit from public expenditures by the State on health and other social services. Given that informality, and sometimes illegality, underlies most of informal sector many government services do not reach them or they have very limited access to them. Unless the government makes a special effort to reach those in the informal sector who are driven away from the visible existence into hidden shelters they may never benefit from the government programs which seek to improve their lives. Targeted interventions might be necessary in the beginning to ensure they know of the availability of services. These interventions will enable the government to be a pro-active partner in expanding the opportunities for the informal sector which will in itself be more than adequate to pull them out of their vicious cycle of low earnings, low profitability and resultant poverty. Such measures will also reduce vulnerability and the probability of exposure to shocks. However, it is essential to underscore the importance of allowing the informal sector to maintain its character and not try to formalize them before they can have access to these services. When such approaches were pursued in many countries it has resulted in a failure to address the core needs of welfare of the informal sector workers.

⁸¹ Among others Tokman (1989), Sethuraman (1998) and Lund and Srinivas (2000) discuss this point in some detail.

⁸² World Bank (2000) shows how human capital is an important way out of poverty and low incomes.

Economic Growth

Irrespective of the above mentioned government programs, it is undoubtedly clear that overall economic growth is essential to expand opportunities. Lack of economic growth limits the potential of informal sector activities and their profitability. Hence, stable fiscal and monetary policy, stable investment regimes, sound financial systems, and a transparent business environment can generate direct and indirect benefits to the informal sector. Although overall economic growth is important, it is even better to have sustainable growth in sectors where the potential for productive activity is high and the activities availed by the informal sector are lucrative. This clearly shows that the pattern and quality of growth is also important for increasing the right type of opportunities for the informal sector. In order to ensure that the economy grows at a healthy pace it is clear that the country needs to adopt the right type of economic policies which unleash the potential of each of the productive sectors. For instance, public investments need to complement private investments which aim at enhancing competitiveness and generating employment opportunities. In addition to the overall economic policies which support growth, policies which remove structural barriers are an essential part of government policies. The implementation of economic reform programs – adopted in most countries in the 1980s and 1990s - has removed many constraints enabling rural and urban households to expand their opportunities, either by venturing into new areas or diversify existing activities to capitalize on newly generated opportunities. For instance, through liberalization, expanding access to international markets in agriculture, services and industry naturally offers huge opportunities for job and income growth for the informal sector.⁸³ Therefore, if a country experiences sluggish growth, it will naturally limit the potential of the informal sector and not enable those in such activities to earn a lucrative return on their investments and activities. Hence, even if targeted programs are aimed at assisting those in the informal sector, the lack of economic growth – especially the right type of growth - can limit the opportunities for those in the informal sector which are essential for many to move out of poverty. This emphasizes the point that economic policies which promote growth should be the center piece of any social protection strategy for the informal sector.

⁸³ Charnes (1998), Tokman (1989) among others highlight the importance of the right type of economic growth as a necessary way to assist the informal sector activities and best form of social protection!

It is essential to mention here that all economic policies are not pro informal sector; some policies will adversely affect informal sector activities and households. For instance, it is not inconceivable to have certain policies and regulations which limit the opportunities that the informal sector currently enjoys. In such cases alleviative programs need to be put in place to assist those who are adversely affected by economic policy reforms such as liberalization, price and regulatory reforms – all of which aim to remove unfair barriers to trade. During economic reforms in Asia, SSA and LAC (Latin America and the Caribbean) there were many instances where policy reforms unfairly affected certain groups of informal sector workers and activities, which had to be addressed using programs which aimed at easing the adverse effects.⁸⁴ In addition, attention should be given to the sequencing of policies and programs such that they do not unfairly disadvantage informal sector activities. Also, policies should give respect to the infant nature of most industries in the informal sector as opening trade and capital markets can lead to unfair advantage to certain multi nationals at the expense of local enterprises in the informal sector.

Asset Ownership

The limited stock and access to human, physical, natural and financial assets of the informal sector is clearly highlighted by many past studies. There is a very close link between asset ownership and access to opportunities. Government programs in health, education, infrastructure, etc. mentioned above are a very important means of building the human capital asset base of those in the informal sector. This means the government has to ensure that expenditures on these programs are protected over time so that the poor in the informal sector who depend on them are not adversely affected even during times of crises.⁸⁵ It is possible that the State can also provide incentives to the formal private sector to participate in the provision of some of these services, in addition to ensuring that government institutions do a better job in delivering quality services. One of the issues for improving the quality and relevance of these services is the participation of informal sector groups in deciding the types of programs they

⁸⁴ Tokman (1989) shows how economic reforms hurt the poor, especially in the informal sector in Latin America. Demery et al (199?) discuss the social dimensions of adjustment highlighting both the negative and positive effects of economic liberalization.

⁸⁵ SSA economic reform and East Asian crises literature highlight the magnitude of this challenge.

need and where they are needed most, especially in an environment of tight fiscal resources.⁸⁶ The linkages between different types of assets – human, physical, social, natural and financial – necessitate that action on all fronts are important and the inadequacies in one asset is closely linked to another. This definitely calls for a comprehensive framework for SP such that the inter-linkages are realized.

Gender and Social Inequalities

The lack of opportunities which limit the potential of the informal sector are not homogenous throughout the informal sector. These inequalities and differences are sometimes based on gender, ethnic, racial and social divides. The inequalities of opportunities in terms of gender are described in the literature and by the groups who are organizing themselves to fight such institutional discrimination.⁸⁷ As we have already observed, women, who form the majority in the informal sector, are the primary victims of gender based discriminations and inequalities that exist in societies. However, it is important here again to note that even among women there are some who are better endowed than others – that is to say those who have access to assets are less affected than the poor women who are institutionally and asset wise powerless. The heterogeneity in these aspects has not received adequate attention. There are other socially entrenched inequalities through ethnic, racial and class identities in different societies which prevents the realization of their full potential. There are instances where one group or caste dominates a trade area which naturally prevents others from being free to engage in such activities.⁸⁸ These issues have received inadequate attention in the call for public action hitherto. In SSA, and South Asia there are many examples in the informal sector where class, race and ethnicity in addition to gender perpetuating inequalities which need to be addressed if the informal sector is to provide equal access to opportunities for all. Government actions to resolve some of these challenges involve institutional change, and reforms which allow for local participation and public spending allocations to address the needs of those discriminated. In the case of gender, some of the areas which have received attention has been increasing access to

⁸⁶ Woolcock and Narayan (2000) discuss the effective role the poor can play in ensuring better service provision.

⁸⁷ Charmes (1998) Lund and Srinivas (2000) discuss this point in more detail.

⁸⁸ For instance, in Ghana it has been observed that the “Market Queens” monopolize the trade of fruits and vegetables which limits the potential for other women groups to enter such activity.

schooling, increasing access to credit through microcredit programs and reforming legal and regulatory frameworks to address asset ownership discrimination of women.

Spatial Inequalities

In addition to these social inequalities there are spatial inequalities which undermine the potential opportunities of informal sector activities. The literature clearly indicates that the informal sector is disadvantaged when located in poor and remote areas of most countries while the same activities are more profitable when they are closer to markets and better infrastructure.⁸⁹ For instance, many urban slums and rural areas face many disadvantages which limit their opportunities. The lack of health, education, infrastructure and financial services in these areas is looked upon as a form of discrimination against the informal sector. Some of the policies and programs mentioned above can directly and indirectly remove the inequalities which exist in the remote areas. However, in addition, there may be need for targeted interventions to remote areas to remove any barriers or basis of disadvantage those regions may face.

It is evident from this discussion that the areas in need of action are enormous and the State should join hands with all stakeholders, including informal sector workers and employers, if it is to be successful in ensuring that hindrances are removed and opportunities are created for the informal sector to be an important player in the economy and society of any country.

4.2 Facilitating Empowerment

We saw that enhancing the opportunities of the informal sector is a means to improve its predicament. However, it is important to verify that those in the informal sector have the means of benefiting from increased opportunities. Studies reveal that although opportunities are important it is not always possible for those in the informal sector to benefit because they are cut off from the channels of transmission and they seldom have the ability to take advantage of available opportunities.⁹⁰ It is indeed their status of informality that enhances their chances of being left out of many lucrative opportunities. Hence, it is essential that those in the informal sector are empowered to

⁸⁹ In fact Sethuraman (1998) discusses the positive and negative effects of being visible and closer to markets for informal sector activities.

⁹⁰ The point that economic reforms and growth per se is adequate to address the informal sector is a naïve view as highlighted in the literature repeatedly (see Tokman 1989; Portes, 1994; Sethuraman, 1998;)

claim their fair share of the economic dividend of policy reforms and are also able to exploit opportunities that open up for them. It is also true that increased opportunities for the informal sector can in themselves lead to greater empowerment. Thus, opening up a world of opportunities through economic reforms mentioned in the previous section can go a long way towards eliminating some of the obstacles to empowerment. One needs to recognize empowerment as a public good with many positive externalities to the broader economy and the informal sector. Empowerment can effectively act as a risk prevention and mitigation mechanism and reduce the need for a “band aid” approach to risk management. Where there are still constraints to empowerment, specific policy and program measures might be essential to deal with them.⁹¹

Institutional Reforms

The processes which inhibit the empowerment of those in the informal sector are deeply entrenched and sometimes epitomize the current institutional limitations. Thus, it is essential that institutional reforms are implemented to remove the barriers to empowerment and enable those in the informal sector to have free access to the opportunities. Institutions are not always accessible to those in the informal sector—due to institutional measures—some of which are unintended while others are deliberate owing to an unclear view of the workings of the informal sector. Thus, local government administration which is meant to assist the informal sector workers who are street vendors, market women, and SMEs have become agencies which are alienating and sometimes confrontational towards the informal sector. To change the current adversarial relationship one needs to bring about institutional reforms which remove existing barriers to interaction with the informal sector and also measures which communicate information about the rights and responsibilities of informal sector workers, which, in turn, will facilitate the empowerment of the informal sector.

Role of Trade Unions

Despite the increased recognition of informal sector’s contribution to employment and GDP among others, the lack of worker rights and legal status has tended to adversely affect the

⁹¹ Here again note our position is that economic policies and programs should be seen as first option for addressing empowerment before designing special programs to address specific empowerment needs. Among others McKee, Bhatt and Chen (1989) also support this view.

informal sector prospects. Trade Unions which traditionally tended to focus on protecting the formal sector workers have recently become increasingly aware of the need to bring the informal sector into their fold.⁹² Recent work by the ILO (2000) shows that the demand for such empowerment of the informal sector is great and the unions have to address these concerns if they are to represent *all* worker interests. In developing countries there are some “good practice” examples of the role of trade unions can play in assisting informal sector. Trade unions have the capacity and know-how to assist the informal sector workers to organize and make representation in national policy debates such that their rights are protected. Hence the need to empower workers in the informal sector and provide the much needed legal assistance is greatest today.⁹³ Unions also need to voice their concerns on behalf of the informal sector on issues such as the minimum labor standards, minimum wage negotiations among others to protect the rights of wage workers in the informal sector.

In many countries the lack of strong principles underlying governance has led public administration, legal institutions and public service delivery to become less efficient and accountable to the people it serves. Some of these problems are doubly serious for the informal sector as they do not have a cordial relationship with the state. The State for its part mostly views them as those who are evading tax and is mostly interested in pursuing them for tax purposes.⁹⁴ As argued by many, some of these positions are based on flawed or old fashioned economic theories, which viewed the informal sector as an illegal or underground activity. Some economists even seriously believed that the processes of economic growth and development will gradually eliminate the informal sector by making it formal.⁹⁵ All these views, have with time been proven inadequate and overly simplistic. It is now clear that informal enterprises (especially SMEs) are legitimate and they are here to stay and will not disappear with economic growth. In fact, there is evidence to the contrary – the informal sector is a growing phenomena in many parts of SSA and South Asia. These trends call for a complete change in the economic

⁹² Ratnam (1999) shows how in India unions traditionally considered interests of the organized and the informal sectors as conflictual and as threat to organized sector's future. Even when unions represent informal sector they mostly represent the interests of those in paid work.

⁹³ For instance, Adu-Amankwah (1999) demonstrates how trade unions in Ghana play an effective role in nurturing links with the relevant public authorities which can provide the protection the sector needs.

⁹⁴ In fact, there is long tradition of academic literature which has perpetrated this argument as discussed in Castells and Portes, (1989); Tokman (1989); Sethuraman (1998), Swaminathan (1991)

theories and outlook on informal activities and institutions. Therefore, governance reforms which seek to make the institutions more accountable and efficient need to pay special attention to the way existing institutions relate to the informal sector. Institutions need to be responsive to the needs of the informal sector by design and functioning, necessitating a cultural change in the way institutions accommodate the needs of the informal sector. Institutions need to be transparent and allow for participation of those in the informal sector as they seek to serve them so they will be able to better relate to those in the informal sector and to their needs. One area which can help informal sector empowerment is the legal assistance both in terms of disseminating information about rights and responsibilities and also in terms of access to legal aid in the course of legal procedures.⁹⁶ This is an area where the informal sector has been consistently disadvantaged and has shown a need for assistance.⁹⁷ The State, therefore, has a definite responsibility to protect the rights of the workers and ensure they are protected from discriminatory practices.

Participation

An important means to empower people is to promote community development with, participation of community members. Given that most informal activities are organized around occupational groups, the problems they face tend to be similar. Thus, forming them into groups and strengthening their networks to address some of their needs is essential. This will also ensure that government interventions are selective and mainly deal with issues which are not addressed due to market failure or where the informal sector needs public sector interventions most. SEWA, among others, has shown how most informal sector needs can be addressed through organizing and encouraging full participation of members of the informal sector community.⁹⁸ There are many other countries where local trade unions have played an effective

⁹⁵ Lewis (1954), Garcia (1982) among others expected informal sector to decline dramatically with industrialization. But as the data presented in Castells and Portes (1989) shows that it did not happen.

⁹⁶ Bhatt (1999) describes the importance of legal assistance in terms of her SEWA experience and Tokman (1989) also discusses this in some detail as part of his action plan.

⁹⁷ For instance Chune and Egulu (1999) discuss how the Kenyan unions have been on the forefront putting in place an enabling legal environment to assist in informal sector representation with government.

⁹⁸ The work of WIEGO, Home Net and Street Net in this aspect has been noteworthy as they have been at the forefront of organizing informal sector groups and empowering them.

role in enabling informal sector groups to be integrated into broader development policies and programs.⁹⁹ In

⁹⁹ Yu (1999) discusses how unions in Phillipines have risen up to the occasion to represent the informal sector interests.

addition, there is also sometimes a need for decentralizing the institutions which seek to serve the informal sector. When institutions are remote, they inhibit community participation and identification. Thus, we need to take the institutions closer to communities involved in informal sector activities to ensure that the informal sector relates better to the institutions that seek to serve them and benefit from it. Governments should also encourage dialogue between public institutions, trade unions and the informal sector groups as a way of empowering them. Given that most problems are common to most informal sector groups, seeking to understand their problems and explore solutions through open dialogue is very essential for appropriate reforms. In addition, government may also encourage discussions between and within informal sector groups such that through collective action and learning from others, the informal sector can be enabled to take measures to reduce their exposure to risks and uncertainties that are common to them.

Strengthening Networks

A very important way of empowering people is to encourage and strengthen networks among groups. This gives a group solidarity and social cohesion which encourages minority or discriminated groups to make their voice heard in policy and institutional reforms¹⁰⁰. Sometimes the divisions among these groups also lead to lower bargaining power. Hence, occupational groups and trade associations can be important media of empowering the informal sector activities. They will be able to ensure that their rights and benefits are not infringed out of ignorance or through deliberate measures. In addition to representation at the national level, there is also a need at the international level to recognize the rights of informal sector groups such that their concerns can be addressed through international fora and indirectly put pressure on governments to address the needs of informal sector groups. Here again WIEGO, HomeNet and StreetNet are some examples of international networks which provide a voice to informal sector groups at the national and international levels.

Social and Gender Discriminations

Some of the constraints on the empowerment of the informal sector are discriminatory practices in terms of class, gender, locality or industry which introduce barriers to their

¹⁰⁰ Robb (2000) and Narayan (2000) among others have emphasized the importance of the poor's views in influencing policy and programs choices, which equally applies to the informal sector.

interactions with institutions. Thus, measures need to be introduced to address these issues at the source of their origin such that they can be treated with appropriate measures to address the root cause of the problem. Empowering marginalized groups should be an essential element of any SP strategy for the informal sector.

Empowering Women

As we already noted under opportunities, women are a very integral part of the informal sector. They exceed men in terms of participation in informal activities.¹⁰¹ This means that special attention needs to be given to women and womens groups such that they can be empowered to fight both structural and institutional discrimination. In many cases, access to resources and markets are constrained along gender lines. Also, in the context of families where culture unfairly treats women with limited rights, the women who are involved in the informal sector face double discrimination both within the family and at work place. Thus, gender empowerment deserves special attention and as many examples indicate, gender based solutions go a long way towards empowering those in the informal sector . In addition to ensuring gender discriminations are addressed, empowering women will make certain their contribution to the family and the economy is further enhanced. However, given that some of this disenfranchisement is deeply rooted, evidence shows that the measures for empowerment require action on many fronts – political, legal, public action and awareness creation. Representation of women in local government and institutions which seek to address informal sector issues can ensure that women’s concerns are recognized and addressed. It also gives women a seat at the table when it comes to political, local government or institutional reforms.¹⁰² Discriminations in access to credit markets has received a lot of attention and experience shows measures through micro finance has enabled women to be empowered in their activities.¹⁰³

Empowering the Poor and Voiceless

In addition to gender, there are also class based inequalities which exclude certain groups. These become obstacles in carrying out economic activities, especially in the informal

¹⁰¹ Charmes (1998) very clearly show using statistics the growing importance of women in the informal sector, while Sethuraman (1998) gives many examples of women being treated unfairly compared to men in the informal labor markets in terms of working conditions, wages and other benefits.

¹⁰² SEWA has some pioneering work in this area encouraging women to have their concerns expressed in various local government institutions.

sector. It is clear that given that some of these class based discriminations are deep rooted, affirmative action may be required to empower them to fully participate and benefit from the economy. Some of these discriminatory practices are also supported by local written and unwritten legislation. Hence, legal and legislative systems need to be reformed as part of empowering groups which are systematically discriminated. Also, representation of minority groups in local government, community organizations and national organizations can ensure that to some extent their interests are represented.

4.3 *Enhancing Security*

By virtue of its character and in terms of its activities, the informal sector is exposed to a variety of risks which makes people insecure. In addition, the prevailing conditions in the economy also leads to differing levels of vulnerability which also needs to be considered in conjunction with exposure to risks and existing insecurities.¹⁰⁴ The informal sector – like many other groups in society – is exposed to economic shocks, natural disasters, ill health, disability and personal violence.

Economy wide Shocks

The economic literature, especially the economic history literature, provides ample evidence to conclude that economic shocks are more the norm than the exception (Collier). Many countries face economic crises due to one reason or another, which results in substantial downturns in fortunes and opportunities of various activities in the economy. This is even more true for the informal sector which is vulnerable due to the many precarious conditions under which it operates. Also, the fact that most informal sector activities are trying to exploit the limited profit margins from activities in the periphery of the formal economy, they are more exposed to the harsh consequences of economic downturns. The fact that a majority of those in the informal sector lack opportunities for diversification and have inadequate capacity to cope with economic downturns makes their predicament worse than most others in the economy. Hence, special consideration may have to be given in times of economic shocks to protect those in the informal sector against the vagaries of crises. Also, programs must be put in place *ex ante*

¹⁰³ Murdoch (1999) among others discuss this point in detail.

¹⁰⁴ Alwang and Siegel (2000) discuss the concept of vulnerability and exposure to risk and highlight how our lack of understanding might lead to wrong policy choices and instruments in dealing with them.

to build their capacity to mitigate risks when they occur, in addition to addressing risk prevention and risk coping strategies. Governments may choose to develop insurance programs which enable those in the informal sector to be protected during times of crises. Some of these insurance programs can be community based or at micro level of an industry or occupational groups.¹⁰⁵ Examples of this abound in large numbers around the world although the efficacy of this instrument is still somewhat unclear. But the fact that many in the informal sector do not have access to formal sector insurance, social protection for the informal sector naturally opens the door for innovations such as micro insurance or community insurance which can go a long way towards reducing the harsh effects of economic shocks and other household crises. The literature emphasizes the need for a mix of community based, markets based and state level interventions to support the management of risks in the informal sector (Holzmann and Jorgensen, 2000). The specific combination of programs and policies will of course depend on the nature and frequency of risks and adequacy of existing risk management strategies (Lund and Srinivas, 2000). Of course, institutional and implementation capacity is another criteria that determines what programs are relevant.

Macro Shocks (Covariate Risks)

It is clear that there are some common risks which all households and workers face. Financial and terms of trade shocks have impact on all activities but more so for the already vulnerable informal sector through quick and arbitrary changes in input and output prices. In this sense it is essential that governments implement sound macro economic policies and financial systems to ensure that they are resilient or have the potential of reducing the effects of broad macro shocks. In addition, measures need to be put in place to protect the public spending on programs which seek to serve the poor and informal sector during times of fiscal crises such that they are not exposed to additional shocks during such downturns. Apart from these broad policy measures, it is important to design and activate safety net programs during macro shocks such that the informal sector does not face harsh effects. Since these can be expensive, governments need to be prudent in mixing safety nets with broad policy support to elicit self help and other coping strategies as alternatives.

¹⁰⁵ SEWA, Grameen Kalyan, FINCA a few of the examples of many of these programs. Brown and Churchill (2000) discuss many of these programs in detail.

Natural Calamities

In addition to economic shocks, there are many natural disasters like floods, drought, famine, earthquake, etc., which also have a devastating impact on the informal sector. Sometimes the informal sector not being engaged in diversification of primary agrarian activities makes their situation even more vulnerable to natural disasters. Also, as we have already observed, natural disasters do not only wipe out the productive base of the informal sector, but can also affect the limited household assets they own. This, therefore, becomes a double negative effect on the informal sector prospects. Thus, in order to reduce the harmful effects of natural disasters on the informal sector, programs may have to be put in place, in addition to the general programs for the affected population. Weather based insurance schemes have been proposed in a few countries to reduce the impact of weather related disasters on the primary agrarian activities and other informal sector activities, which are derived from it.¹⁰⁶ Government support for these programs have been limited and the need for overall government policy support will go a long way towards securing the future for informal sector in the midst of natural disasters, which have become all too common.

Illness

One of the important insecurities any worker faces is the risk of illness, which can have a detrimental effect on the earnings potential. This is especially important for informal sector worker/employer whose health risks do not only affect his business but also the welfare of the whole family. Many studies show health risks as the primary risk of informal sector workers.¹⁰⁷ Many health insurance schemes have been experimented around the world and have shown to be useful in addressing health risks. However, in addition to the general risk of health conditions, the case of the informal sector can be more precarious due to several work related factors. Adherence to Occupational Safety and Health (OSH) standards are very weak in many micro and small scale enterprises in

¹⁰⁶ This new instrument seems promising and measures are under way to experiment them in few countries (see Skees et al, 1999; Varangis et al, 2001).

¹⁰⁷ Dror and Jacquier (1999) discuss in detail the demand and innovations in health insurance in the informal sector to protect those excluded from formal schemes.

the informal sector. The low profit margins and lack of knowledge of safety standards have been prime reasons for higher levels of accidents in the informal sector, leading to adverse health outcomes. Evidence from developing countries is replete with examples of many informal sector activities having low safety standards leading to the higher incidence of accidents, which are seldom addressed by social protection measures. The lack of coverage of safety standards and limited coverage of compensation schemes for the informal sector necessitates action by the government to improve security in the informal sector. Improving safety standards in the informal sector will decrease accidents and increase their security against such health effects and thereby prevent and mitigate the risks due to the lack of OHS.¹⁰⁸ On the other hand, reforms aimed at improving social protection schemes such as compensation and social security will ensure that in case ill health limits the earning potential of informal sector participants in the short or long term, there are programs that protect the incomes and the welfare of their families, thereby providing options for coping with risks.

HIV/AIDS

Another recent development in health concerning the informal sector is the incidence of HIV/AIDS. The high rate of this in informal sector can be attributed to many reasons, which are beyond the scope of this paper. Within the purview of this paper, however, it is important to explore how to develop programs which can reduce the incidence of HIV/AIDS and how the industry can cope with those who have already become victims of this illness. There are many examples of community level awareness campaigns, which aim at informing individuals about risky sexual behavior.¹⁰⁹ In addition, there are also programs which aim at providing care and rehabilitation to those infected at the community level.

Insurance

One way in which informal sector has been able to cope with shocks and natural calamities is through a variety of insurance products. Most of the formal insurance programs and pensions schemes which are very useful helping individuals cope with risk in the formal sector are seldom available to those in the informal sector. The lack of formal insurance, social

¹⁰⁸ Forastieri (1999) discuss the OSH policy issues in the context of informal sector in detail.

¹⁰⁹ Lund and Srinivas (2000) discuss the HIV/AIDS issues in the informal sector with some community care options in detail.

security or pension type instruments to protect informal activities has necessitated innovative mechanisms.¹¹⁰ In terms of providing social security for different occupational groups Welfare Funds have become very popular in assisting informal sector manage risks in times of crisis. In India, for example, there are many examples of occupational group based welfare funds in insuring occupation specific risks.¹¹¹ However, the efficacy of these instrument when covariant risks affect the whole economy or informal sector group is still not clear. This is an area which needs more research. It is worth mentioning, in the absence of insurance, that national safety nets or risk management programs which have proven effective in protecting households from the many covariant risks have also aided self employed and home based workers immensely.

Civil War

One outlier, of course, is the risks generated by civil strife. Naturally, these unrests among other consequences limit the potential of those in the informal sector to earn a living. The opportunities of the informal sector can be unfairly affected during civil war. Although the first-best measure to deal with these risks are to prevent the crisis in the first place, when that is not possible one needs to put in place programs which sustain informal sector workers and employers such that the short fall in incomes can be compensated.¹¹²

Discrimination/Austerity measures

The informal sector has evidenced many sources of discrimination from public agencies in the process of their productive activities. The authorities have resorted to violent activities against individuals and households in the informal sector bringing about much physical harm and loss to productive activities. Some of these have been carried out in the pretext of ensuring the informal sector is registered and is liable for taxes. The lack of legal protection for informal sector has resulted in insecurity for those in the informal sector against the violent atrocities committed against them. This means that the state has to put some protective clauses which secure the informal sector individuals and their activities from violent attacks. This will also ensure that informal sector activities are carried out to their full potential without having to

¹¹⁰ Alwang and Siegel (2000) discuss the potential and problems of micro insurance which has shown new promise as a risk management instrument for the poor and those in the informal sector.

¹¹¹ Subrahmanya (2000) discusses the existing experience and potential for innovation of these welfare funds in detail. See also Rajan (2001) for a discussion on the promise of many Kerala welfare funds.

operate underground and for the fear of being harassed, which tend to curtail their investments. In addition to measures of legal protection, the state may also put in place programs which will reduce the harmful effects due to violence against informal sector. The street vendors in many countries have faced violence which has been addressed both through legislative reforms and introduction of programs. For example in South Africa, in Durban township, there have been innovations which have brought about amicable solutions for the informal sector and local government authorities concerned with the implementation of law and order (Lund and Srinivas, 2000). There is a need for every government to learn from such “good practices” such that the plight of the informal sector can be addressed and their concerns about their safety and security resolved.

There are examples of public authorities, which when alerted to these excesses, have taken appropriate action which have resulted in substantial improvements on the working conditions of informal sector workers and hence addressed their insecurities. However, there is a definite need for clarification of rules and regulations by which informal sector has to operate and by which authorities enforce laws. Unless and until this is done informal sector will continue to be insecure and vulnerable to the many obscure laws. The above discussions show that the informal sector is frequented by risks – both covariate and idiosyncratic – to a greater extent and is in need of sustainable and cost effective risk management instruments to continue their productive role in the economy.

5. Informal Sector and the SRM framework

The SRM framework provides an integrated approach to SP, primarily using risk as the foundation. It explains how all individuals, households and communities are vulnerable to multiple risks from different sources. It also distinguishes between different types of risk (e.g. covariate and idiosyncratic), especially highlighting the fact that some risks can be prevented and mitigated while others are unavoidable and how the strategies for risk management have to be cognizant of those realities as they develop a variety of instruments and coping strategies. This, therefore, provides a framework to discuss how the poor in particular can better manage income and

¹¹² Collier has addressed the economic and social consequences of civil war and conflict and how it affects the livelihood strategies of the poor which is relevant here.

consumption risks. In this context it discusses three broad mechanisms of dealing with risks – namely risk prevention, risk mitigation and risk coping¹¹³.

According to the SRM approach “Social Protection consists of public interventions (i) to assist individuals, households and communities better manage risks and (ii) to provide support to the critically poor.”¹¹⁴ However, because the SRM approach deals with the whole population or all the poor, it does not expound in detail or exclusively address issues related to workers’ interaction with markets and risks nor does it address the concerns of workers who are outside the formal sector, whose incomes are dependent on informal activities. This section will try to explore in some detail the implications of the SRM framework for understanding the informal sector risks and how it can aid in developing a comprehensive approach to social protection for the informal economy.

At the outset it is clear that those in the informal sector face risks and uncertainties which are different and sometimes with greater probability than the poor population or workers in general. Hence, first understanding the sources of risks the informal sector face and trying to see what measures are in place to deal with them will allow us to evaluate the adequacy of the existing social protection measures for the informal sector. As we have argued already, such an exercise will also more clearly highlight the narrowness of the current SP approaches, especially in the light of the needs of the informal sector.

The informal sector literature provides numerous examples to highlight the fact that informal sector workers and employers face increasing vulnerability due to the absence of a conducive regulatory environment or failure to implement existing policy measures. In addition, the inability to deal with the risks they face leads those in the informal sector to engage in low yield and low risk activities. This could be due to the fact that existing risk management instruments are weak or inadequate. It is important to

¹¹³ Holzmann and Jorgensen (1999) provide clear definitions and examples for each of the risk management categories (Table 1), while Lund and Srinivas (2000) provide informal sector specific examples for each (see Tables 4.2 and 5.2). Hence we will not repeat them here.

¹¹⁴ Holzmann and Jorgensen (2000, p9) provides this definition. This definition is more inclusive than the other ones in the literature which tend to limit to special programs and interventions targeted at the informal sector, especially for risk coping. Lund and Srinivas (2000) do go beyond risk coping but do not include economic policies and traditional government programs such as health and education among others. We want to highlight that such an inclusive approach is an integral part of any SP strategy, because economic policies and health and education interventions primarily seek to address risk management comprehensively, albeit inadequate to cover all risk management.

emphasize that in addition to sometimes poorly designed SP instruments, there are numerous examples of good social protection instruments being weakly implemented due to the lack of institutional capacity or budgetary problems leading to significant increases in social costs to the informal sector. The inadequacy and lack of appropriate instruments to deal with risks lead the informal sector to use strategies which endanger future earnings capacity, contributing to deeper poverty and destitution in many cases, e.g. child labor, misuse of physical and human assets, corruption, illegal activities, etc.

Asymmetric information problems which are abundant in the informal sector lead to absence or poor functioning of insurance markets which are essential in managing risk. For instance, moral hazard, adverse selection and insufficient property rights which lead to limited insurance options for the informal sector need to be addressed by appropriate public interventions which address regulatory reform and facilitate the development of appropriate insurance instruments to manage risks. It is important to note, as we also mentioned in enhancing opportunity section, that some of the measures to deal with market failures of this kind require efficiency and redistribution considerations which go much beyond the narrow constructs of current SP programs.

In addition, the concepts of vulnerability and exposure to risks which are important in SRM has relevance for designing appropriate SP interventions for the informal sector. Many SP discussions do not pay adequate attention to these two issues which are very important in deciding the end result of any risk.¹¹⁵ SP measures can be designed such that they can reduce exposure to risks. The presence of risk in itself should not deter informal sector activities as many high risk activities are also high return activities. Thus, measures which reduce exposure to risk through mitigative actions are important in encouraging a lucrative and attractive informal sector. In addition, even if one is exposed to risk, measures can be put in place such that the level of vulnerability is reduced . Such measures can go a long way towards reducing the harmful effects of many inevitable risks the informal sector faces. Hence, the SRM framework points us towards actions which are more pro-active and inclusive rather than passive and narrow in dealing with risks which are pervasive in the informal sector.

¹¹⁵ Alwang and Siegel(2000) provide an excellent discussions on this important issue.

6. Implications for Bank's SP Operational Strategy

The previous two sections have highlighted how these different development frameworks which have been put forward can be used to view the various issues that impinge on the informal sector and what they mean for developing an appropriate social protection strategy for the informal sector. The role for each of the stakeholders can be spelt out based on the above discussions. However, in this section we mainly deal with the implications of these frameworks for a broader view of SP for The World Bank and its strategy to assist the informal sector as an integral part of its development agenda. Parts of these discussions can be generalized to be applicable to other international donor communities, of which there may be others, which are not spelt out in detail here because they are beyond the Bank's current mandate. It is worth emphasizing that this section should be seen as the beginning of a dialogue on expanding current SP strategy and not the last word.

It is essential that informal sector concerns are well integrated into the Bank's work program. The Bank's mandate of addressing poverty through lending and non-lending services should integrate informal sector concerns clearly as part of its objectives. In addition to incorporating informal sector issues into on-going operational tasks and non-lending services, one may need to develop new instruments which can provide the services required by countries. In this section we provide some possible suggestions on how the Bank and possibly other donors might address informal sector issues by modifying their interventions.

The Bank has 4 possible options for the way it can approach SP for informal sector. They are:

1. No Change in current Policy
2. Expand non-lending Services to recognize and address informal sector issues
3. Encourage on-going lending programs and new lending operations to incorporate informal sector issues
4. Change operational practices and design new instruments to deal with informal sector issues

The Bank's current policy, however, does not exclusively address informal sector concerns as part of its on-going activities. Hence the first option of "no change in current policy"

is basically not a possibility. In fact, such a position will be in conflict with Bank's mandate of poverty reduction, given that a large majority of informal sector workers would be classified as below or near the poverty line. Thus the Bank needs to move away from its apathetic view of the informal sector and ensure that it is considered as an integral part of its development mandate and dialogue. To be fair, one can say that the Bank is not completely indifferent to informal sector concerns, but its current concern with that issue is rather inadequate.

The second option for the Bank is to objectively include informal sector issues in Analytical Advisory and Advocacy (AAA) services. These AAA services broadly include Bank's non-lending and policy dialogue services which are an integral part of Bank services to its client governments. It is clear that this option is very necessary to address informal sector concerns much more broadly as discussed in this paper. The failure to address this will not enable the government to use the instruments at its disposal to effectively address informal sector concerns. If AAA activities increase the knowledge base of donors and other stakeholders to develop a better understanding of the informal sector issues that in itself can go a long way towards expanding the options for addressing such issues.

The third option of encouraging Bank's lending programs to recognize and include informal sector issues in on-going and new lending programs is both necessary and feasible. This gives opportunity for the Bank to engage in a dialogue through its lending operations to highlight and include informal sector needs through projects. For instance, Bank's lending programs address a variety of development concerns of a country and this gives the best opportunity to integrate informal sector into the mainstream policy and program interventions. This will also provide options for selectivity in addressing informal sector through macro or sector programs as the case may be. This is an area which has had the least amount of progress and a concerted effort is required to remedy this situation.

The fourth and final option is to explore the possibility of designing new interventions – both lending and non-lending services – which can address informal sector concerns. This is akin to the outcry by some external agencies for the Bank to expand its instruments such that it can work with partners other than the government in poverty reduction efforts. Such new approaches among other things will include options to provide lending and non-lending services to NGOs, informal sector occupation groups, and community organizations representing

informal sector interests. Although the payoff from such a strategy is great it involves changes in Bank's operational practices which may not be feasible in the short run.

Let us now explore in detail what options two and three entail. These include non-lending services and lending programs which the Bank provides to countries and how they can be used to address informal sector concerns. It is obvious that the former is definitely the most important and also can form the basis for the latter given the current lack of understanding of informal sector needs.

Non-lending Services

It is clear that there is a range of non-lending services which should take a high priority in the Bank's effort to address informal sector SP needs. This is because we need to know more about factors that influence the welfare of those in the informal sector. It is extremely difficult to design useful interventions based on our existing limited knowledge. Also, current policies are very narrow and policy reforms need detailed information on issues and options in a broad array of interventions.

At the country level a first task the Bank could assist in carrying out is a risk and vulnerability mapping and SP inventory exercise for the informal sector. It is essential in this regard to do a *risks analysis-social protection matrix* which will highlight the source, correlation, frequency and intensity of risk and a mapping of responses by different stakeholders.¹¹⁶ We will have to then identify which current SP programs address identified risks and assess their adequacy and effectiveness to address the specific risks. It is essential that there is a detailed analysis of risks and existing formal, informal and market based programs for the informal sector before one decides what new programs, if any, should be introduced. This will lead to the subsequent exercise which is how to comprehensively protect individuals from the risks they face. For instance, in some cases it will be measures which can expand the existing program, while in others it will be reforming existing approaches, in still some others it will be to design new instruments. This exercise and resultant dialogue will provide a conducive environment to discuss SP issues for informal sector within the broader SP framework espoused in the previous sections. In the PRSP/HIPC countries there is a good opportunity to address

¹¹⁶ World Bank (2000) PRSP SP toolkit has suggestions on how such a risk-vulnerability mapping exercise can be done. Few of these exercises are currently under way in World Bank's Latin America region.

these issues contextually as the majority of poor in these countries belong to the informal sector and are exposed to many risks and lack interventions which can assist them.

In addition, this in-depth knowledge will assist in ensuring the policy reforms pursued, say, in the financial, private, agriculture, and industrial sectors, or issues relating to the regulatory environment can be meaningfully addressed. Currently, there are extremely few cases in which reform programs have exclusively recognized and addressed informal sector issues. In fact, one could say most government policy choices do not consider the existence of informal sector as a legitimate entity. Even the World Bank's CAS dialogue is mostly oblivious to informal sector needs. Sometimes projects realize too late during implementation when it is almost impossible to address informal sector issues. This lack of recognition of the informal sector in policy reforms can lead to adverse consequences due to errors of omission or errors of commission. By errors of omission we mean that implementation of certain components of the reform programs which ignore informal sector having a harmful effect, while errors of commission implies the limited or incorrect informal sector view in policy agenda leading to implementing anti informal sector reform measures which unfairly affect those in that sector. Both these are equally harmful and, thus, need to be addressed by all stakeholders.

Institutional reforms also need to include informal sector issues in its agenda. Also, institutional capacity building and awareness programs need to ensure informal sector issues are given importance. The lack of understanding and ignorance of institutions about informal issues leads to inappropriate actions by those in authority. Informal sector institutions themselves should make appropriate reforms to better work with the wider economy and government administration. For instance, lack of information leads those in the informal sector not to follow regulations due to ignorance. Apart from lack of understanding, the absence of regulations and laws which protect the rights of those in the informal sector also needs to be addressed. Judicial and legal reforms which form an essential part of reviving private formal sector growth should also consider private informal sector which is much bigger and has greater potential in many countries. The Bank and the broader development community should address together with the government informal sector concerns as part of judicial reform, regulatory reform for the private sector, urban upgrading programs, social sector reforms and safety net interventions. In this context, broad macro and development policy dialogue with government should incorporate

informal sector issues. The Bank should assist client governments to undertake a critical review of existing policies, programs and reforms being implemented or proposed, to identify and alert governments to the potential adverse effects it could have on the informal sector. Such interventions will ensure that the untapped potential of the informal sector is effectively realized for broader economic gains and private sector growth.

The Bank should forge partnerships – internally and internationally - to further the informal sector cause. This is important because the effectiveness of SP for informal sector depend upon the existence of social alliance which seeks to protect informal sector. On the international front, the Bank has already started working on informal sector issues with some of the lead agencies like ILO (STEP), WIEGO, and SEWA among many others as a way of increasing knowledge of the Bank and its clients on this issue and raise public exposure to the issue. The Bank is participating in conferences on informal sector to play a role in the formulation of the emerging consensus on policies regarding the informal sector. Internally Bank's ability to raise awareness and sensitivity of staff to informal sector issues will be a prerequisite for the success of these interventions. Social Protection network at the Bank has already started a series of seminars and workshop on many informal sector issues towards achieving this objective. Internally there is already regional (South Asia, Latin America, Sub-Saharan Africa) and network (Macro (PREM), Financial Sector (FSD), Gender) partnerships which are collectively addressing the common informal sector concerns. These activities inform staff of the facts about informal sector, promote discussions on how Bank could address informal sector issues through its many activities. In fact, the Bank commissioned two seminal papers on the link between informal sector, poverty and gender as part of WDR 2000/1 which has become very useful not only for the Bank but also for the outside world to understand the problems and potentials of this "hidden" sector.

The Bank should also emphasize the importance of strengthening social capital and social networks in client countries through its policy dialogue.¹¹⁷ It is very clear that informal sector problems are not addressed partly because they do not have networks which can collectively find solutions to the many risks and uncertainties they face. The lack of social capital

¹¹⁷ Woolcock and Narayan (2000) discuss the importance of social capital issues for development policy and practice.

has proven a major handicap for the informal sector in terms of addressing risk and uncertainties that frequent the sector. Hence an effective program to build and harness social capital is an important part of SP for the informal sector. It is also important for the Bank to expand its dialogue to include informal sector associations, say in CAS or PRSP discussions, such that their views and concerns can be represented as part of the national dialogue. This is an area where the Bank has just started to broaden its scope and there is a long way to go, at least in terms of bringing the informal sector into the fold.

Lending Services

Currently, the Bank has at its disposal many instruments which can address informal sector needs. Refocusing lending programs to address informal sector concerns is a feasible option. This may, however, involve redesigning or developing new project components which can be integrated within existing lending operations. On going and new social sector investments – health, education, social welfare – need to include the informal sector as an important beneficiary of its investments. Such programs can address the human capital needs of the informal sector. Apart from building human capital, lending activities can also assist in building physical capital through infrastructure interventions, through road projects and social fund programs. Many studies show that limited access to markets and ancillary facilities unfairly affect the informal sector activities which can benefit from investment in infrastructure, especially if they are developed in areas where informal activities are predominant. Poverty reduction initiatives also have to ensure they address the needs of the informal sector poor. Given that large number of informal sector workers are poor women and have limited access to credit, has enabled Bank's gender and micro credit programs to address the informal sector needs in many countries. However, now the challenge is in mainstreaming some of these experiences such that they can be replicated widely.

In addition, the Bank should ensure that informal sector needs are addressed when it is called upon to design and finance safety net interventions, which mostly ignore the peculiar needs of the informal sector. For instance, after the East Asia crisis, the Bank designed safety net programs which did include the informal sector as an exclusive beneficiary. These activities show that there are many opportunities to address informal sector needs. The Bank should also retrospectively review existing lending programs in each of the sectors, during mid term reviews,

to ensure that informal sector activities are not being neglected and are addressed wherever possible.

New initiatives like Community Driven Development (CDD), Poverty Reduction Strategy Credit (PRSC) and HIPC should be seen as potential opportunities to explore how informal sector issues can be addressed in a country. These new instruments provide additional opportunities to include informal sector issues as part of the lending operations of the Bank.

7. Concluding Thoughts

As already mentioned, this paper is just a beginning on the dialogue to expand SP instruments and interventions which deal with the informal sector. We hope that these discussions will not merely end up expanding our understanding but will also influence government and donor policies and programs which address informal sector issues.

It is worth emphasizing the congruence of the different frameworks which we have highlighted in enabling us to expand the SP framework. All three measures or action fronts of the WDR – opportunity, empowerment and security - are equally important to revive the informal sector and to provide greater impetus to the future of informal activities. These three principles complement the SRM framework of risk prevention, mitigation and coping. For instance, increased opportunity will increase the security and bargaining power of the informal sector in relation to state, society and markets. Similarly, empowerment measures will expand opportunities and result in greater security. Also, increased security means greater scope for new opportunities, diversification of portfolio and greater power. Hence, the three lines of attack on the informal sector need to continue. This paper has argued that there is a role for state, formal and informal institutions, markets and community organizations, individuals and households in meeting the formidable challenge of providing SP measures to the informal sector in order to protect workers from the risks they face and realize their untapped potential.

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