

## **OECD Development Centre Seminar**

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### **Informality: Exit and Exclusion**

**Comments on the book written by Guillermo E. Perry, William F. Maloney, Omar S. Arias, Pablo Fajnzylber, Andrew D. Mason and Jaime Saavedra-Chanduvi  
The World Bank, 2007**

The book is a major and challenging insight and new look at informality in Latin American and Caribbean countries in the light of the famous “Exit, Voice and Loyalty” by A. O. Hirschmann (1970).

Latin America is probably the region of the world where data on informality have been collected and accumulated the most regularly since the 1970s. It must be recalled, however, that since the very beginning of the reflections on the concept of informality, Latin American social scientists associated the term with marginality, poverty and exclusion: the reason for that is that they were used to define the informal activities by the criterion of earnings and to measure employment in these activities by the number of workers earning less than the legal minimum wage.

Therefore it is not surprising that informality was, in their works, quasi-entirely defined by exclusion. It must be noted that it was different in Africa where the ILO Kenya report (1972) orientated research towards the dynamics of micro-enterprises in poor and low income countries opening and paving the way for more optimistic views on the informal sector. And as a matter of fact, it exists empirical evidence in the region that own-account workers and employers of micro-enterprises earn several times the legal minimum salary and even several times the average wage in the formal sector. In this sense, the interpretation by exit rather than exclusion was present though not expressed as such and the evidence provided by the book that “voluntary entrants in the informal sector yield higher or equal levels of welfare” compared to the formal sector, though a new view in Latin America, echoes some findings in other regions .

The originality and value of the book is in its dynamic approach of the three margins of informality: owners of small unregistered firms contemplating registering their workers, formal and informal workers weighing advantages and disadvantages of jobs in the two sectors (informal and formal), and large size firms contracting their workers without labour benefits.

The originality of the approach also lies in the use of data sources which are not so common in the studies of informality: labour force surveys of course, but especially used as panel data, and also motivational and self-rated welfare responses from Business surveys. Various definitions (productive, legalistic) or proxies (self-employment, size, absence of social protection) were also mobilised to investigate the heterogeneity of informality and finally this empirical approach succeeded in finding again the ILO definitions adopted in 1993 and 2003 (in fact the definitions adopted by the International Conference of Labour Statisticians).

According to the authors, the traditional exclusion view of informality characterises mainly the wage-earning informal workers who represent nearly 30% of urban jobs and the new exit view of informality characterises the self-employed who represent approximately 24% of the urban jobs.

Of course there are some more complexities on which I would like to insist:

- In many cases, it is much more a question of “no entry and stay outside” rather than “exit”
- There is another alternative to “exit”: it is “no exit” and simultaneously undertaking an informal activity as self-employed for instance multiple jobs holding (the so-called pluri-activity) that allows wage-earners of the formal sector to stay in the formal sector and benefit from social protection while operating simultaneously informal activities. This is another margin which is still difficult to identify clearly because data are scarce and not very reliable. The Italian method (an indirect method in the terminology of chapter 1) used for the revision of GDP in the 1980s is interesting in this respect.
- Another complexity lies in the so-called “missing middle”, this intermediary sector which is missing in the statistics and based on the observation that the distribution of employment in a country is generally bi-modal: many jobs are created by the micro-enterprises of the informal sector, many jobs are created by large firms and in the middle, small and medium enterprises are missing, giving room to the interpretation of an absence of transition from informal to formal. As a matter of fact, growth in micro-enterprises can take the form of a multiplication of small establishments which are subsidiaries of the main firm but are captured as autonomous in the statistical surveys. These small establishments have the advantage to remain hidden or not too visible and not to need any change in the type of management of the workforce. Tunisia and Turkey have provided some evidence of the existence of the “missing middle”. Of course the missing middle is of particular interest because these enterprises are precisely at the margin, trying to push the borders of informality further.
- A third complexity lies in the status of the home-based workers or outworkers. Labour force surveys in Latin America have all and for a long time, collected information on place of work, but the use of these data has been very scarce. Statistics and graphs presented for Mexico and Brazil show that the proportion of informal workers increase in large size firms (but is not true for Argentina). There is here a problem of invisibility of home-based workers in this sense that they can be considered as sub-contracted by formal firms that pay for their services and include their cost as an intermediate consumption in their accounts, while many of these workers will declare themselves as paid employees in labour force or household surveys. Therefore they don't contribute to the value added or to the GDP, appearing as simple costs.

- The balance between work and household-social responsibilities for women is well addressed and it explains why self-employment may be preferred to paid employment in the formal sector. Recent time-use surveys in Latin America (Mexico, Nicaragua, Uruguay) can provide useful data to inform this complexity.
- Finally the other complexity lies in the content of social protection. The single question asked to the workers: do you benefit of any social protection? is probably insufficient to draw the border between formality and informality. Some labour force surveys in transition countries and also in other countries have developed a set of questions to take into account the variations in the observed situations: do you benefit of paid annual leave, paid sick leave, maternity leave, unemployment benefits, etc. The book notes that even in informal enterprises, workers may benefit from annual paid leave and actually social protection may not be envisaged as uniquely public social protection.

Lastly, I would not like to add my contribution to the cacophony of characterisations and methods of measurement of informality, but it is necessary to say that national accounts and official statistics (on labour force and employment) do capture informality or at least most of informal activities, but they cannot allow distinguishing them precisely.

The household sector production can be used as a proxy for informal sector production and actually the informal sector has been defined as a sub-sector of the household sector in the System of national Accounts (the SNA) itself. In this sense, the comparison between the household sector production in the satellite account of Mexico and the estimate by Schneider, is not valid because the first refers to production by informal economic units and included in the GDP, while the second refers to illegal, underground, unregistered activities which may or may not be included in the GDP.