Informality and Globalisation

IN SEARCH OF A NEW SOCIAL CONTRACT

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Preface

The global reality of informal work today is one of both change and continuity. Where globalisation and technology bring about new activities, too often they informalise previously formal employment and enable new forms of informal work; yet in activities that continue to be dominated by precarious and low-income self-employment, such as agriculture in the poorest countries, informality remains the norm.

In most cases, therefore, the changes brought about by globalisation have not induced – within the political, economic and social configurations of low- and middle-income countries – an organic, positive change in the status of workers in the informal economy.

As a result, nearly 60% of the world's workers are excluded from the protections afforded to formal workers, but also from public services, such as healthcare, education and skills training, which are necessary to support working life.

In this context, the idea of the social contract provides a useful analytical lens for several reasons. It helps to assess the problems with the status quo: the systemic failures, blind spots, unfair relationships and unspoken assumptions which reproduce the inequalities disadvantaging workers in the informal economy. It also warns us against falling into a situation of even deeper inequality, one in which predatory forms of capitalism and punitive actions from the state are intensified.

Perhaps most importantly, however, it sets out a vision for transformation, towards a level playing field. A collective vision where workers in the informal economy are recognised as workers; laws and policies are responsive to their needs; reciprocal, productive relationships unite them, the state and capital; rights and responsibilities are fairly distributed and spaces for dialogue opened up.

On the back of its detailed portraits of informal workers, and its fresh analysis of informality within the global economy and digital platforms, this report makes a critical contribution by delineating the differences and interactions between the substantive and procedural dimensions of social contracts. It makes the case that understanding how the two interact within a particular society or context is vital to understanding where and how a social contract that is more inclusive of informal workers and their families may be established.

The conclusion that addressing informality requires the procedural dimension of the social contract to better reflect the substantive realities of a society, and that working towards this requires social dialogue between all parties, including informal workers themselves, must be taken seriously by governments at all levels, from the local to the global.

Laura Alfers

Director, Social Protection Programme

Women in Informal Employment: Globalizing and Organizing (WIEGO)

Foreword

Informality has been at the heart of the OECD Development Centre's work since its creation. In 2009, its seminal report *Is Informal Normal?* highlighted the fact that, despite a preceding decade of fast growth and poverty reduction worldwide, most workers were in fact operating in the informal economy. It helped frame the Centre's *Multi-dimensional Review of Peru* in 2015 and the *Multi-dimensional Review of Paraguay* in 2018.

The follow-up report, *Tackling Vulnerability in the Informal Econom*y, published with the International Labour Organization (ILO) in 2019, provided an unprecedented exploration of the many faces of informality, highlighting the need for multisectoral approaches to address vulnerabilities of informal workers, as well as the need to promote formalisation. The report remains a reference guide for the Centre and its partners in their efforts to promote the development of more cohesive societies.

Since 2019, a series of major international crises have sent shock waves throughout the global economy and disrupted labour markets worldwide, which prompted the Centre, building on its earlier work, to highlight the causes and consequences of informal employment in the context of globalisation. This report thus provides:

- up-to-date, detailed portraits of informality in low- and middle-income countries, with a unique cross-country comparative dimension, identifying a number of common trends – including the staggering impact of the coronavirus disease (COVID-19) crisis on informal workers and their families – as well as regional and country specificities.
- a detailed overview of the complex impacts on both formal and informal labour of trade liberalisation, the development of global value chains (GVCs) and the consequences of technological change, including the emergence of digital labour platforms.
- a comprehensive analysis of the links between informality and the social contract, opening new avenues for tackling informal employment and the vulnerabilities of informal workers and their families.

The report is based on rich micro and macro data, including (i) recent ILO individual-based indicators of informality, available for 147 developing, emerging and developed economies, and (ii) the OECD Key Indicators of Informality based on Individuals and their Household (KIIbIH), available for 43 developing and emerging economies.

The objective of the report is to provide a better understanding of what can be done to support the formalisation agenda, taking into account the opportunities and challenges brought about by globalisation and new forms of work, and how enhancing social contracts may contribute to this agenda.

Informality and Globalisation: In Search of A New Social Contract has been produced in the context of the OECD Development Centre project "Tackling the Vulnerability of Informal Workers and their Household Members", with financial support from the Swedish International Development Cooperation Agency (Sida). The report supports the priority actions of the "New Deal for Development", agreed at the High-Level Meeting of the Governing Board of the OECD Development Centre in October 2020.

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The report is the result of data collection, analytical work, drafting, and fruitful collaboration between various authors across the Organisation for Economic Co-operation and Development (OECD), including Mariya Aleksynska, Antoine Bonnet, Alexandre Kolev, Thomas Manfredi, Justina La, and Emilie Wojcieszynski. Following collaboration between the OECD Development Centre and the International Labour Organization (ILO) on their joint report *Tackling Vulnerability in the Informal Economy* (2019), Florence Bonnet (ILO) drafted the Portraits of Informality (Chapter 2) based on the recent ILO statistical update of *Women and Men in the Informal Economy* (2023). Uma Rani (ILO) provided special input to Chapter 5.

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Editorial

We are midway to the 2030 deadline for the Sustainable Development Goals (SDGs). When global leaders signed off on the SDGs in 2015, they promised to leave no one behind. This year, when they gather to take stock at the UN SDG Summit, they will find that billions of people worldwide remain marginalised and that much remains to be done on the road to sustainable development.

Nothing describes this challenge as starkly as the plight of informal workers, who make up nearly 60% of the global workforce, and nine in ten workers in low-income countries. Informal workers lack social protection, enjoy fewer rights at work, and have fewer opportunities to upgrade their skills. Too often, their families live in highly precarious situations.

Policy makers have long known that promoting sustainable development means considering the informal economy. Creating more formal jobs, converting informal jobs into formal, and reducing vulnerability of informal workers and their families by affording adequate protection serve important developmental functions. The ability to deliver better public services, such as education and healthcare, to all citizens, including informal workers and their families, not only improves longer-term outcomes of populations, but also makes economies more resistant to shorter-term crises. Yet, progress towards formal employment has been slow since the OECD Development Centre published its seminal *Is Informal Normal?* report in 2009.

The problem, as this study argues, is that informality cuts deep. It cannot be addressed through economic growth alone, or through one-off policy measures in individual sectors or domains. What we really need is a fundamental look at social institutions, underlying norms and cultures. We need to understand how citizens, the state, workers and enterprises agree on shared goals, work together towards them, and distribute power and resources. In other words: we need to discuss the social contract.

This study helps us understand how global trends have affected informal employment and the importance of the social contract in mediating its impact. It shows that some countries have managed to turn international trade, global value chains and new technologies into more formal and better jobs. In other countries, globalisation has undermined working conditions and eroded public trust in institutions.

Our analysis shows that countries with strong social contracts have been better at harnessing the benefits of globalisation and weathering storms such as the COVID-19 crisis. A strong social contract is one where legal frameworks are inclusive, fair and relevant for all citizens. It is where citizens are able to comply with laws that are adapted to their needs, and trust their institutions to deliver good-quality public goods and services. It is where multinational companies conduct their businesses responsibly, and where informal worker associations, civil society organisations, and consumers have a voice.

For policy makers, this vision can be as daunting as it is inspiring. But it is also urgent. The global context will not become easier anytime soon, and the next big challenge for informal workers is looming: dealing with the climate crisis and environmental depletion, and with the transition to green energy.

Helping policy makers address informality and boost social protection will continue to be a high priority for the OECD Development Centre in the years ahead. It is a main pillar of our Programme of Work.

Stronger, more shared and greener: this is development we can do together.

Ragnheiður Elín Árnadóttir

Director, OECD Development Centre

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Abbreviations and acronyms

ASEAN	Association of Southeast Asian Nations
AUC	African Union Commission
BPO	business process outsourcing
CEPII	Centre d'études prospectives et d'informations internationales
CFW	contributing family workers
ELMPS	Egyptian Labor Market Panel Survey
Eora26	global supply chain database
EU	European Union
FAO	Food and Agriculture Organization of the United Nations
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GVC	global value chain
HDI	Human Development Index
IBGE	Instituto Brasileiro de Geografia e Estatística (Brazilian Institute of Geography and Statistics)
ICLS	International Conference of Labour Statisticians
ICSE	International Classification of Status in Employment
IFC	International Finance Corporation
ILO	International Labour Organization
IOM	International Organization for Migration
ISIC	International Standard Industrial Classification
ITMF	International Textile Manufacturers Federation
ITUC	International Trade Union Confederation
KIIbIH	Key Indicators of Informality based on Individuals and their Household
KOF	Konjunkturforschungsstelle (Swiss Economic Institute)
LAC	Latin America and the Caribbean
MENA	Middle East and North Africa
NAFTA	North American Free Trade Agreement

NEET	not in education, employment, or training
NGO	non-governmental organisation
NHS	National Household Survey
OAW	own account worker
OECD	Organisation for Economic Co-operation and Development
OSH	occupational safety and health
PALMS	Post-Apartheid Labour Market Series
PCA	principal component analysis
PNAD	Brazil National Household Sample Survey
PPP	purchasing power parity
Sida	International Development Cooperation Agency (in Sweden)
SME	small and medium-sized enterprise
T&C	textiles and clothing
TiM	trade in employment
UNDP	United Nations Development Programme
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNICEF	United Nations Children's Fund
UNRISD	United Nations Research Institute for Social Development
VHLSS	Vietnam Household Living Standards Survey
WB	World Bank
WIEGO	Women in Informal Employment: Globalizing and Organizing
WTO	World Trade Organization
WZB	Berlin Social Science Center

Executive summary

Informality worldwide is a reflection of the social contracts in place

Globally, informal employment remains the norm. Even before the coronavirus disease (COVID-19) crisis, nearly 2 billion workers, representing close to 60% of the world's employed population, had informal jobs, which typically means they have no social protection, fewer rights at work, and less access to training.

The longstanding structural deficit in formal job creation, coupled with a non-existent or inadequate level of protection for informal workers, remain a major source of vulnerability for those workers and their families, particularly in low- and middle-income countries. Any sustainable development strategy must therefore have formalising the economy and reducing the vulnerability of informal workers at its heart.

But where to start? Informality is highly heterogeneous. Its determinants and manifestations are diverse, complex and context specific. They do not merely result from insufficient growth. They depend on a society's institutions, norms, culture, and level of economic development, among other factors. Informality is in fact best explained as the reflection of the *social contract* of any given society.

A social contract is the implicit agreement between citizens, the state, workers, and enterprises on how to distribute power and resources in the pursuit of common goals such as equity, fairness, freedom, security, and eventually social justice. Social contracts differ across countries and change over time. Where legal frameworks, institutions and procedures fail to deliver on that agreement, whether as a result of poor design or implementation, informality levels tend to be high and in turn associated with poor social outcomes (e.g. in terms of access to healthcare and education prospects), which reinforces the vulnerability of informal workers and their family members. In many parts of the world, particularly in low- and middle-income countries, the COVID-19 crisis has considerably eroded the social contracts, which had already been weakened by decades of globalisation and rapid technological change.

Globalisation and the COVID-19 crisis have contributed to eroding social contracts, especially in poorer countries

While greater integration in the global economy can be a powerful determinant of economic growth, productivity and efficiency, its impact on formal job creation in much of the developing world thus far has been ambiguous. Greater integration with the world economy has been associated with lower levels of informal employment in upper-middle-income and high-income countries, but not in lower-middle-income and low-income countries. A comprehensive analysis of recent trends shows the following:

- *Trade liberalisation* has an asymmetrical impact on informal employment: increased export opportunities tend to boost formal employment opportunities, whereas import liberalisation can lead to formal employment losses in sectors, industries, and regions most exposed, reallocating labour to where informality is prominent, and raising the general level of informal employment.
- The expansion of *global value chains* (GVCs) has created additional, complex challenges. Informality within GVCs depends on the types of linkages (backward or forward), the way

production is organised, governance modes, possibilities of upgrading within and across GVCs, purchasing practices, and activity sectors. GVCs in agriculture and in garment manufacturing have some of the largest informal employment footprints.

- New forms of employment, largely spurred by changes in technology, have created more challenges for social contracts. In particular, although *digital labour platforms* offer new opportunities for formalisation – by providing better traceability, transparency and accountability in economic activities – they remain largely associated with high shares of informality.

In that context, the COVID-19 crisis' staggering impact led to a further erosion of social contracts: lockdown measures, curfews, travel restrictions and international trade disruptions resulted in massive job destruction, particularly for women and in sectors with higher-than-average rates of informality. At the height of the crisis, the number of informal jobs plunged by 20%, about twice the impact on formal employment. As the world recovers from the COVID-19 pandemic, informal employment is reverting to its pre-COVID-19 crisis levels, led by the return of informal workers to their activities; new entrants into the informal sector, including workers previously outside the labour force (casual, own-account or unpaid family workers); and the informalisation of previously formal jobs.

Policy recommendations to reinvigorate social contracts to tackle informality

As the *social contract* approach reveals, reducing informality and the vulnerability of informal workers and their household members requires more than boosting economic growth or developing one-off policy responses. A comprehensive effort to reinvigorate social contracts is key to addressing the challenges posed by globalisation and rapid technological change, thus rendering societies more resilient to current and future crises. It requires actions on many fronts and from a wide range of stakeholders:

Governments should:

- expand the coverage of formal legal frameworks and social protection; ensure sufficient levels of protection; and improve compliance by making them relevant and fair to informal workers
- improve access to, and quality of the public services most valued by all citizens, including informal workers and their family members, such as healthcare, education, and skill development
- enable the development of formal employment through co-ordinated policies on labour, social protection and skills, but also by supporting innovation, access to credit, and labour mobility
- accompany GVCs development by policies regulating sub-contracting; promote voluntary and create legally binding due diligence standards, such as the ones set in the *OECD Guidelines for Multinational Enterprises* and *OECD Due Diligence Guidance for Responsible Business Conduct*
- bring digital labour platform work within the scope of existing regulations; encourage the formalisation of self-employment; ensure that platforms pay their share of taxes and social security contributions; enforce regulations to categorise workers as employees where appropriate; modernise laws to address the platforms' modes of work; and leverage technologies to formalise.

Multinational enterprises should improve their responsible business conduct in order to promote formal employment in subsidiaries and among suppliers. The lead firms should strive to ensure that the suppliers and sub-contractors disclose the details of sub-contracting arrangements, honour existing contracts, use written contracts, and comply with national labour and social security regulations.

Finally, informal worker *associations*, *civil society* organisations, as well as *consumers*, have an important role to play in helping to ensure that integration into the global economy is beneficial for all. They should be given a voice and included into the development of policies that concern them.

1 Overview

This overview summarises the key findings and policy recommendations of the report. It shows how the recent crises underscored the necessity to enhance the social contract in many countries, to make it inclusive of informal workers and their families, with the goal of building better and stronger societies.

The three years since 2020 have presented the world with a series of challenges – from the COVID-19 crisis to Russia's war of aggression against Ukraine – which are greatly affecting the poorest and most vulnerable groups, in particular informal economy workers and their family members. In many parts of the world, these crises added to existing challenges and considerably eroded the social contract between citizens, the state, workers and enterprises. In fact, these crises underscored the extent to which most social contracts were already weak and eroded by years of globalisation and rapid technological change. Major gaps and shortcomings in labour and social protection systems were exposed, such as the lack of social support for workers in the informal economy, in particular for women, and the massive economic costs of inadequate social protection. These crises also highlighted the vulnerability of different actors to disruptions in global production, especially in GVCs built according to subcontracting models; and vulnerability to new ways of work that shifted the risk burden to workers. Overall, these crises underscore the necessity to enhance or even rethink the nature of the social contract in many countries, and to make it more inclusive of informal workers and their families.

Portraits of informality in world recovering from the COVID-19 crisis

Prior to the COVID-19 pandemic, informal employment was already a major challenge in many countries

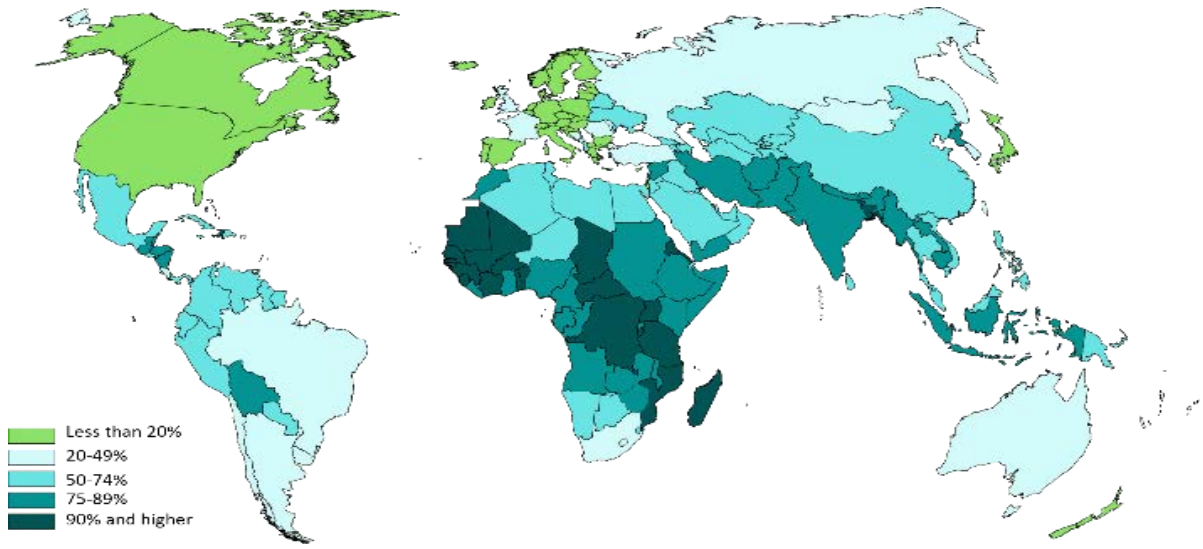
On the eve of the COVID-19 crisis, about 2 billion workers, or almost 60% of the world's adult labour force, were in informal employment (Figure 1.1). More than 80% of enterprises operated in the informal sector worldwide (ILO, 2023[1]).

- Informal employment represents 89.0% of total employment in low-income countries, 81.6% in lower-middle-income countries, 49.7% in upper-middle-income countries and 15.9% in high-income countries.
- The percentage is highest in Africa, but with significant differences between countries in the region, ranging from 15.0% in Seychelles to more than 90.0% in several African countries.
- In Asia and Pacific, the rate of informal employment ranges from less than 20.0% in developed countries in the region, such as Australia or Japan, to almost 90% or more in Bangladesh, Cambodia, India, and Lao People’s Democratic Republic.
- The Arab States have the third-highest regional level of informal employment (54.0%).
- In the Americas, informal employment ranges from 9.8% in North America to 53.6% in Latin America and the Caribbean (LAC). There is also significant variation across the region, ranging from 24.5% in Uruguay to between 30.0% and 40.0% in Costa Rica and Chile, almost 80% in Guatemala and more than 80% in the Plurinational State of Bolivia, Honduras and Nicaragua.
- In Europe and Central Asia, informal employment represents 19.7% of total employment, standing at 13.5% in high-income countries and at 27.8% in middle-income countries. In Albania, Armenia, Kyrgyzstan and Tajikistan, at least one-half of workers hold informal jobs.

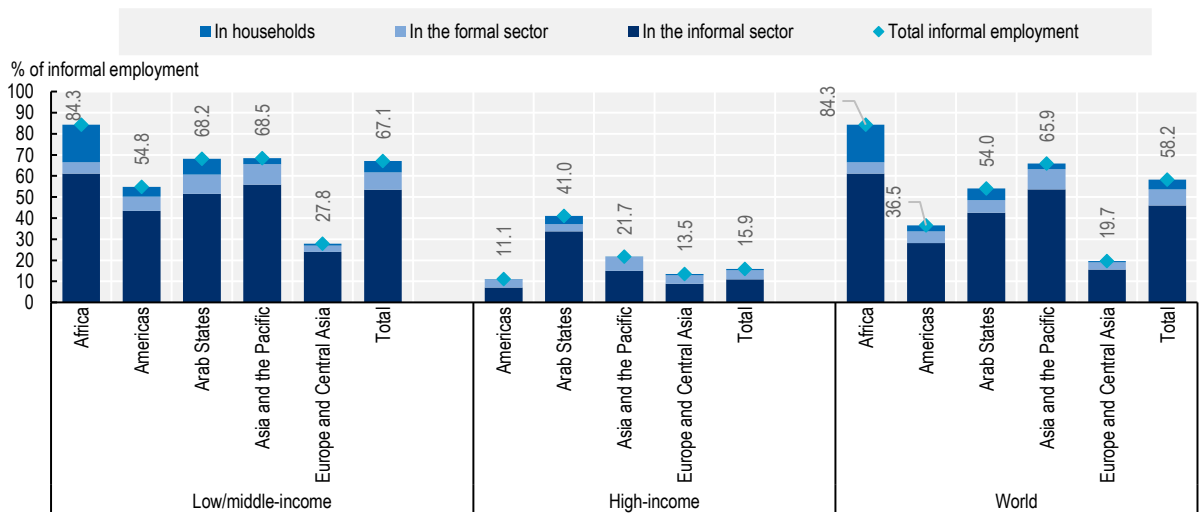
Figure 1.1. Informal employment dominates in the Global South

Informal employment as percentage of total employment

Panel A. Country data



Panel B. Global estimates



Note: A common set of operational criteria is systematically used to identify workers in informal employment and those employed in the informal sector. Own-account workers and employers are in informal employment if they run informal sector economic units (non-incorporated private enterprises without formal bookkeeping systems or not registered with relevant national authorities). Employees are in informal employment if their employers do not contribute to social security on their behalf or, in the case of missing answers in the questionnaires if they do not benefit from paid annual leave and paid sick leave. Contributing family workers are in informal employment by definition (ILO, 2003[2]; ILO, 2018[3]).
Source: (ILO, 2023[1]).

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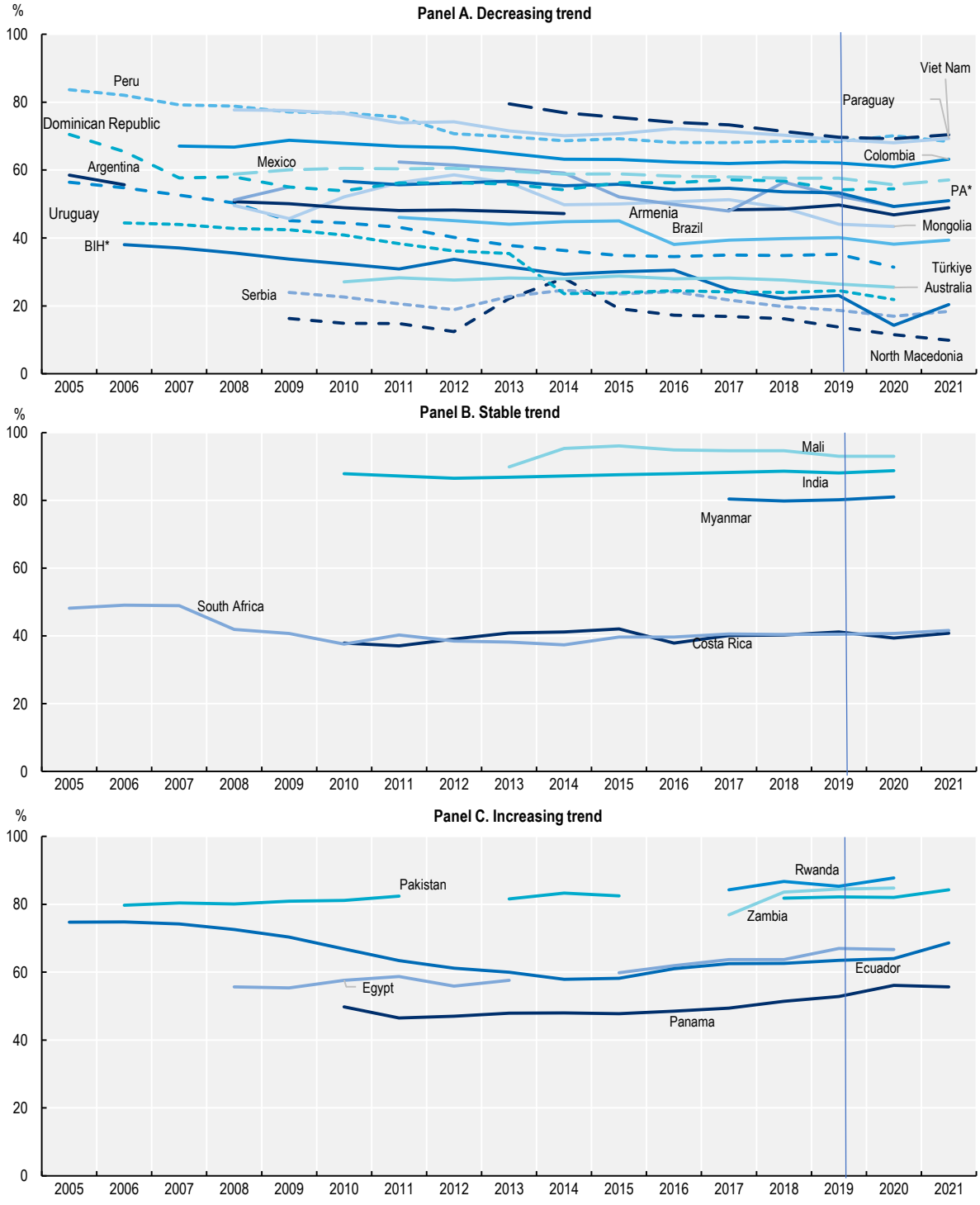
Informal employment trends also vary greatly across countries, with some countries making considerable progress towards formalisation, whereas others experiencing persistent or increased levels of informal employment (Figure 1.2).

Figure 1.2. Global trends in informal employment

Informal employment as percentage of total employment



Note: See note under Figure 1.1, Panel A. *PA: Palestinian Authority. *BIH: Bosnia and Herzegovina.
Source: (ILO, 2023[1]).

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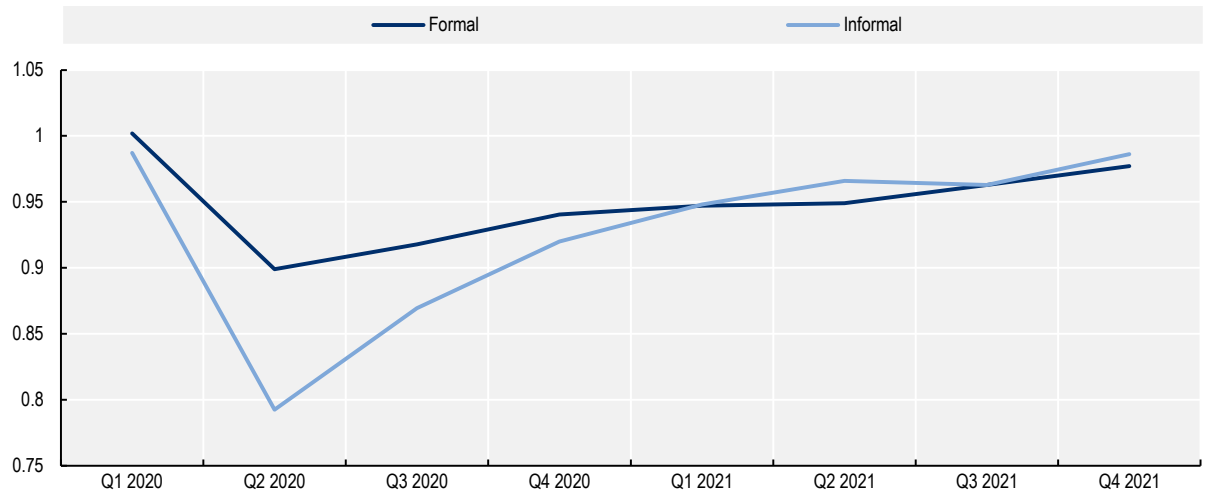
The COVID-19 crisis disproportionately affected the informal economy

Unlike previous recent economic crises, the COVID-19-related crisis has been unique in the way it has affected informal employment. For the first time ever, the informal economy did not provide a safety net for formal workers – something that it usually provides in a recession. Around the world, both formal *and* informal workers lost their jobs and became inactive, losing access to any economic opportunities whatsoever. In many countries, informal workers were more likely than formal workers to lose their jobs and to leave the labour force, for several reasons: widespread informality pervaded sectors heavily affected by lockdown and containment measures; there was limited possibility of telework; terminating informal employment relationships was relatively easy; and there was a higher incidence of informal workers in smaller enterprises, which struggled to survive longer periods of inactivity and had less (or no) access to support measures, including worker retention schemes (ILO, 2020[4]; ILO, 2022[5]). Since the majority of informal workers do not have employment-based social protection or, in the case of independent workers, access to measures aimed at keeping enterprises afloat, these workers and their families were left unprotected.

At the height of the crisis, the number of informal jobs plunged by 20%, about twice the impact for workers in formal employment (Figure 1.3) (ILO, 2020[4]). The decline of informal employment, as a share of total employment, led to a one-off formalisation of the labour market in Q2 2020 in many countries. This, however, was associated with the destruction of informal jobs rather than their formalisation, and a surge in poverty. After the initial losses, informal employment recovered faster than formal employment, especially by Q3 2021. By Q4 2021, the recovery in informal employment had overtaken that of formal employment.

Figure 1.3. Evolution of informal and formal employment (adjusted for population aged 15-64 years)



Note: Estimates based on trends in the number of formal and informal jobs in Argentina, Bolivia (Plurinational State of), Brazil, Chile, Costa Rica, Dominican Republic, Ecuador, Guyana, Mexico, North Macedonia, Palestinian Authority, Paraguay, Peru, Saint Lucia, South Africa, Uruguay, and Viet Nam. See individual country results in *A review of country data. Impact of the Covid-19 pandemic on informality: Has informal employment increased or decreased?* (ILO, 2022[6]). Missing observations are imputed using time-fixed effects in a panel regression of countries without missing observations.
Source: Authors' computations.

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Three transitions underpinned the growth of informal employment in 2021. First, many informal workers returned to their economic activities. Second, new entrants, previously outside the labour force, entered

informal employment, often as casual workers, own-account workers or unpaid family workers, to offset losses in household income. Third, the informalisation of previously formal jobs also took place. In the absence of formal employment opportunities, formal wage earners or formal business owners sought any opportunity to earn income, including in the informal economy. This structural deficit of formal job opportunities represents a serious challenge for an inclusive recovery. The prevalence of each of these forces determined the extent of (in)-formalisation of labour markets in different countries.

Globally, the incidence of informal employment is highest for own-account workers, home-based workers, small firms, in agriculture and rural areas

Status in employment has a major bearing on the risk of informality. Globally, own-account workers and workers in non-standard forms of employment are most at risk of informality. Own-account workers and contributing family workers represent 62.7% of informal employment, five times more than among workers in formal employment (12.3%) worldwide. In 2019, 50.0% of part-time and 69.8% of temporary employees were informally employed; the corresponding figure for employees in permanent full-time employment was 15.6%.

There were about 260 million home-based workers in the world in 2019 (ILO, 2021[7]). The percentage of informality among home-based workers ranges from 98% in Southern Asia and the Middle East and North Africa to 63% in Eastern Europe, Southern Europe and Central Asia (Bonnet et al., 2021[8]). During the COVID-19 crisis, homeworking related to teleworking has expanded. In contrast, home-based workers who do not use Internet in their work, including traditional self-employed and industrial outworkers, as well as the contributing family workers who depend on them for work, suffered the greatest loss of work and income (ibid).

In small enterprises, most employment is informal, but the amount of informal employment in large formal enterprises is also significant. Smaller enterprises account for the bulk of total employment globally, especially in low- and middle-income countries. Units with fewer than 10 workers accounted for 55% of total employment globally, and as many as 8 out of 10 workers or more in low- and lower-middle-income countries and in Africa. Nearly 90% of own-account workers operate informally, with informal employment standing at 82.5% in enterprises with between 2 and 5 workers, and at 25.3% in enterprises employing more than 50 workers. As a result of small enterprises' greater use of informal employment, enterprises with fewer than ten workers account for 76.7% of total informal employment globally and up to 90% or more in low-income countries and in Africa.

Informality has a strong sectoral dimension. The sectors where informal employment rates exceed the global average include agriculture; the domestic work sector; household production for own use; construction; accommodation and food service activities; the wholesale and retail trade; and repair of motor vehicles and motorcycles. Informality also stands at 51% among workers in essential occupations and sectors of activity – those that helped economies run amidst the pandemic (ILO, 2023[9]). Strong gender segmentation also figures in informal employment across sectors. The COVID-19 crisis amplified the vulnerabilities of many informal workers because of its strong sectoral dimension. Accommodation and food services were disproportionately affected by lockdowns and travel restrictions (ILO, 2022[10]). Workers in agriculture faced difficulties selling their products in urban markets, despite being considered at lower risk catching and spreading the virus, and playing the role, in some countries, of "last resort" employment (ILO, 2020[11]). The consequences of the war in Ukraine exacerbated the crisis, and agricultural workers were further affected by disruptions in imports of agricultural products and fertilisers, as well as soaring prices.

Finally, informality has a strong rural dimension. Workers in rural areas are almost twice as likely as those in urban areas to be in informal employment: 82% versus 43%. Conversely, 63% of workers in informal employment live in rural areas, whereas 78% of those in formal employment live in urban areas.

Women and men in informal employment remained unequal in the face of the COVID-19 crisis

Globally, informal employment is a greater source of employment for men, but there are large disparities across countries and occupations. Worldwide, more men (60.2%) than women (55.2%) are employed informally, but this global estimate reflects the weight of major countries, such as the People's Republic of China (hereafter "China"), where men face greater exposure to informality. The gender difference at the global level also results from structural effects associated with low female labour force participation rates in some countries (as seen in India or Pakistan), which attenuate the effect of their high female informal employment rates in the global and regional estimates.

At the country and regional levels, there are large gender inequalities. In a small majority of countries for which data are available (56%), the share of women in informal employment exceeds that of men. Informal employment is a greater source of employment for women than for men in Central and Western Asia, Southern Asia, sub-Saharan Africa, Northern, Southern and Western Europe, and in most low- and lower-middle-income countries. By contrast, the percentage of informally employed men is substantially higher than the percentage of women workers in the Arab States and North Africa, where the female employment-to-population ratio is much lower than the male ratio. In this region, the minority of women employed are overrepresented in the public sector, as well as in occupations and types of enterprises that are more likely to be formal. In most regions, women in informal employment are among the most vulnerable groups in the informal economy.

Informality not only exacerbated workers' vulnerability to the COVID-19 pandemic shock, but also widened gender employment gaps during the crisis. Women tend to be overrepresented in sectors that were massively hit by the crisis and the lockdown measures, such as food and accommodation, tourism, domestic services, or retail and wholesale, often working informally or with low-status jobs. Moreover, when faced with the decision to leave employment to care for children (during closures of schools) or sick people, many households chose the individuals who earned the least amount of money, usually women. The increase in unpaid care and domestic work and the consequence of lockdowns (need to care for the children out of school) forced many women out of the labour force. This disproportionately affected women working informally, who faced poorer working conditions, the absence of flexible work arrangements, and who, in most cases, did not benefit from social protection or unemployment benefits. As a result, the share of informally employed women declined by 24% in Q2 2020; the corresponding figure for men was 18% (Figure 1.4). Among formally employed workers, however, no such trend emerged; over the same period, formal employment declined by about 10% for both men and women.

Figure 1.4. Evolution of informal and formal employment by sex, 15-64 years

Reference quarters in 2019 =1

Estimates based on trends in the number of formal and informal jobs in Argentina, Bolivia (Plurinational State of), Brazil, Chile, Costa Rica, Dominican Republic, Ecuador, Guyana, Mexico, North Macedonia, Palestinian Authority, Paraguay, Peru, Saint Lucia, South Africa, Uruguay, and Viet Nam. See individual country results in *A review of country data. Impact of the Covid-19 pandemic on informality: Has informal employment increased or decreased?* (ILO, 2022[6]). Missing observations are imputed using time-fixed effects in a panel regression of countries without missing observations.
Source: Authors' computations.

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Youth, older workers and migrants also face greater risks of informality

Globally, there is substantial variation in the level of informal employment over the life course, with youth and older workers disproportionately affected. More than three-quarters of youth and older workers are in informal employment, whereas the comparable figure for those aged 25-64 years is 55%.

In contrast to native-born populations, migrant workers typically tend to be employed in informal jobs. The average incidence of informal employment is three percentage points higher for the foreign-born population than for the native-born population; it is seven percentage points higher for non-citizens than for workers who are citizens of the country in which they live. In some countries, such as Argentina, Bolivia, Brazil, Colombia, Costa Rica, Ethiopia, and South Africa, there is a more than ten percentage point difference in the informality rate among foreign-born and native-born populations.

Informal employment as a reflection of the social contract in place

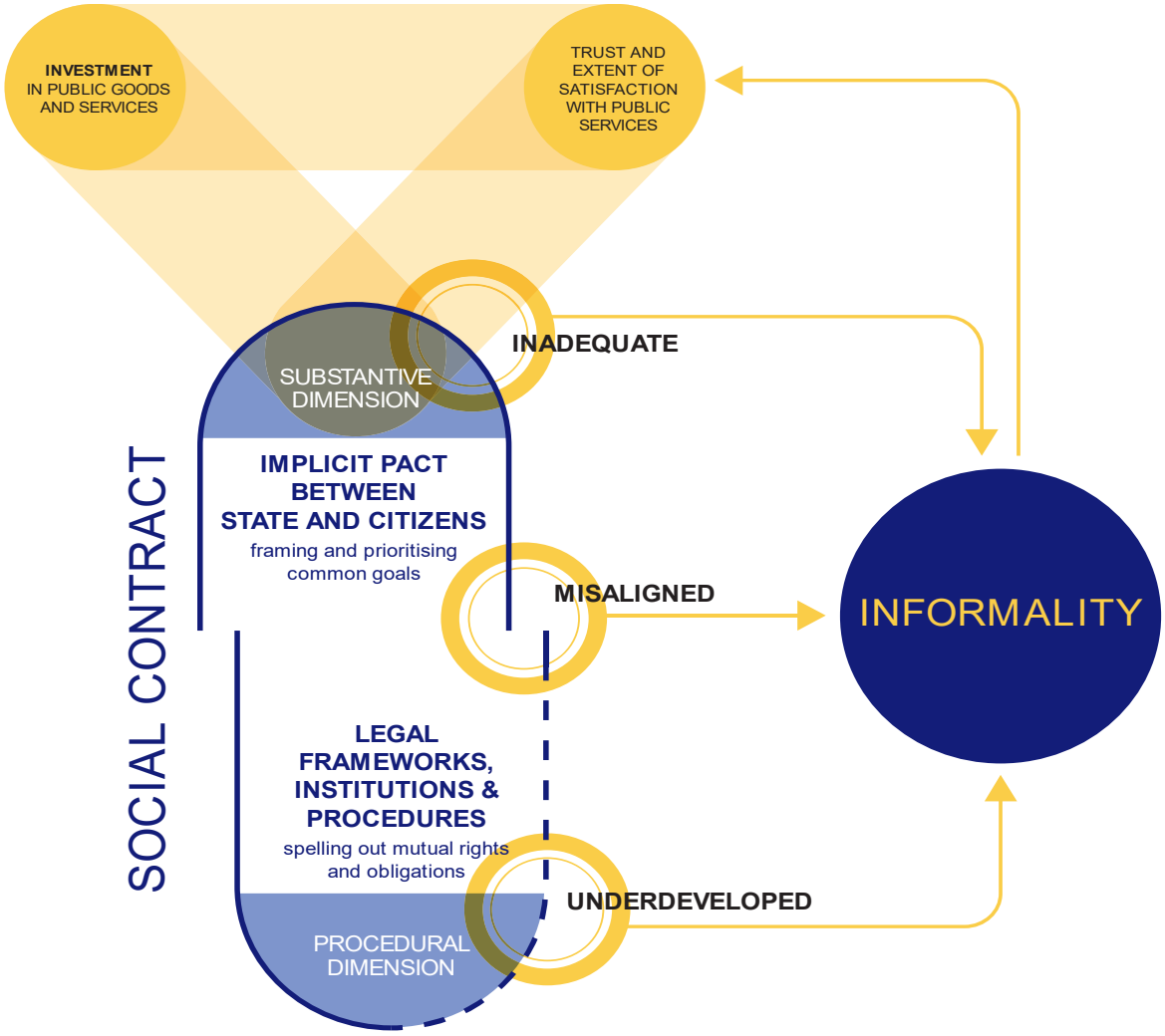
The longstanding structural deficit of low- and middle-income countries in formal job creation, which was worsened by the COVID-19 crisis, as well as the non-inexistent or inadequate protection available to informal workers, remain major sources of vulnerability for those workers and their families. The informal economy is highly heterogeneous (OECD/ILO, 2019[12]). In many settings, it represents a consequence of low level of development, the inability of the economy to create formal quality jobs, and the inability of institutions to deliver and improve people's lives. In some instances, it can also incorporate elements that distort competition between enterprises and hamper governments' revenues. Any sustainable development strategy must therefore have formalising the economy and reducing the vulnerability of informal workers at its heart.

Understanding the nature of the social contract, and its links with informality

Informality, its determinants and manifestations, are diverse, complex and context specific, but ultimately informality happens within a given social contract in any society. Social contracts represent an implicit agreement between various actors – citizens, state, workers, enterprises – on how to distribute power and resources in order to achieve common goals such as equity, fairness, freedom, security, and eventually social justice. Social contracts have substantive and procedural dimensions.

The substantive dimension pertains to the manner in which common goals are framed and prioritised in a society. The procedural dimension pertains to legal frameworks, institutions and procedures that help to make this implicit pact explicit. The question of formality arises only in relation to existing laws and regulations, as well as their implementation in practice. As such, informality can reflect either the underdeveloped procedural dimension of the social contract (when workers and enterprises are not covered by formal legal frameworks or are insufficiently covered), a weak substantive dimension (when states do not deliver sufficient good quality public services, while trust and satisfaction with public services are low), a misalignment between the substantive and the procedural dimensions, or all of these situations at once (Figure 1.5).

Figure 1.5. Schematic representation of the linkages between the social contract and informality

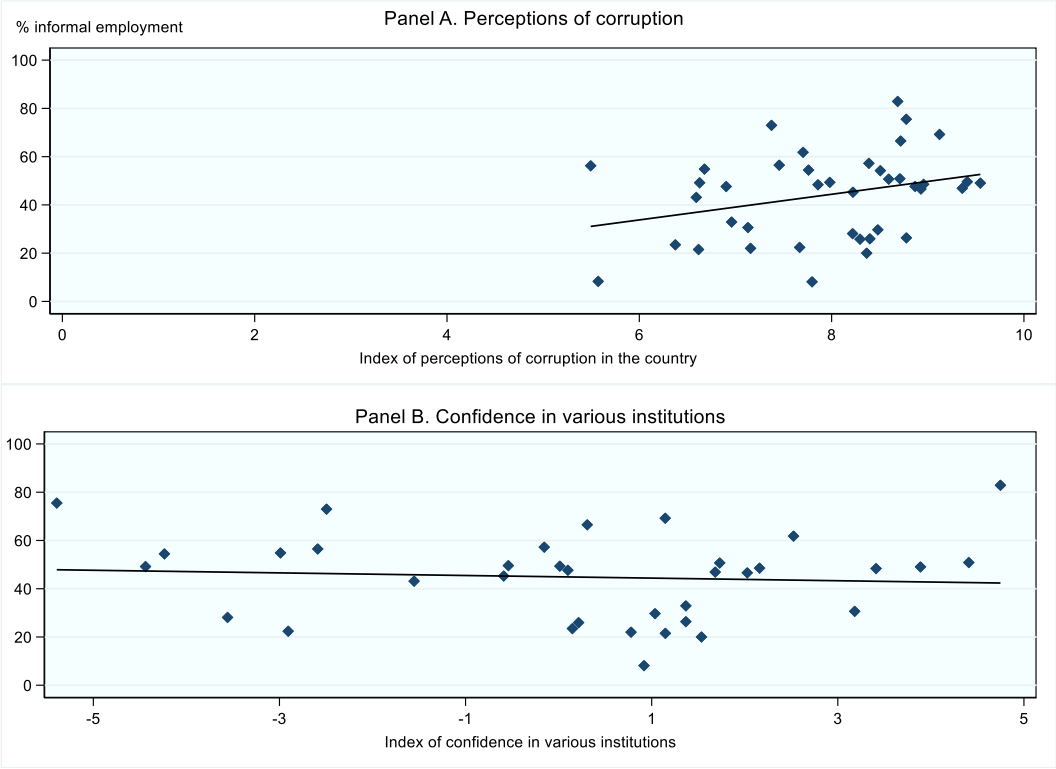


Source: Authors' elaboration.

In some settings, informality may be a symptom of a weak substantive dimension of the social contract

The substantive dimension of the social contract is strong when the majority of citizens perceive that the pact with the state is reliable, beneficial for them, and fair (Shafik, 2021[13]). A strong social contract between the state and its citizens is an essential condition for sustaining development over time (OECD, 2011[14]; Bussolo et al., 2018[15]). Conversely, the social contract is weak when most citizens see it as non-reliable, non-beneficial or unfair. The latter perception manifests in low levels of trust and confidence in public institutions. Another key aspect of a strong social contract is the expectation that taxes and social security contributions are not misused. In other words, misuse of public funds and corruption weakens social contracts. In countries where the substantive dimension is weak, as manifested by a high level of corruption, mistrust in public institutions (Figure 1.6), or dissatisfaction with various public services, informality also tends to be ubiquitous.

Figure 1.6. Informality correlates positively with perceptions of corruption and negatively with confidence in institutions



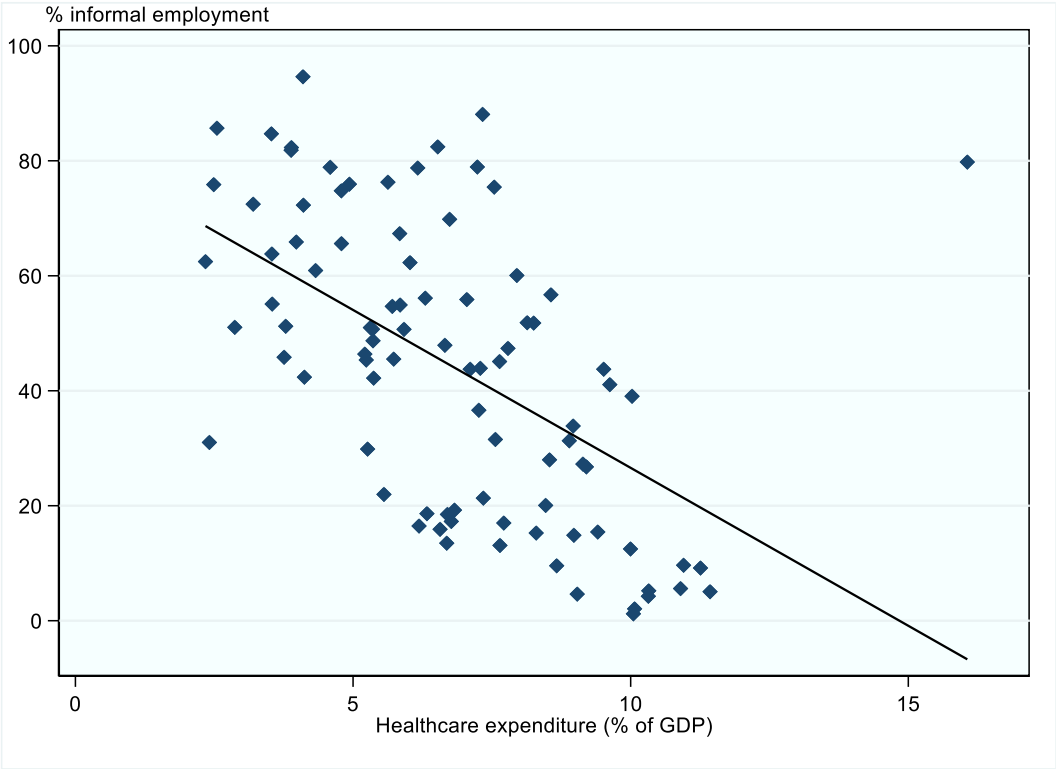
Note: Predicted values of informal employment (International Labour Organization (ILO) definition). Controls include seven geographic regions (East Asia and Pacific; Europe and Central Asia; Latin America and the Caribbean (LAC); Middle East and North Africa (MENA); North America; South Asia; sub-Saharan Africa); gross domestic product (GDP) per capita, purchasing power parity (PPP) constant 2017; income share held by the lowest-income 10% of the population; population growth; trade as a percentage of GDP; the Human Development Index (HDI); ease of doing business as of 2018; and political rights and civil liberties. Index of perceptions of corruption (Panel A) is computed as an average of individual responses to the question: "How much corruption is there in your country?" Answers ranged from 1 to 10, with 1 meaning "There is no corruption in my country" and 10 meaning "There is abundant corruption in my country". Then, averages were taken by country within a subsample of all workers. Index of the confidence in institutions (Panel B) is first computed on an individual level using the principal component analysis (PCA) procedure, and extracting the first principal component. The PCA is applied to nine questions, asking about the degree of confidence the person has in: armed forces, the press, the labour unions, the police, the justice system, the government, political parties, parliament, and the civil service. The answers are measured on a scale of 1 to 4, where 1 refers to "no confidence at all", and 4 refers to "full confidence". Then, averages were taken by country within a subsample of all workers. Informal employment: latest available data. See the annex of Chapter 3 for the full list of countries.

Source: Authors' computations based on the following data: informal employment: (ILO, 2023[1]), *Women and Men in the Informal Economy: A Statistical Update;* geographic regions, GDP per capita, population growth, and trade as a percentage of GDP: (World Bank, 2021[16]), World Development Indicators (database), www.data.worldbank.org/products/wdi; ease of doing business: (World Bank, 2022[17]), Doing Business Indicators (database), www.doingbusiness.org; political rights and civil liberties indices: (Freedom House, 2019[18]), Freedom in the World (database), freedomhouse.org/report/freedom-world; perception of corruption and confidence in institutions: own computations based on (World Values Survey, 2020[19]), Wave 7 (database), worldvaluessurvey.org.

If one of the main components of the social contract is the agreement that citizens comply with laws (including labour and social security laws), pay taxes and make social security contributions, another no less important component is that, in exchange for this, citizens receive good-quality public goods and services, such as education and healthcare. Access to good-quality public goods and services is also one of the key components of redistribution and of promoting equality of opportunity.

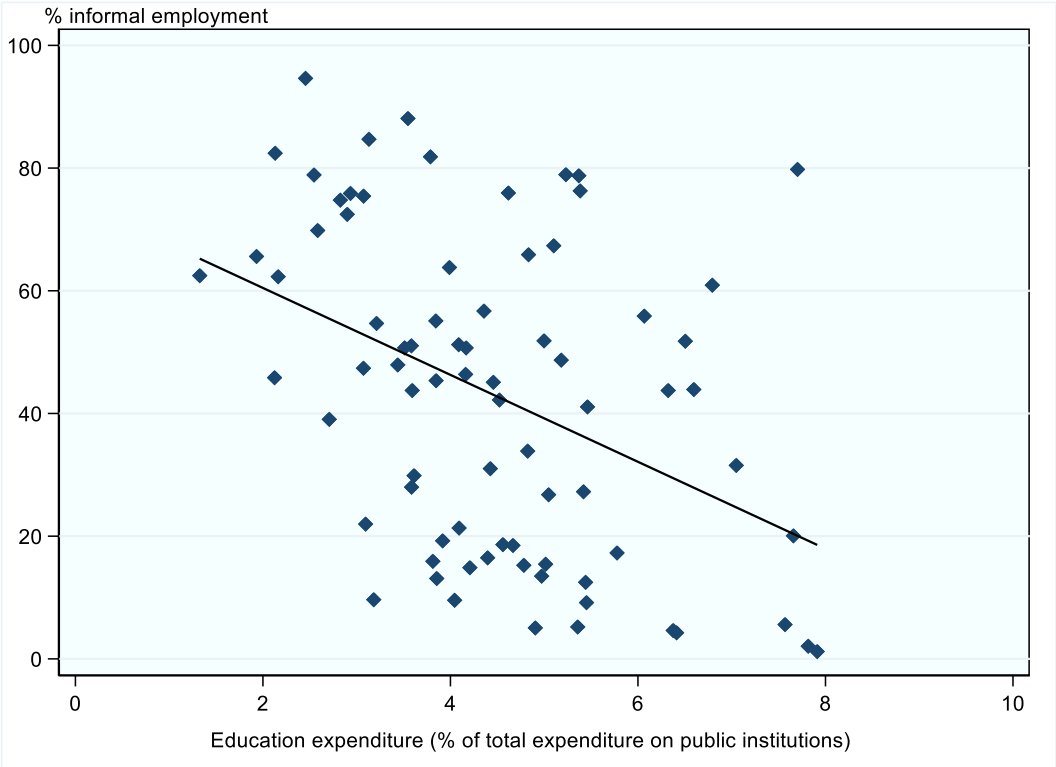
The level of public spending on public goods and services, such as healthcare (Figure 1.7) or education (Figure 1.8) negatively correlates with informality. This translates into poorer social outcomes (Figure 1.9), reinforcing the vulnerability of informal workers and their family members, especially during crises.

Figure 1.7. Informality negatively correlates with higher healthcare expenditure



Note: Predicted rather than actual values of informality are reported. They are obtained from multivariate analysis controlling for seven geographic regions (East Asia and Pacific; Europe and Central Asia; LAC; MENA; North America; South Asia; sub-Saharan Africa); GDP per capita (2017 PPP); life expectancy; population growth; age dependency ratio; 2018 ease of doing business; and trade. Informal employment: latest available data. See the annex of Chapter 3 for the full list of countries.
Source: Authors' computations based on the following data: informal employment: (ILO, 2023[1]), *Women and Men in the Informal Economy: A Statistical Update*; GDP per capita (2017 PPP), life expectancy, population growth, age dependency ratio, trade, and healthcare expenditure: (World Bank, 2021[16]), World Development Indicators (database), www.data.worldbank.org/products/wdi; ease of doing business: (World Bank, 2022[17]), Doing Business Indicators (database), www.doingbusiness.org.

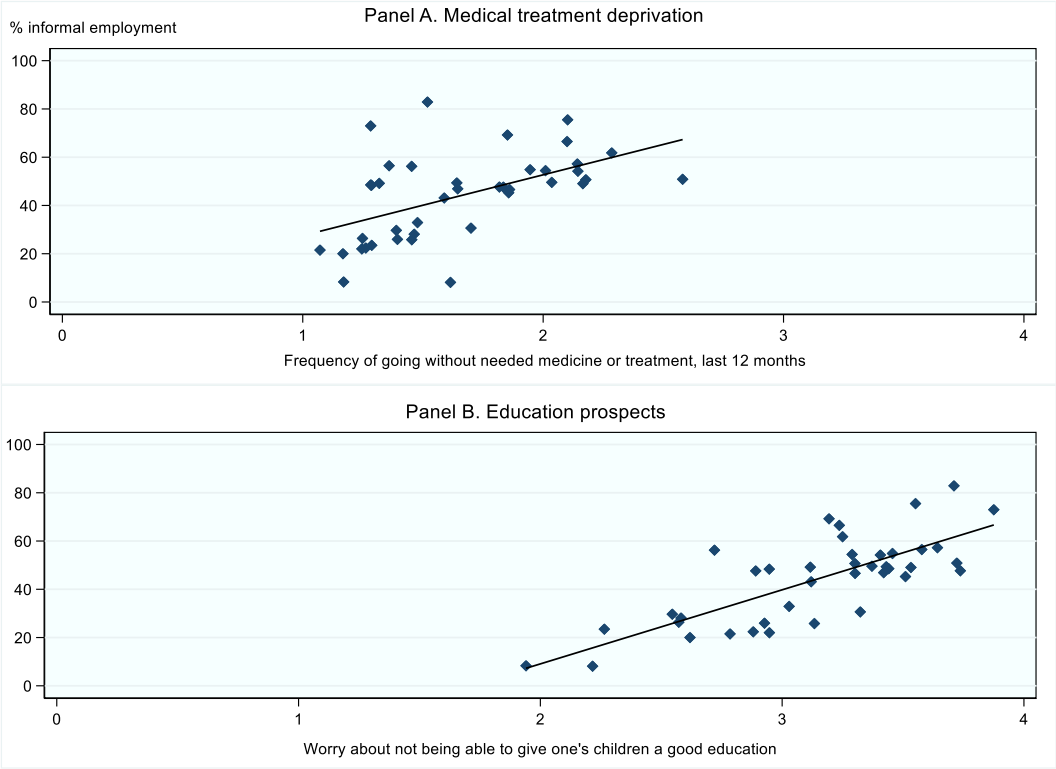
Figure 1.8. Informality negatively correlates with higher education expenditure



Note: Predicted rather than actual values of informality are reported. They are obtained from multivariate analysis controlling for seven geographic regions (East Asia and Pacific; Europe and Central Asia; LAC; MENA; North America; South Asia; sub-Saharan Africa); GDP per capita (2017 PPP); life expectancy; population growth; age dependency ratio; 2018 ease of doing business; and trade. Informal employment: latest available data. See the annex of Chapter 3 for the full list of countries.

Source: Authors' computations based on the following data: informal employment: (ILO, 2023[1]) *Women and Men in the Informal Economy: A Statistical Update*; GDP per capita (2017 PPP), life expectancy, population growth, age dependency ratio, trade, and education expenditure: (World Bank, 2021[16]), World Development Indicators (database), www.data.worldbank.org/products/wdi; ease of doing business: (World Bank, 2022[17]), Doing Business Indicators (database), www.doingbusiness.org.

Figure 1.9. Informality positively correlates with adverse social outcomes, either actual or perceived



Note: Predicted values of total informal employment. Controls include seven geographic regions (East Asia and Pacific; Europe and Central Asia; LAC; MENA; North America; South Asia; sub-Saharan Africa); GDP per capita, PPP constant 2017; income share held by the lowest-income 10% of the population; population growth; trade as a percentage of GDP; the HDI; ease of doing business as of 2018; and political rights and civil liberties. In Panel A, frequency of going without necessary medicine or treatment is computed as an average of individual responses to the question: "How often you or your family have gone without needed medicine or treatment in the past 12 months", with answers measured on a scale of 1 to 4, where 1 means "never" and 4 means "often". Averages were taken by country within a subsample of all workers. In Panel B, worry about not being able to give one's children a good education is computed as an average of individual responses to the question: "To what extent do you worry about not being able to give one's children a good education", with answers measured on a scale from 1 to 4, where 1 means not at all and 4 means very much. Averages were taken by country within a subsample of all workers. See the annex of Chapter 3 for the full list of countries.

Source: Authors' computations based on the following data: informal employment: (ILO, 2023[1]), *Women and Men in the Informal Economy: A Statistical Update*; GDP per capita, PPP constant 2017; income share held by the lowest-income 10% of the population; population growth; trade as a percentage of GDP; the HDI: (World Bank, 2021[16]), World Development Indicators (database), www.data.worldbank.org/products/wdi; ease of doing business: (World Bank, 2022[17]), Doing Business Indicators (database), www.doingbusiness.org; political rights and civil liberties indices: (Freedom House, 2019[18]), Freedom in the World (database), freedomhouse.org/report/freedom-world. For frequency of going without necessary medicine or treatment, and worry about not being able to give one's children a good education: own computations based on (World Values Survey, 2020[19]), Wave 7 (database), worldvaluessurvey.org.

In other settings, informality may be the norm as part of a social contract that has only a recent or an underdeveloped procedural dimension

In some of the least developed countries, the logic for informal employment in relation to the social contract is profoundly different when these countries are compared with richer and more developed countries. In many instances, the procedural dimension of the social contract, which takes the form of legal arrangements and frameworks, is not yet developed enough to cater to all citizens or to be relevant to all of them, especially where castes or tribal traditions remain strong. It may not cover some specific sectors (such as agriculture or waste picking) or some specific workers (such as traditional farmers, fishers,

indigenous communities, or domestic workers). When legal frameworks exist, governments do not always have the capacity to enforce them. Governments may also lack the infrastructure and the capacity to deliver the benefits of adherence to the social contract (such as education and health infrastructure), or the qualified specialists to deliver the services.

In some settings, informality also persists because there is a misalignment between the procedural dimension (formal institutions) and the substantive norms of the society, as well as between institutional responses to the true needs of workers, their families, and citizens generally (Gërxhani, 2004[20]; Williams and Horodnic, 2015[21]). This misalignment may be historic, reflecting colonial legacies. It may also reflect the fact that the state is not catching up with the challenges that the ever-changing world is presenting – as is the case in countries undergoing substantial socio-economic and political transformation. This misalignment further justifies the existence of the informal economy, and legitimises informal practices in the eyes of the community, even if they are not seen as legitimate in relation to the state (Van Schendel and Abraham, 2005[22]).

Improving resilience to crises requires strengthening the social contract. This presupposes continuous efforts to render the procedural dimension of social contracts more relevant for all workers, in order to ensure that the substantive dimension is strong, inclusive and fair for informal workers, and also to ensure that the procedural dimension reflects well the substantive dimension of the social contract.

Globalisation, the social contract and informality

Social contracts differ across countries and change over time. National economic, social, and political changes present both opportunities and challenges to the strength of the social contract and ultimately affect social cohesion. In addition, international factors may also alter the substantive dimension of the social contract in a given country and render the procedural dimension inadequate to the fast-changing realities. Already prior to 2020, social contracts around the world were being challenged by a variety of internal and international factors, including demographic shifts, climate change, rising inequality, increased income insecurity, lower social mobility, economic globalisation, digitalisation and fragile or weakening social dialogue and decline in trust in institutions. In all countries, regardless of their level of development, governments should remain vigilant against the erosion of the social contract, and use it as a lens through which to address informality.

Trade liberalisation has challenged the social contract in many countries

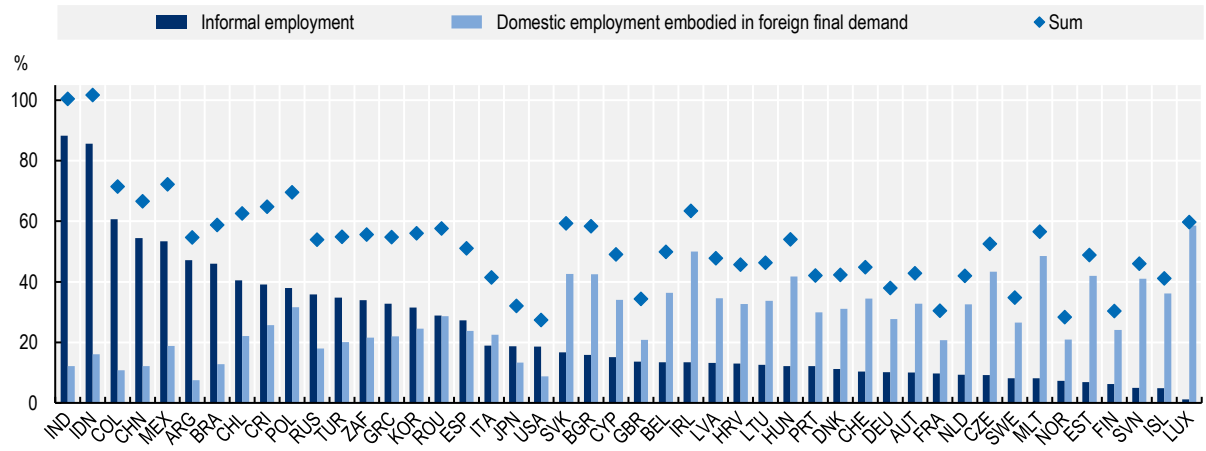
Economic globalisation can be a powerful determinant of economic growth, enhanced productivity and efficiency. However, economic globalisation can also destabilise existing equilibria of power relations between different economic actors within a given country, and with them, the existing social contract. For much of the developing world, integration into the global economy created significant challenges in terms of employment adjustment. The impact on formal job creation has often been ambiguous and is not uniform across countries. If a greater degree of globalisation has been associated with lower levels of informal employment in upper-middle-income and high-income countries, it is not the case in lower-middle-income and low-income countries.

International trade is an aspect of economic globalisation that has an asymmetrical impact on informality, so that the aggregate impact remains ambiguous. Trade liberalisation induced by the reduction of export tariffs, and hence the expansion of export opportunities, has led to a decrease in the informal employment share in the affected sectors and regions. In contrast, trade liberalisation induced by the reduction of import tariffs, and hence the expansion of imports, has tended to increase the share of informal employment in the affected sectors and regions. These effects have been pronounced in sectors, industries, and regions most affected by trade liberalisation.

GVCs can be an important source of informal employment

By 2020, up to 70% of international trade was organised through GVCs (OECD, 2020[23]). Among countries with available data, the risk of the informality footprint is highest in GVCs originating from India and Indonesia. In these countries, the sum of the percentage of informal employment and of the percentage of domestic employment embodied in foreign final demand is greater than 100%, which means that at least some of the GVC-related employment is definitely informal. The greater the sum, the higher the probability that at least some GVC-related employment is informal, which means that in some countries one cannot rule out that informal employment and GVCs are related (Figure 1.10).

Figure 1.10. Informal and GVC-related employment, by country



Note: Both informal and domestic employment embodied in foreign final demand are expressed as a share of total employment. If the sum of these indicators is greater than 100%, one can interpret these results as evidence of overlap between informal employment and trade-linked employment.

Source: Authors' computations based on the following data: informal employment: ILO (2018[3]), www.ilo.org/global/publications/books/WCMS_626831/lang--en/index.htm; domestic employment embodied in foreign final demand (%): OECD (2019[24]), Trade in employment (TiM): Principal indicators (database), https://stats.oecd.org/Index.aspx?DataSetCode=TIM_2019_MAIN.

StatLink https://stat.link/m67wer

The informality footprint of GVCs depends on how they are organised and managed

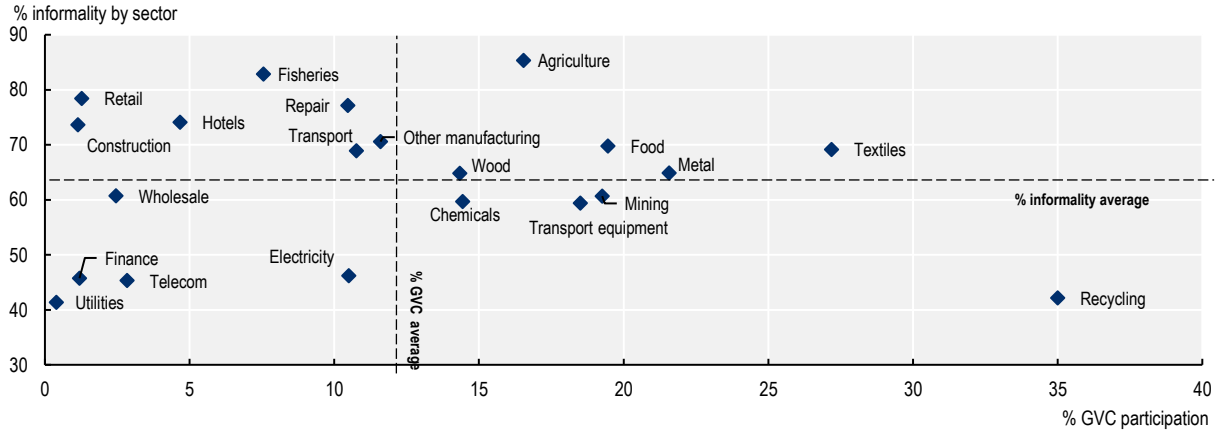
GVCs have the potential to create opportunities for both higher productivity and better quality of employment, including for women and young workers. The extent to which this is actually happening depends on many factors. First, the type of linkages matters: the expansion of forward linkages in a chain can decrease informal employment, whereas the expansion of backward linkages does not necessarily have this effect. Second, the way production is organised is also important: if the lead firms prefer outsourcing over direct ownership of overseas subsidiaries, this can increase the risk of informality in the lowest tiers of supply chains (Abramovsky and Griffith, 2006[25]; ILO, 2016[26]). Third, purchasing practices, and in particular inappropriate lobbying, poor forecasting, and excessive sampling substantially increase the risk of employing workers informally. Finally, possibilities of upgrading, and especially of process upgrading, within a GVC, can help formalisation and improve the working conditions of both formal and informal workers.

In terms of sectors, GVCs in agriculture and in garments have some of the largest informal employment footprints

The size of a GVC's informal employment footprint appears to be largely sector specific but not necessarily linked to the level of GVC participation in a given sector. Analysing the association between the level of GVC participation and the percentage of informal employment (Figure 1.11) enables us to identify four types four types of sectors: (i) sectors with higher-than-average informality and GVC participation (such as agriculture, food and beverages, textiles, wood, and metals); (ii) sectors with lower-than-average informality and GVC participation (utilities, electricity, and certain higher-added value services such as finance, telecommunications; (iii) sectors with higher-than-average informality but lower-than-average GVC participation (i.e. fishing, lower-added value service sectors such as retail, hotels, repair, construction, transportation, and other manufacturing); and (iv) sectors with lower-than-average informality but higher-than-average GVC participation (chemicals, transportation equipment, mining, and recycling).

GVCs in agriculture have some of the largest informal employment footprints due to a combination of factors such as the pervasive informality in the first segment of the chain, the production structure in agriculture; and the way GVCs are organised in agriculture (often outsourcing without direct ownership). Informal employment is also ubiquitous in some sectors of the textiles industry, such as garments, with the largest shares of informal employment found among home-based workers in the downstream tiers.

Figure 1.11. Total GVC participation and informality, by sector



Note: GVC participation is defined as exported value added which crosses at least two borders. Here, GVC participation is expressed as a percentage of value added. Country coverage: Argentina (2018), Armenia (2016), Brazil (2018), Burkina Faso (2014), Chile (2017), Colombia (2018), El Salvador (2018), Gambia (2015), Ghana (2013), Liberia (2016), Madagascar (2012), Malawi (2016), Mali (2012), Mexico (2018), Namibia (2015), Nicaragua (2014), Niger (2014), Peru (2019), Senegal (2011), Tanzania (2014), Thailand (2017), Uganda (2015), Uruguay (2018), Viet Nam (2016) and Zambia (2015).
Source: Authors' computations based on the following data: For the percentage of informal employment at the sector level: OECD (2021[27]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)*, https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm. For GVC indicators: Belotti, Borin and Mancini (2020[28]) based on Eora26 data.

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Informality and digital labour platforms: An opportunity yet to be seized

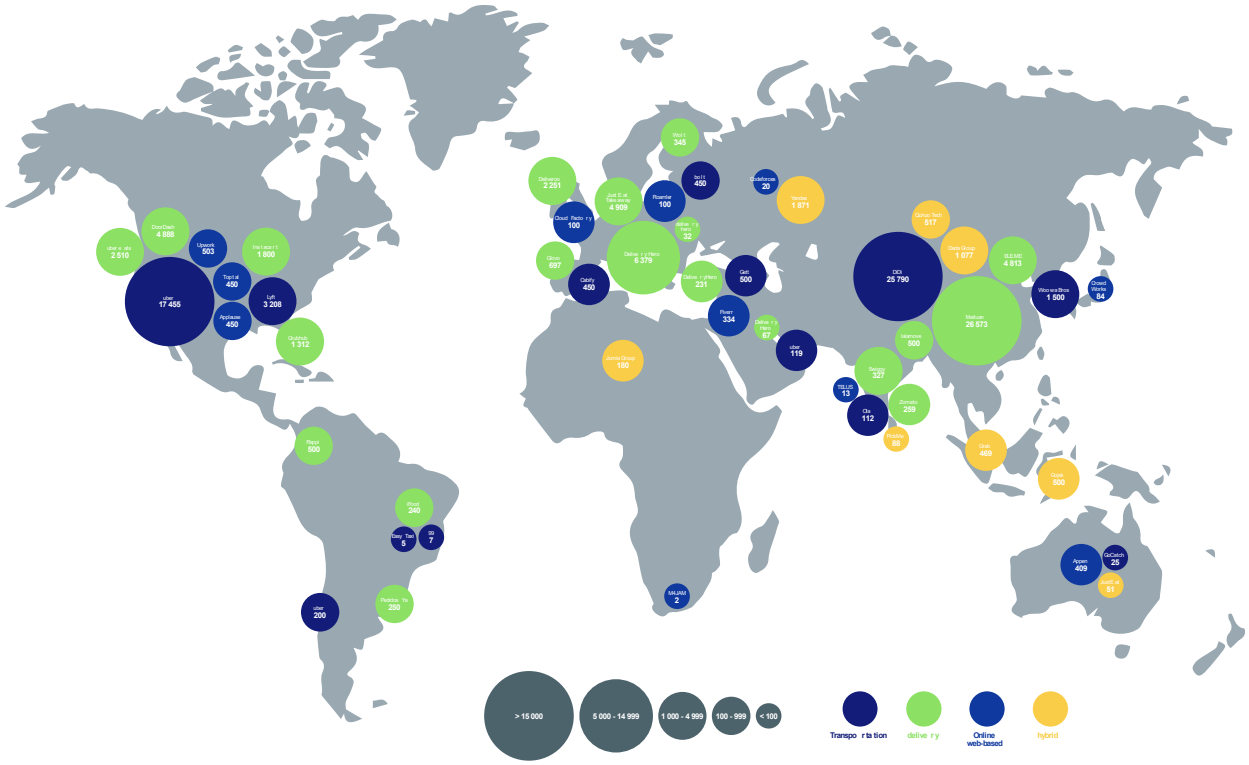
Work through digital labour platforms: A new challenge for social contracts

Digital labour platforms that mediate work provide new ways of organising production and work (OECD, 2019[29]; OECD, 2019[30]; ILO, 2021[31]). As such, they also present a challenge to employers, workers, and governments by disrupting traditional ways of doing business and altering competition, worker protection, and informal employment (ILO, 2022[32]). The typology of digital labour platforms includes (ILO, 2021[31]; ILO, 2022[32]):

- online web-based platforms for online delivery of non-material services by a workforce that is potentially scattered around the world
- location-based platforms for serving clients locally in a specific area.

Work through digital labour platforms grew since the early 2000s, penetrating all geographic regions (Figure 1.12).

Figure 1.12. Estimated annual revenue of digital labour platforms, selected categories, by region, 2021 (in USD millions)



Note: For details of construction, please refer to (ILO, 2021[31]).
Source: (ILO, 2021[31]), based on Crunchbase database; courtesy of the ILO, with authors' adaptation.

The COVID-19 crisis further popularised the use of digital labour platforms

The COVID-19 pandemic further generalised the use of digital labour platforms, although at various stages of the pandemic sizeable variations were observed by sector of economic activity and by country (OECD, 2021[33]; ILO, 2022[32]). In many sectors, digital labour platform workers had high exposure to the COVID-19 virus and also experienced work and income loss due to lockdown measures and changing consumer

behaviour (OECD, 2020[34]). Most of these workers were not covered by social protection, including health insurance, work-related injury, disability and unemployment insurance. The majority of them could not afford either to self-isolate or to take days off in the absence of paid sick leave and sickness benefits – even if they tested positive for COVID-19 (ILO, 2021[31]). This presented major risks not only to workers but also to their clients.

The share of informal employment is often higher among workers on digital labour platforms than among workers in the traditional offline economy (Aleksynska, Bastrakova and Kharchenko, 2018[35]; Berg, 2016[36]). This is because the vast majority of digital labour platform workers are classified as independent contractors, or self-employed (Berg et al., 2018[37]; ILO, 2021[31]; Schwellnus et al., 2019[38]) who often remain unregistered. Even for those self-employed workers who are registered, and hence de jure part of the formal sector, there is a risk of sliding into dependent self-employment, and even into a disguised employment relationship – a situation where the worker is misclassified as an independent, self-employed worker, even though they are, in fact, in a subordinate employment relationship (ILO, 2016[39]).

However, work channelled through digital labour platforms could also be an opportunity for formalisation (OECD, 2019[30]). Available technologies for digital work record workers' and clients' identities through digital accounts and track the transactions, allowing for monitoring of economic activity, traceability, transparency and accountability (ILO, 2022[5]), all of which are important elements for formalisation. In order for those technologies to support formalisation effectively, governments need to create more enabling environments, and digital labour platforms and public authorities must co-operate more closely.

Digital labour platforms could create opportunities for formal jobs, but this has yet to happen

Thus far, formal job creation by digital labour platforms remains limited and sector specific. On the one hand, digital labour platforms allowed to monetise tasks that previously would not have been carried out for money, and to outsource them to developing countries. This has led to an increase in demand, and consequently in supply of work, in sectors such as creative and multimedia services or software development (OECD, 2018[40]; Schwellnus et al., 2019[38]). Platforms also make it easier for parties to find each other and to match demand with supply. By doing this, they lower the transaction costs of finding labour and they minimise frictions in labour markets (McKinsey Global Institute, 2015[41]), which can increase total employment. On the other hand, the bulk of the work channelled through digital labour platforms today – whether taxi driving, domestic work, cleaning or auditing services – existed prior to the emergence of digital labour platforms, and they often co-exist today in traditional labour markets. Rather than creating new jobs, platforms use technologies to mediate work, help outsource services, and change the nature of existing jobs (ILO, 2016[39]; Schwellnus et al., 2019[38]). Digital labour platforms also allow to more easily substitute wage employment by services delivered by self-employed workers. As a result, the total new job creation effect is unclear. The newly created jobs are not always formal, and some formal wage jobs in the traditional economy are converted into informal self-employed jobs on digital labour platforms.

But it does not have to be this way. For example, for domestic workers, platforms can act as temporary agency platforms that favour formalisation. In some national legislation (for example, in China), access to social security is conditional on whether the person is employed by an enterprise. In this case, being employed by a temporary agency, including temporary agency platforms, is the only way domestic workers can access formal wage jobs. In addition, platforms themselves can play a role in helping to formalise their workers; for example, by enrolling workers into public insurance programmes. As such, platforms have the potential to serve as a bridge towards formalisation (OECD, 2019[30]).

Policy recommendations to reinvigorate social contracts

As the *social contract* approach reveals, reducing informality and the vulnerability of informal workers and their household members requires more than boosting economic growth or developing one-off policy responses. A comprehensive effort to reinvigorate social contracts is key to addressing the challenges posed by globalisation and rapid technological change, thus rendering societies more resilient to current and future crises, and supporting formalisation. It requires actions on many fronts and from a wide range of stakeholders.

The role of governments

The role of governments is paramount in ensuring that the substantive dimension of the social contract is strong, inclusive and fair for all workers, including informal workers; in rendering the procedural dimension of social contracts relevant for all workers; in improving the alignment between the substantive and the procedural dimensions; and in staying vigilant against a possible weakening of social contracts under the effect of external pressures.

1. Enhancing the procedural dimension means expanding coverage of formal legal frameworks and social protection, ensuring sufficient levels of protections, and improving compliance with formal arrangements by making legal frameworks relevant and fair to informal workers.
2. Strengthening the substantive dimension requires improving access to and quality of those public services that are most valued by all workers, including informal workers, such as healthcare, education and skill development, but also fighting corruption, strengthening trustworthiness of the judiciary system and the police, and improving how government performs its duties.
3. Strengthening the social contract in an open economy requires additional efforts to create enabling environments for the development of formal employment through a range of co-ordinated policies to support innovation, formal enterprise and formal job creation, access to credit, labour mobility, and increasing employability. To alleviate the consequences of labour reallocation, trade liberalisation policies should be accompanied by policies on vocational training for adult learners (including special provisions for women and migrant workers); lifelong learning that targets skill changes arising from globalisation; the anticipation of skill changes in a country's changing production structure; and skill recognition policies. To ensure that global competition does not scrimp labour protection, effective labour inspection and enforcement of current regulations is necessary.
4. Accompanying GVC development with the view of alleviating informality can be done with the following non-exhaustive measures:

- promoting the use of written rather than oral contracts by foreign enterprises and their local suppliers
- developing policies to regulate sub-contracting and ensure fair treatment of locally employed workers, including dependent contractors
- raising awareness among businesses about the existence of *OECD Guidelines for Multinational Enterprises* and *OECD Due Diligence Guidance for Responsible Business Conduct*, as well as OECD due diligence recommendations in specific sectors and supply chains, including minerals, agriculture, garments and footwear, extractives, and finance; and working with businesses to ensure that they see value in adhering to the principles prescribed therein. To the extent possible, integrating these frameworks into national binding regulations

5. Responding to new developments in the world of work, such as work through digital labour platforms, requires actions to reinforce both substantive and procedural dimensions of the social contract. In this context, new developments can also be seen as an opportunity to strengthen social

contracts and grasp the possibilities for formalisation. Specific tools to tackle informality and reduce the vulnerabilities of informal digital labour platform workers include (Lane, 2020[42]; ILO, 2016[39]; OECD, 2019[30]):

- bringing digital labour platform work within the scope of the existing regulations
- encouraging the formalisation of self-employment and ensuring that digital labour platforms are paying their share of taxes and social security contributions
- strengthening and enforcing regulations to correctly categorise workers as employees
- empowering workers to challenge their employment status
- modernising laws to address the digital labour platform modes of work
- leveraging technologies to formalise workers
- including digital labour platform workers in the existing social protection schemes
- supporting the universal right of all workers to bargain collectively
- encouraging platforms to exercise social responsibility.

The role of a whole range of other actors

In an open economy, in order to create social contracts that are inclusive, adequate and regarded as fair by all actors in society, it is critically important to ensure that the voices of all these actors can be heard. A robust commitment for this is required not only from governments but also from a wide range of other actors, including employers, managers in multinational enterprises, consumers, and civil society.

- Strengthening the voice and bargaining power of *informal workers and informal workers' organisations* remains one of the key determinants of making progress towards addressing informality. This is especially relevant for workers in the lower tiers of supply chains; in sectors with particularly high levels of informality; and workers channelling their work through digital labour platforms. These workers are significantly more knowledgeable about their needs than anyone else. A strong social contract is one that recognises these workers and enables them to participate in the formulation of policies that concern them, as well as into the design and oversight of enforcement mechanisms.
- *Multinational enterprises* should be encouraged to engage in improving their responsible business conduct in order to promote formal employment in subsidiaries and among suppliers. Multinationals' suppliers' compliance with international and local laws and regulations, the implementation of good practices when contracting people to carry out work outsourced from the multinationals' home countries, and having responsible business conduct embedded within business decisions, operations, and supply chains are key in this respect. The purchasing practices of some enterprises are identified as one of the factors in the potential rise of informal employment. Raising awareness of this, and taking steps to modify purchasing practices in order to improve forecasting can be a viable tool to reduce informality. The lead firms should strive to ensure that the suppliers and sub-contractors disclose the details of sub-contracting arrangements, honour existing contracts, use written contracts, and comply with national labour and social security regulations.
- *Consumer* awareness regarding working conditions at the very bottom of the value chain, as well as on digital labour platforms, can help to create the necessary momentum for changing demand, improving working conditions and increasing formalisation.
- *Civil society* can also play an important role, for example in process traceability within the GVC. If civil society has the space and opportunity to engage with multinational enterprises and local governments, and be heard, it can help with process upgrading which includes formalisation.

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2 Portraits of informality

This chapter presents the informality profile of people across countries and regions in 2019 on a global basis and for selected countries, as well as the latest trends covering the COVID-19 pandemic period. It relies on International Labour Organization (ILO) individual-based data on informal employment for 147 developing, emerging and developed economies, and the Organisation for Economic Co-operation and Development's (OECD) Key Indicators of Informality based on Individuals and their Household (KIIbIH) database, available for 43 developing and emerging economies. Both refer to the ILO's definition of informal employment. The resulting comprehensive portrait of informally employed individuals and their dependents shows distinct patterns that policy makers must take into account in order to effectively tackle the challenge of vulnerability in the informal economy.

Today, the informal economy absorbs six out of ten workers and eight out of every ten economic units in the world. Informal economy workers and economic units were the most affected by measures imposed to contain the spread of the virus during the coronavirus disease (COVID-19) crisis. This disproportionate impact on the informal economy led, in the second quarter of 2020, to a one-off "formalisation" of the labour market in many countries, which was in fact associated with the destruction of informal jobs rather than with their formalisation. Today, challenges faced by informal workers before the COVID-19 pandemic-induced crisis remain, but the COVID-19 crisis and the spectrum of overlapping crises and potential future shocks have given a new sense of urgency to the formalisation agenda, given the benefits that formality can bring to workers, sustainable enterprises and societies.

Informality is a widespread, multidimensional and persistent phenomenon

Informality is a widespread, multidimensional and persistent phenomenon. It also has multiple (interrelated) dimensions with regard to jobs, enterprises, and its contribution to the economy. Contrary to expectations however, it has not disappeared over time, or significantly diminished with economic growth alone.[1] In 2019, prior to the COVID-19 pandemic, nearly 2 billion people were working in the informal economy, representing 58% of the world's employed population and 50% of the world's employed population excluding those working in agriculture (ILO, 1993[1]; ILO, 2003[2]; ILO, 2023[3]).[2] Globally, more than 80% of enterprises operate in the informal economy and it is estimated that informal gross domestic product (GDP) fluctuates between 15% and 35% of total GDP, depending on the region (Deléchat and Medina, 2021[4]; World Bank Group, 2021[5]).

The COVID-19 crisis has merely heightened the relevance of informality, as many countries are still reeling from its economic and social effects. Supply shocks, induced by disruptions to supply chains, ongoing geopolitical tensions, and more frequent natural disasters, have contributed to rising inflation and uncertainty globally. Workers in the informal economy, those at the lower end of income distribution, in insecure forms of work have been among the hardest hit due to the volatility of their employment and labour incomes and their lack of, or inadequate, access to social protection.

This chapter focuses on the informality of jobs. It discusses how the structural factors that define a country's labour market, such as the composition of employment, influence both the level and profile of informality in each country, at the national level. It then focuses on the characteristics of individual jobs that are highly correlated with informality, such as a non-standard employment. It also considers characteristics of individuals, such as age and gender, that can further increase the likelihood of informal employment. Finally, it considers the impact of the COVID-19 crisis, where data permit, across all of these dimensions and it sets the scene for emerging challenges discussed in subsequent chapters.

In particular, while traditional forms of informal jobs persist, changes in the organisation of work and production, such as the development of the platform economy (Chapter 5), "fissuring" and the creation of increasingly elaborate (and often cross-border) supply chains (Chapter 4); increases in non-standard forms of employment, such as on-call and casual work, result in growing forms of employment associated with a high risk of informality.

Box 2.1. Differentiating between the informal economy and informal employment

The informal economy refers to all economic activities, excluding illicit activities, by workers and economic units that are, in law or in practice, not covered or insufficiently covered by formal arrangements (ILO, 2015[6]).

The definition of informal employment used in the report differentiates between three groups of workers: (i) employees, (ii) employers and own-account workers, and (iii) contributing family members.

i) Employees are considered to have informal jobs if their employment relationship is, in law or in practice, not subject to national labour legislation, income taxation, social protection or entitlement to certain employment benefits (advance notice of dismissal, severance pay, paid annual or sick leave, etc.). In statistical terms, employees are considered informally employed if their employer does not contribute to social security on their behalf or, in the case of a missing answer, if they do not benefit from paid annual leave or sick leave.

ii) Employers (with hired workers) and own-account workers (without hired workers) are considered informally employed if they run an economic unit in the informal sector (a non-incorporated private enterprise without a formal bookkeeping system or not registered with relevant national authorities). In the case of the question not asked or a missing answer, the enterprise is considered part of the informal sector if there is no fixed place of work or it employs five employees or fewer. This threshold can vary, depending on the reporting structure of country questionnaires.

iii) Contributing family workers are informally employed by definition, regardless of whether they work in formal or informal sector enterprises.

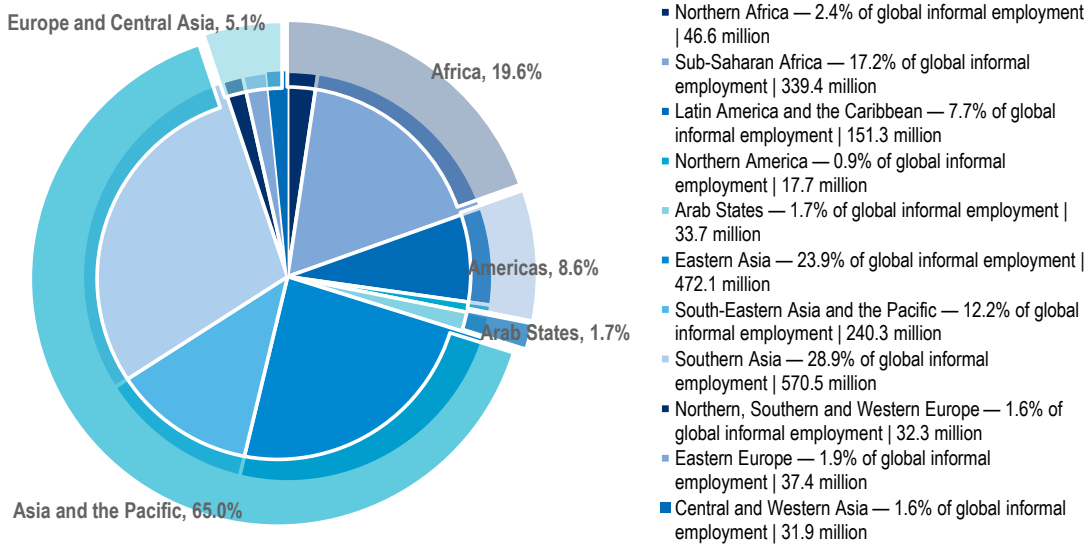
Estimates of informal employment presented in this report follow the Resolution concerning statistics of employment in the informal sector (ILO, 1993[1]) and the Guidelines concerning a statistical definition of informal employment (ILO, 2003[2]). Some adjustments to the definition of informal employment are currently being discussed for adoption during the next International Conference of Labour Statisticians (ICLS) in 2023. The revised definition will take into account the introduction of the broad concept of work and the more restricted definition of employment in the 19th ICLS resolution (ILO, 2013[7]). In addition, it will consider the different categories of status in employment, as defined by the International Classification of Status in Employment (ICSE-18) (ILO, 2018[8]) such as the new category: dependent contractors.

Informality is strongly linked to the degree of economic and institutional development

The informal economy is strongly linked to the degree of economic and institutional development as well as the structure of the economy and the labour market. As a result, while the informal economy exists everywhere, it is more prevalent in low-income countries where it constitutes 89.0% of total employment, compared to 81.6% in lower-middle-income countries, 49.7% in upper-middle-income countries and 15.9% in high-income countries. From the perspective of many who work in the informal economy, informality is first and foremost a means to survive – often the only solution to earn a living. Within this context, the vast majority (65.0%) of workers in informal employment live and work in Asia and Pacific, largely on account of the People's Republic of China (hereafter: China) and India (Figure 2.1). One in five informal workers work in Africa; it is followed by the Americas (8.6%, including 7.7% in Latin America and the Caribbean), Europe and Central Asia (5.1%) and the Arab States (1.7%). Sub-Saharan Africa, Southern Asia and

South-Eastern Asia and Pacific are the three sub-regions in which informal workers are over-represented when figures are compared to the distribution of global employment.

Figure 2.1. Distribution of global informal employment by sub-region, 2019



Source: (ILO, 2023[3]).

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The percentage of informal employment is highest in Africa, but with significant differences between countries in the region. While about 84.3% of workers in Africa rely on the informal economy (Figure 2.2), the share of informal employment across countries in the region ranges from 15.1% in Seychelles to more than 90% in two out of five African countries for which data are available. Southern Africa has a lower level of informality (44.0%) due to a combination of relatively higher levels of socio-economic development, higher proportions of wage employment in total employment, lower employment-to-population ratios, and above-average shares of social protection expenditure as a percentage of gross domestic product (GDP) (ILO, 2021[9]).

In Asia and Pacific where 65.9% of workers are in informal employment, similar variations emerge within the region. The rate of informal employment ranges from less than 20% in developed countries in the region, such as Australia or Japan, to close to 90% or more in Cambodia, India, Lao People's Democratic Republic and Bangladesh. The Arab States have the third-highest level of informal employment (54%), followed by the Americas (9.8% in Northern America and 53.6% in Latin America and the Caribbean). In the Americas, there is also significant variation across the region, ranging from 24.5% in Uruguay to between 30% and 40% in Costa Rica and Chile, close to 80% in Guatemala and above 80.0% in the Plurinational State of Bolivia, Honduras and Nicaragua. In Europe and Central Asia, informal employment constitutes about 19.7% of total employment: 13.5% in high-income countries and 27.8% in middle-income countries. In Albania, Armenia, Kyrgyzstan and Tajikistan, at least one-half of workers hold informal jobs.

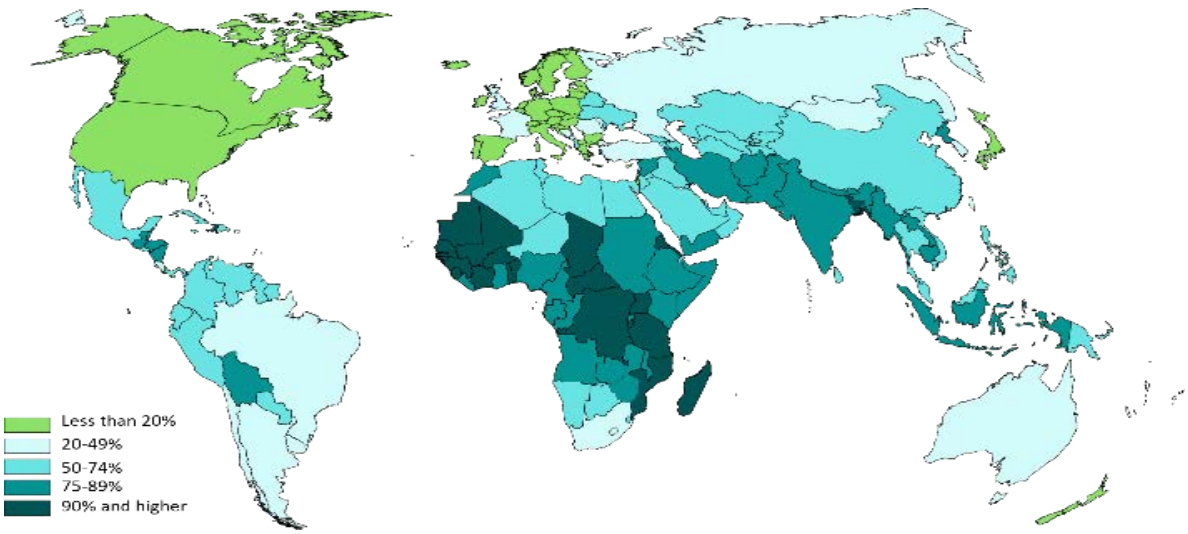
Since 2005, among countries for which data are available and recognising the possible bias associated with this subgroup, the majority show a decline in informal employment, as a share of total employment (Figure 2.3).

Several countries in Latin America, Europe and Asia are representative of this trend, often as a result of a combination of institutional policies and changes in economic structure (Chacaltana and Leung, 2020[10]). In contrast, informality and notably, informal employment, has remained at consistently high levels in a number of countries (Figure 2.3, Panel A) and is even increasing in others (Figure 2.3, Panel B).

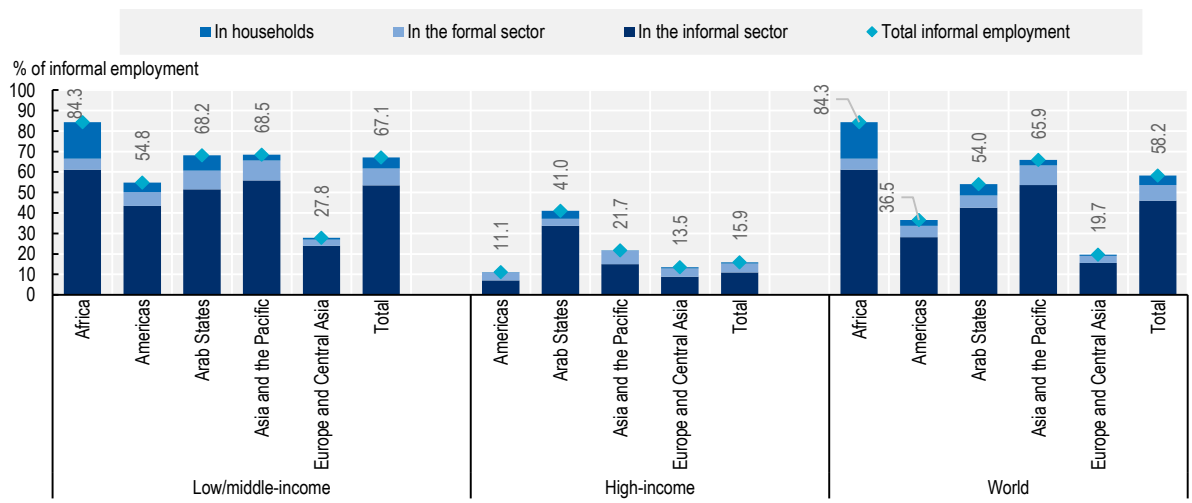
Figure 2.2. Informal employment dominates in the Global South

Share of informal employment in total employment including agriculture (2019)

Panel A. Country data



Panel B. Global estimates



Note: A common set of operational criteria is systematically used to identify workers in informal employment and those employed in the informal sector. Own-account workers and employers are in informal employment if they run informal sector economic units (non-incorporated private enterprises without formal bookkeeping systems or not registered with relevant national authorities). Employees are in informal employment if their employer does not contribute to social security on their behalf or, in the case of missing answer to the question in the household survey that the employer does not contribute, if they do not benefit from paid annual leave and paid sick leave. Contributing family workers are in informal employment by definition (ILO, 2003[2]; ILO, 2018[11]).
Source: (ILO, 2023[3]).

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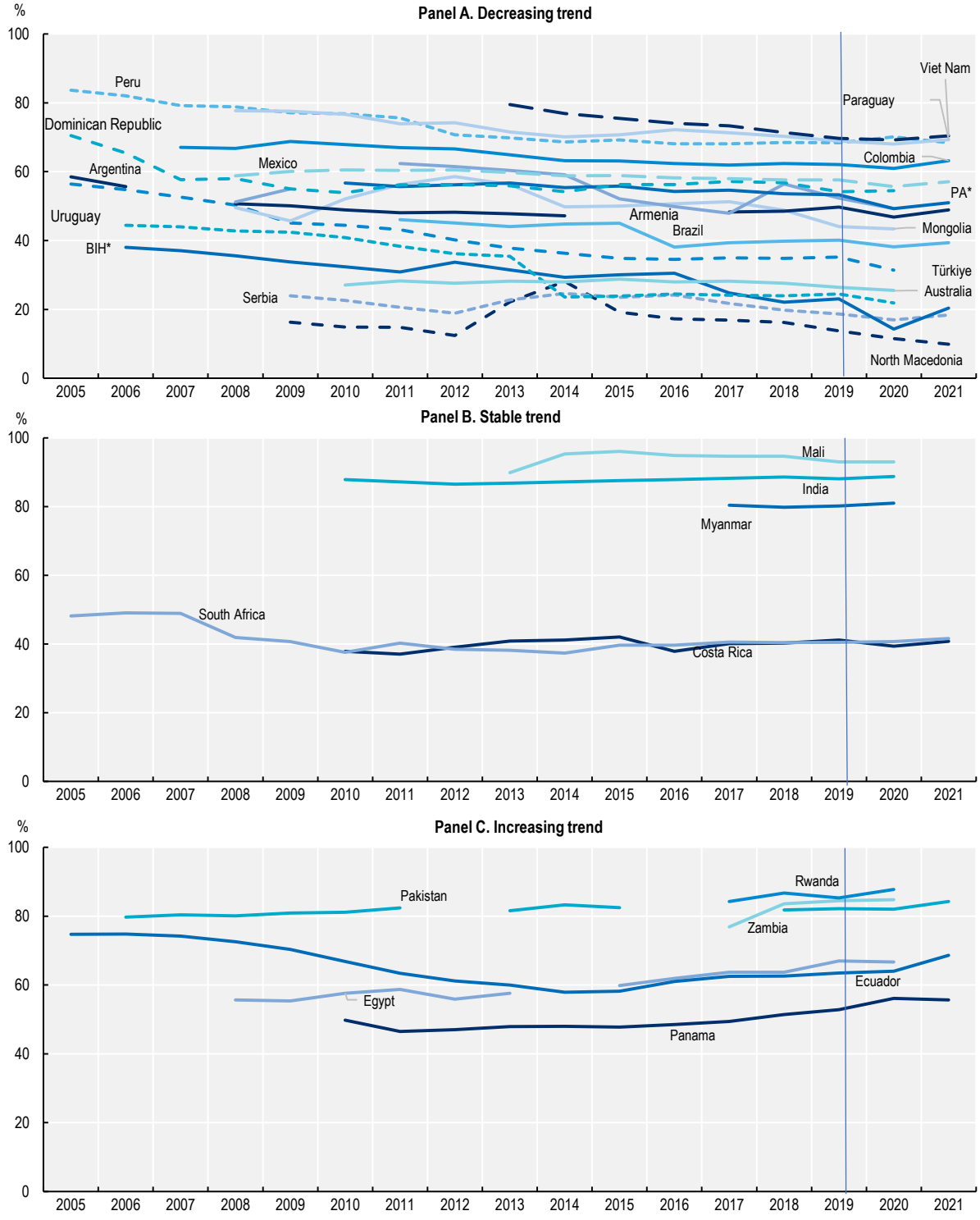
The COVID-19 crisis dramatically changed the traditional role played by the informal economy during crises. In the early stages of the pandemic-induced crisis, in countries with large informal economies, informal employment did not play its traditional countercyclical role of absorbing displaced workers from the formal economy. In many such countries, informal workers were more likely than formal workers to lose their jobs or be forced into inactivity for several reasons: widespread informality pervaded in sectors heavily affected by lockdown and containment measures; the possibility of telework was limited; the relative ease of terminating informal employment relationships; and a higher incidence of informal workers in smaller enterprises, which struggled to survive longer periods of inactivity and had less (or no) access to support measures, including worker retention schemes (ILO, 2020[12]; ILO, 2020[13]; ILO, 2022[14]).

According to the available data, the number of informal jobs dropped by 20% at the height of the crisis, about twice the rate of that for workers in formal employment (Figure 2.4) (ILO, 2020[13]). The decline of informal employment, as a share of total employment, led, in the second quarter of 2020, to a one-off formalisation of the labour market in many countries associated with the destruction of informal jobs rather than their formalisation. After the initial losses, informal employment recovered faster than formal employment, especially towards the end of 2021. By the last quarter of 2021, the recovery in informal employment had overtaken that of formal employment.

Three transitions underpinned the growth of informal employment in 2021. First, many informal workers returned to their economic activities. Second, new entrants, previously outside the labour force, entered informal employment, often as casual workers, own-account workers or unpaid family workers, to offset losses in household income. Third, it is possible that some previously formal jobs became informal. In the absence of formal employment opportunities, formal wage earners or formal business owners sought any opportunity to earn income, including in the informal economy. A complete understanding of this trend remains underway, but evidence of its importance has already emerged in some sectors such as construction, the wholesale and retail trade and food and accommodation activities (ILO, 2020[12]). High and persistent levels of uncertainty have not been conducive to investment or sustainable hiring in the formal economy. This lack of sufficient formal job opportunities presents a serious challenge for any hope of an inclusive recovery from the COVID-19 crisis.

Figure 2.3. Trends in informality in selected countries

Share of informal employment in total employment, including agriculture



Note: See note under Figure 2.2, Panel A. *PA: Palestinian Authority. *BIH: Bosnia and Herzegovina.
Source: (ILO, 2023[3]).

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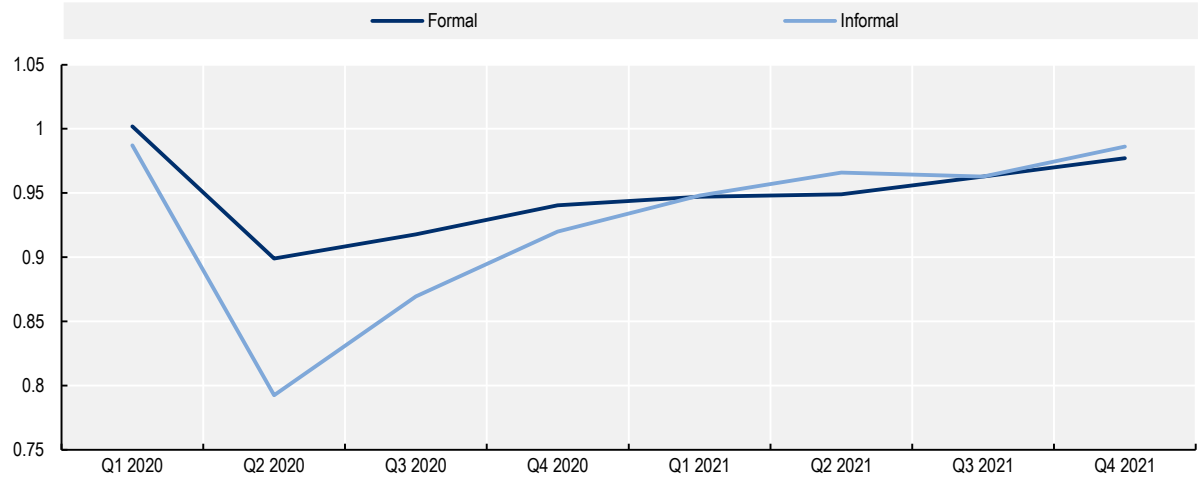
Figure 2.4. Evolution of informal and formal employment (adjusted for population aged 15-64)

Reference quarters in 2019 = 1



Note: Estimates based on trends in the number of formal and informal jobs in Argentina, Bolivia (Plurinational State of), Brazil, Chile, Costa Rica, Dominican Republic, Ecuador, Guyana, North Macedonia, Mexico, Palestinian Authority, Peru, Paraguay, Saint Lucia, South Africa, Uruguay and Viet Nam. See individual country results in (ILO, 2020[12]). *A review of country data. Impact of the Covid-19 pandemic on informality: Has informal employment increased or decreased?* Missing observations are imputed using time-fixed effects in a panel regression of countries without missing observations.
Source: Author's computations.

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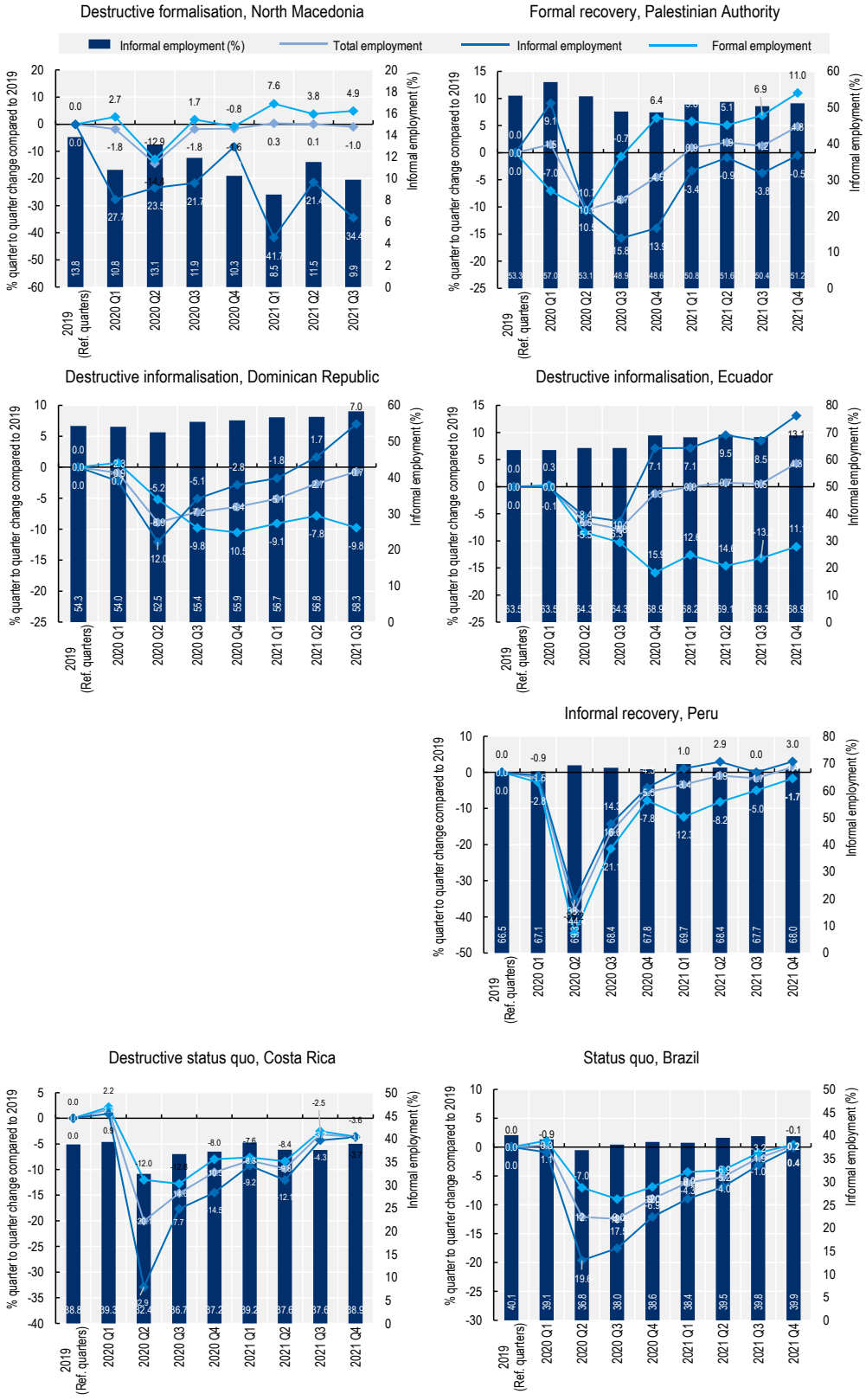
Looking at the countries for which data are available for the period 2020-21, it is still too early to observe a clear trend towards formalisation or informalisation of the labour market (represented by an overall decrease or increase in the share of informal employment) and even less of informalisation of former formal jobs (indicated by the transition of formal jobs to informal jobs, as analysed from panel data). Nevertheless, based on the number of formal and informal jobs in 2021, relative to their levels in 2019, three types of countries emerge.

In one set of countries the labour market formalised. Formalisation occurred through different pathways. In one subset of countries (for example, North Macedonia, Uruguay, and Viet Nam), formalisation occurred through a decline in total employment, with the significant decrease in informal jobs not fully compensated by the recovery in formal jobs (destructive formalisation) (Figure 2.5). By contrast, in Chile and the Palestinian Authority, the labour market formalised as total employment exceeded 2019 levels. In these countries, formalisation occurred as informal job losses were offset by growth in formal jobs (formal recovery).

In another group of countries, the labour market informalised. Total employment nearly recovered to 2019 levels in the Dominican Republic and exceeded the 2019 level in Ecuador and Peru. In all three countries, informalisation occurred as informal employment growth exceeded formal employment growth (informal recovery). However, in the Dominican Republic and Ecuador, by 2021, the number of informal jobs had grown to exceed informal employment levels in 2019. Meanwhile, formal jobs remained well below 2019 levels, with no indication of any sign of recovery (destructive informalisation). By contrast, in Peru,[3] by the end of 2021, while the number of informal jobs was slightly higher than in 2019, formal employment was both close to previous levels and growing (informal recovery).

In a third group of countries, the share of informal employment in total employment in 2021 remained the same as in 2019. In Costa Rica, while total employment declined, losses in formal and informal jobs were similar (destructive status quo). By contrast, in Argentina, Brazil, Mexico and Paraguay, total employment recovered to 2019 levels, with a concomitant recovery in both informal and formal jobs (status quo).

Figure 2.5. Formalisation or informalisation of the labour market during the COVID-19 crisis in selected countries



Note: Countries in which overall employment growth is negative are shown on the left-hand side of each panel. Countries in which overall employment growth is positive are shown on the right-hand side of each panel.
Source: (ILO, 2020[12]).

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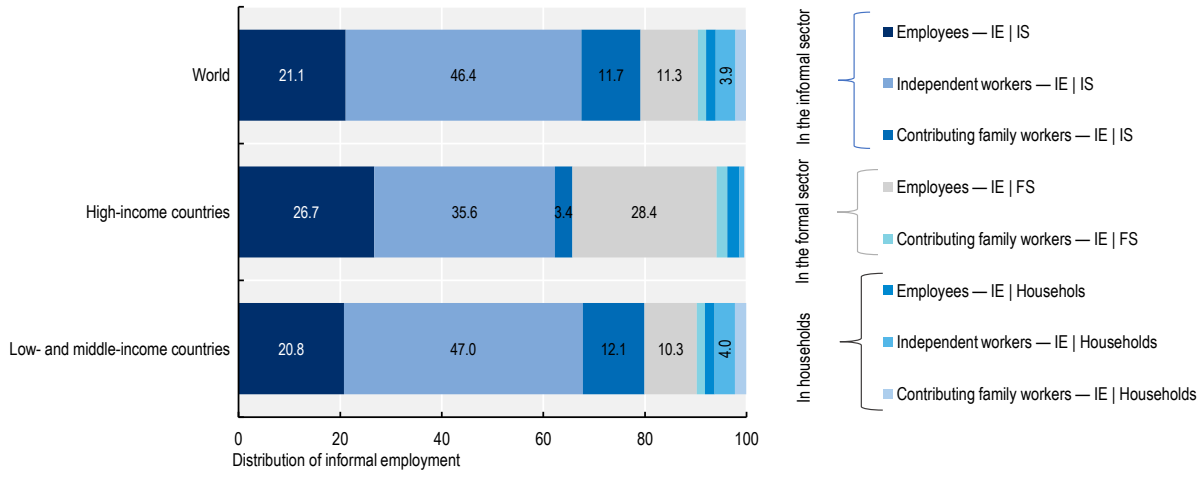
Informality encompasses a variety of forms across and within economies

From street vendors to undeclared workers in formal enterprises, from small farmers to wage employees in informal enterprises, from home-based workers to casual workers, the employment characteristics of informal workers are very diverse. Concomitant with this diversity of workers is the assortment of businesses they operate, as well as the households and enterprises in which they work (Figure 2.6). In particular, while in 2019, the majority (79.2%) of informal workers were employed in the informal sector, informal enterprises vary regarding their size, degree of coverage and compliance with laws, and level of productivity, among other factors. Understanding this diversity of workers, in combination with that of their employers and/or the businesses they operate, and identifying the prevalent forms of informality, are key to achieving formalisation with the appropriate mix of policy responses (ILO, 2021[15]).

Policies and interventions that support the formalisation of enterprises are indispensable to ensuring both independent workers' and employees', employed in the informal sector, access to formal jobs. Strategies to support the formalisation of enterprises include: measures to support their legal recognition as an economic entity, measures to enhance compliance with obligations, and measures to set the conditions for sustainable formalisation, including, importantly, measures to address low productivity (ILO, 2021[16]). Such measures represent the main pathway to formal jobs for independent workers owning or operating their own informal economic unit (46.4%). Policies aimed at formalising enterprises are also a necessary condition for the formalisation of jobs of employees employed in the informal sector (21.1%) (i.e. their access to adequate labour and social protection). The formalisation of enterprises also concerns contributing family workers (11.7%), as a means to improve their working conditions (rather than access formal employment).

Figure 2.6. Prevalent forms of informal jobs depending on income group of countries

Composition of informal employment by status in employment and type of unit of production



Note: IE | IS= Informal Employment (IE) in the Informal Sector (IS); IE | FS = Informal Employment in the Formal Sector (FS); IE | Households: Informal Employment in Households.
Source: (ILO, 2023[3]).

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Informality also includes informal employees who work in formal enterprises (11.3%, including many undeclared workers) and in households (1.3%, domestic workers). The proportion of informal jobs in formal enterprises is nearly three times higher in high-income countries (28.4%) than in low- and middle-income countries (10.3%). For all informal employees, in the formal and informal sectors or in households, formalisation involves: the extension of legal coverage by labour and social protection laws to those excluded or insufficiently covered; the provision of an adequate level of legal protection (levels of benefits, eligibility conditions and modalities to comply); and effective compliance with laws and regulations (ILO, 2021[15]).

Structural factors in the labour market influence the extent and characteristics of informality

The incidence of informality, as well as the characteristics of informality in a country, are partially determined by the level of development and structural factors that define a country's labour market. Structural factors refer to the composition of employment, at the national level or for specific groups, and encompass: the prevalence of vulnerable employment statuses, the dominance of specific sectors, and the composition of enterprise sizes that are most at risk of informality. In addition however, a number of individual job characteristics, such as employment status, full-time or part-time employment, or a permanent or temporary employment contract, also influence the likelihood that a job will be informal. For this reason, in order to address informality effectively, the incidence of informality should be considered in conjunction with other dimensions of employment. This section provides an overview of how informality intersects with some of these dimensions.

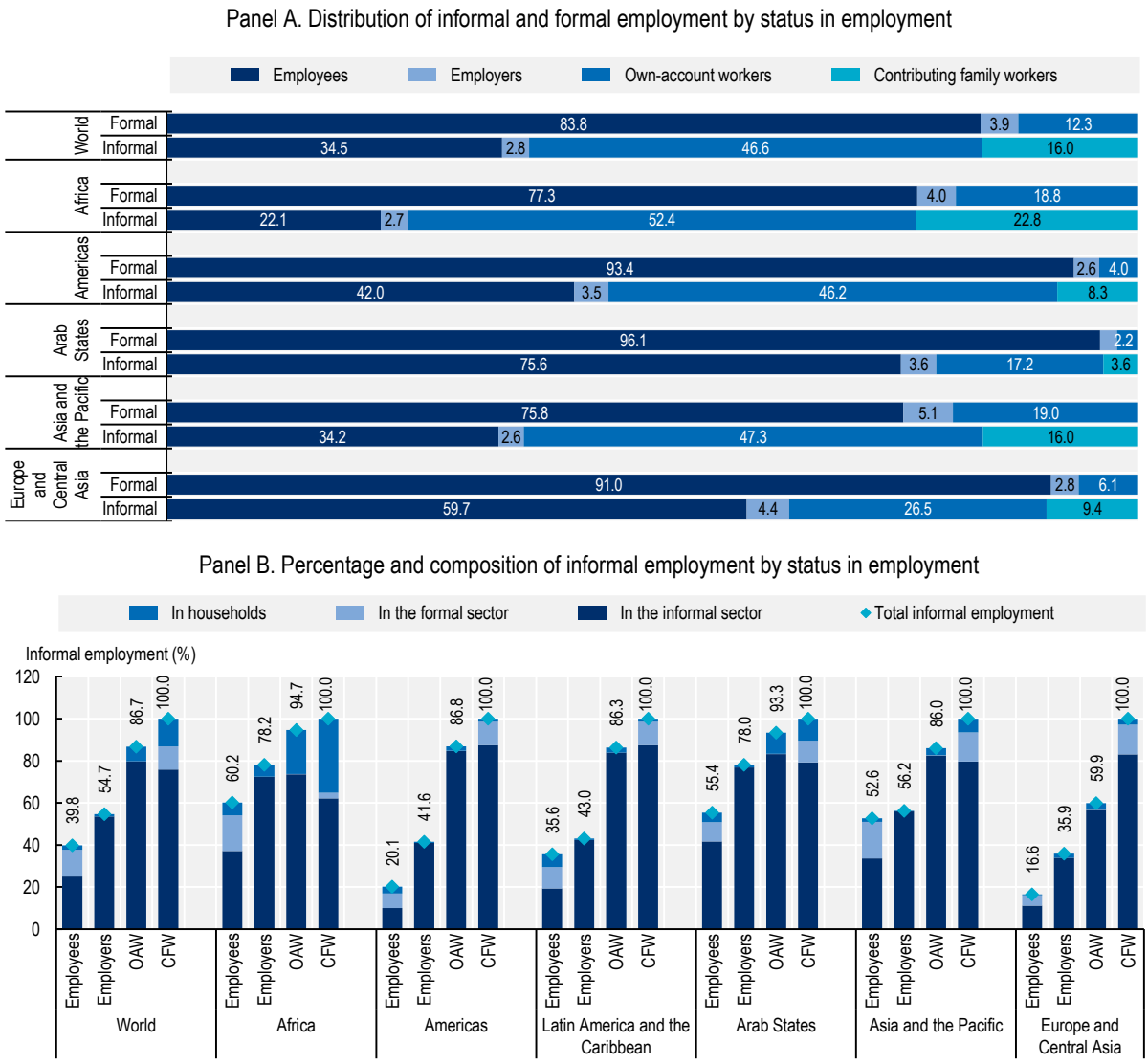
Own-account workers are most at risk of informality everywhere, but with variation by level of development

Globally, own-account workers represent the majority of informal workers (46.6%), followed by employees (34.5%), contributing family workers (16.0%) and employers (2.8%) (Figure 2.7**,** Panel A). Taken together, own-account workers and contributing family workers, both vulnerable statuses, comprise 62.7% of informal employment, which is almost five times their representation among workers in formal employment (12.3%) worldwide.

The level and structure of informality are largely influenced by the overall composition of employment. In low-income and lower-middle-income countries, this is characterised by the prevalence of vulnerable employment statuses, dominance of specific sectors (agriculture, wholesale and retail trade, and manufacturing) and over-representation of small- and low-productivity economic units (micro and small enterprises). In low-income countries, vulnerable employment statuses (own-account workers and contributing family workers) represent close to eight out of ten workers and more than eight out of ten informal workers, 75.2% in Africa and 63.2% in Asia and Pacific. In high-income countries, by contrast, the majority of informal workers are employees in undeclared or unprotected work (62.6%) or disguised self-employed whose employment relationship is not recognised (Williams, 2020[17]).

Apart from contributing family workers, who all have informal jobs by definition, own-account workers are the most at risk of having informal jobs. The majority, 86.7% of own-account workers (including, disguised self-employed) and 54.7% of employers own and operate an informal economic unit. By contrast, four out of ten employees are informally employed. This proportion ranges from 16.6% in Europe and Central Asia to more than 60% in Africa. Among informal employees, 62.9% work in informal sector units, 31.8% work in fully formal enterprises and 5.9% are domestic workers. Given the various levels of exposure to informality by employment status, an over-representation of own-account workers and contributing family workers in countries or in certain sectors or categories of workers contributes to the overall extent of informality in those countries and categories of workers.

Figure 2.7. Own-account work is the dominant form of informal employment followed by informal wage employment (2019)



Note: OAW = own-account workers. CFW = contributing family workers.
Source: (ILO, 2023[3]).

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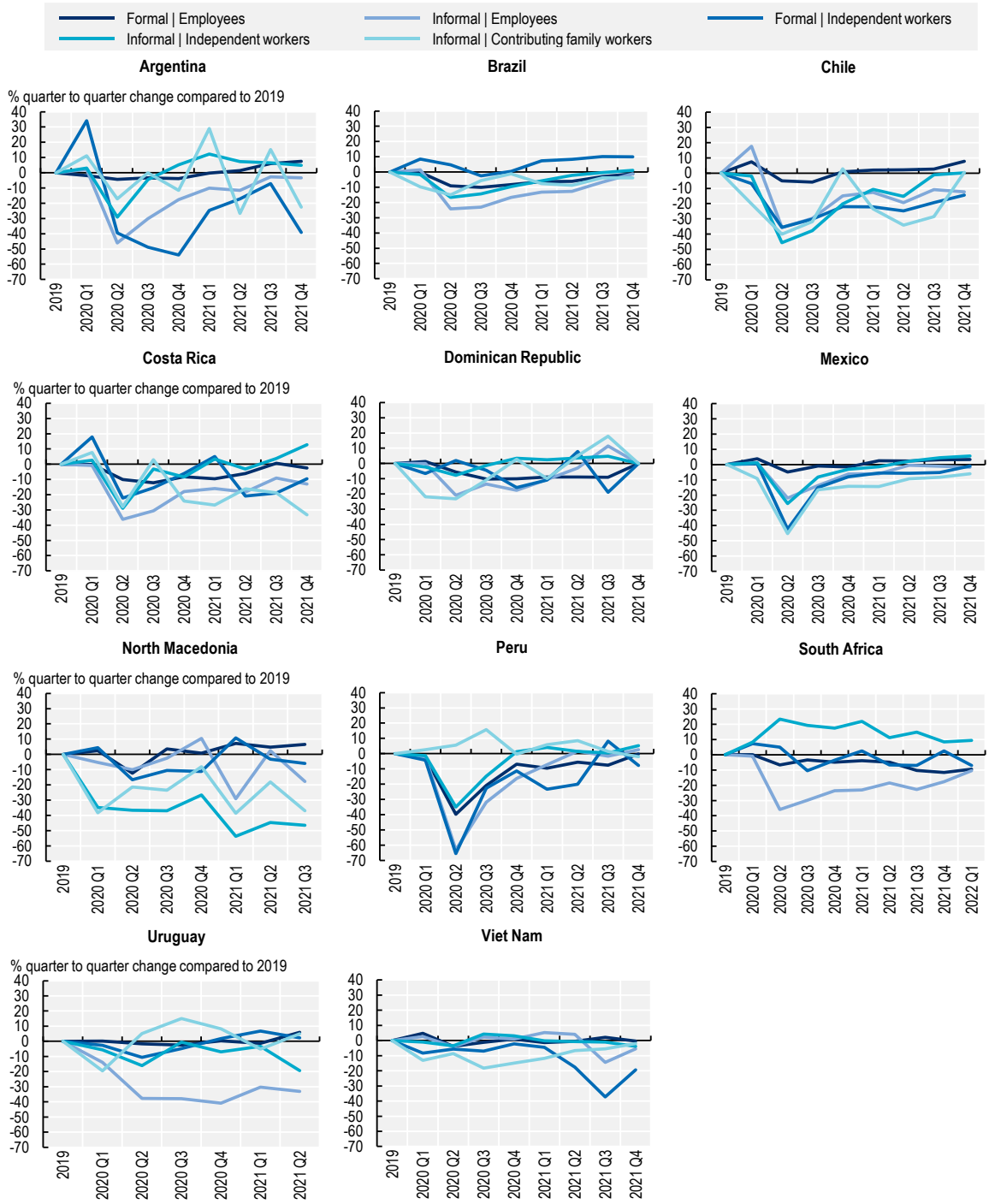
Informal employees were, and in some countries remain, more affected by the COVID-19 crisis than their formal wage counterparts, but also relative to independent workers employed in the informal sector. Using data from a sample of ten middle-income countries, analyses indicate that in the initial stages of the pandemic, informal employees were three times more likely than formal employees to lose their jobs. In subsequent stages, formal wage workers returned to work, while informal wage employment has remained below pre-crisis levels. Figure 2.8 highlights the differentiated impact of the crisis on employees and independent workers, at different stages of the pandemic-induced crisis (ILO, 2022[18]).

Figure 2.8. Trends in the number of workers (informal and formal) by status in employment compared to 2019 in selected countries



Note: Figures present the percentage change in the number of workers in formal or informal employment in a given quarter in 2020 or 2021 compared to the same quarter in 2019 (pre-COVID-19 pandemic) in order to take into account possible seasonal variations. The figure shows, for illustrative purposes only, a subset of the countries for which data are available.
Source: (ILO, 2022[18]).

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At the height of the pandemic-induced crisis (second quarter of 2020), job losses among employees in informal employment were much higher than among employees in formal employment in 22 out of the 25 countries with available data (ILO, 2022[18]). The percentage decline in the number of jobs among informal wage workers compared to their formal counterparts was up to ten times higher in Argentina and Uruguay. Informal wage workers were also more affected than independent workers (employers and own-account workers) in the informal sector in the majority of countries. South Africa and Argentina illustrate this situation, which concerns 18 out of the 25 countries studied. A smaller set of countries experienced the opposite situation, with independent workers more adversely affected in countries such as Chile, Mexico and North Macedonia.

In subsequent stages of the crisis, formal wage workers returned to work, while informal wage employment remained below its pre-crisis level in 11 out of the 13 countries (with some data available until 2021). Argentina, Chile, Costa Rica, Mexico, North Macedonia and Uruguay clearly illustrate this trend. By contrast, the number of formal and informal independent workers over the period was far more volatile. These descriptive trends (rather than panel data) provide some indication of the risk of informalisation of the labour market and to some extent of previously formal jobs. In a number of countries, the growth in informal jobs exceeded the growth in formal jobs (as well as the absolute level of informal jobs) in 2019. This evidence suggests a trend towards the informalisation of independent workers (Argentina, Chile, Costa Rica, Dominican Republic, Mexico or Viet Nam) and/or employees (Dominican Republic and Peru).

Workers in non-standard forms of employment are particularly exposed to informality

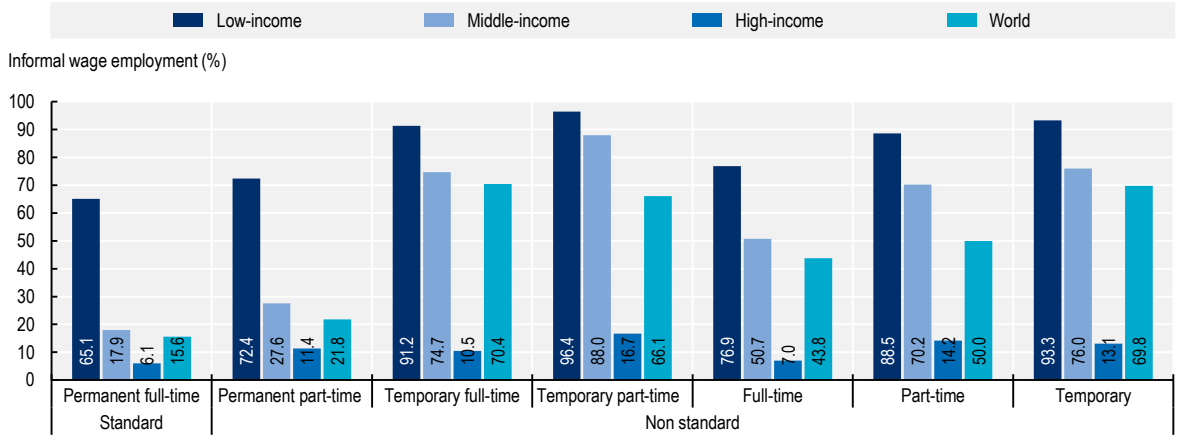
Compared to workers in open-ended full-time employment, employees in non-standard forms of employment[4] (i.e. forms of employment that differ from full-time dependent employment with a permanent contract) are significantly more likely to be in informal employment (ILO, 2016[19]) (Figure 2.9). Globally, in 2019, 15.6% of employees in permanent full-time employment had an informal job, defined as one offering no employment-related social and labour protections. Among part-time and temporary employees, however, 50.0% and 69.8%, respectively, were informally employed. For those employed in temporary part-time work, the rate of informal employment amounted to 66.1%.

Workers in temporary and part-time employment are prone to informality because they are, in some cases, either outside the scope of laws and regulations relating to social security or do not meet the qualifying thresholds, in terms of length of employment or number of hours worked. In some countries, temporary workers are excluded from social security coverage. This is particularly the case for workers engaged in project or task-based work (ILO, 2020[20]). Regarding part-time work, some countries restrict workers' eligibility by stipulating a minimum number of hours of work, which has the effect of excluding some part-time employees from the coverage of social protections. Domestic workers who perform a limited number of hours per week or per day for different employers have been particularly affected by such thresholds[5] (ILO, 2021[21]; ILO, 2022[22]). Such non-explicit indirect exclusions, resulting from the inability to meet minimum qualifying conditions, are numerous but not as widespread as the ineffective implementation of legislation for reasons that include the lack of employment contracts, employer financial constraints, heavy or inappropriate compliance modalities, lack of awareness, or deliberate non-compliance (ILO, 2015[23]).

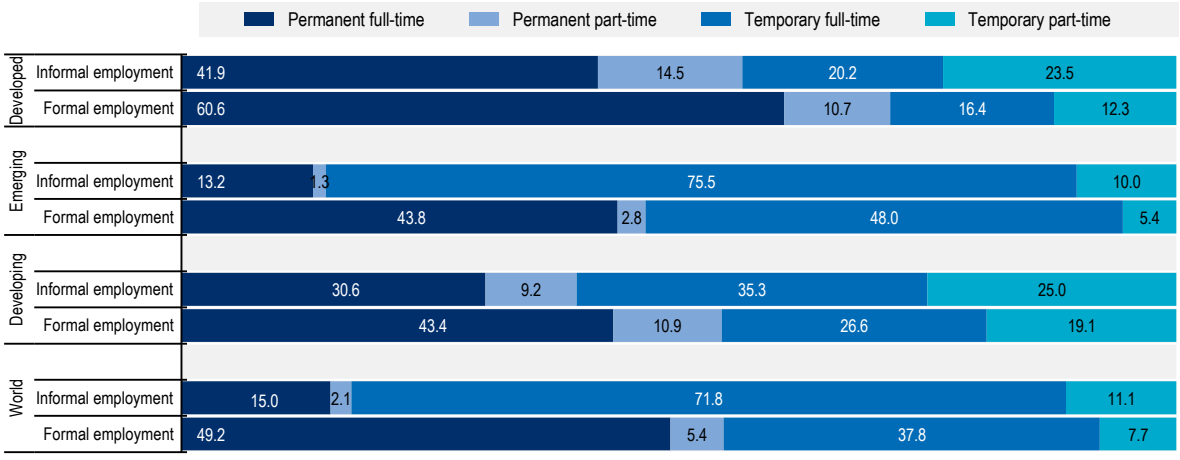
By considering the relative importance of temporary employment among employees according to the formal or informal nature of the employment, the use of temporary or casual employment is also close to twice as high among workers in informal wage employment (82.9%) compared to formal wage workers (45.5%); it is also highest among informal wage workers in emerging countries and more prevalent among men than among women (Figure 2.9, Panels B and C).

Figure 2.9. Informal employment is widespread in temporary employment in developing and emerging countries

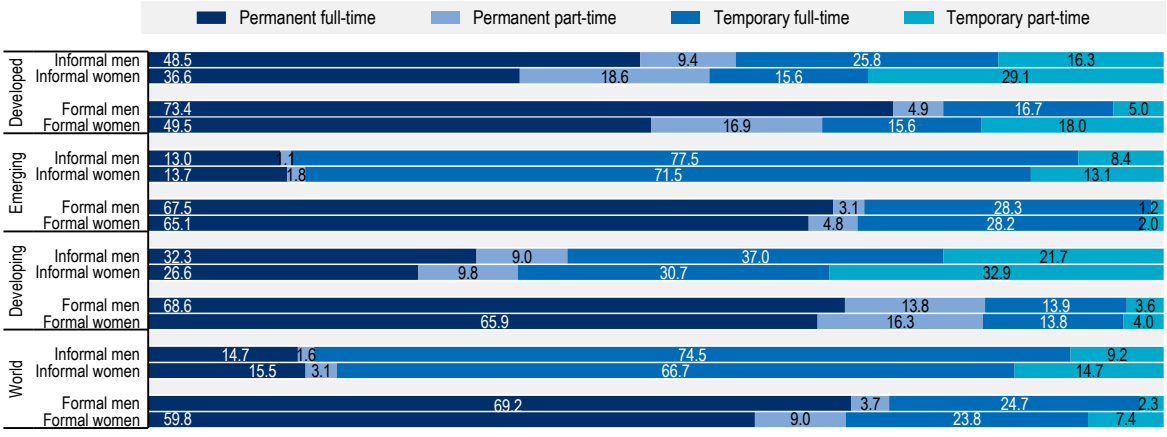
Panel A. Share of informal employment among employees, by type of employment (2019)



Panel B. Distribution of informal and formal wage employment by type of employment arrangement



Panel C. Distribution of informal and formal wage employment by type of employment arrangement and gender



Note: Estimates based on data for 113 countries representing more than 70% of global wage employment. Harmonised definition of informal employment and employment in the informal sector.
Source: (ILO, 2022[18]).

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An additional and growing category of workers excluded from the results above (Figure 2.9), but included as a non-standard form of employment and at high risk of informality, are those in between the "binary divide" many legal systems create distinguishing employees from independent employment (Countouris and Freedland, 2013[24]). This grey area includes "disguised employment relationships" and "dependent self-employment" that are most prevalent in labour-intensive industries such as transport, construction, business services, and cleaning (Jorens, 2008[25]; Thornquist, 2013[26]). Labour intermediaries and elaborate subcontracting chains are common in these industries and contribute to disguised employment relationships as they serve to hide workers' employment status (Pedersini and Coletto, 2009[27]; Lukiyanova, 2015[28]). The various forms of "'platform"' work discussed in Chapter 5 have also been associated with a growth in disguised employment relationships.

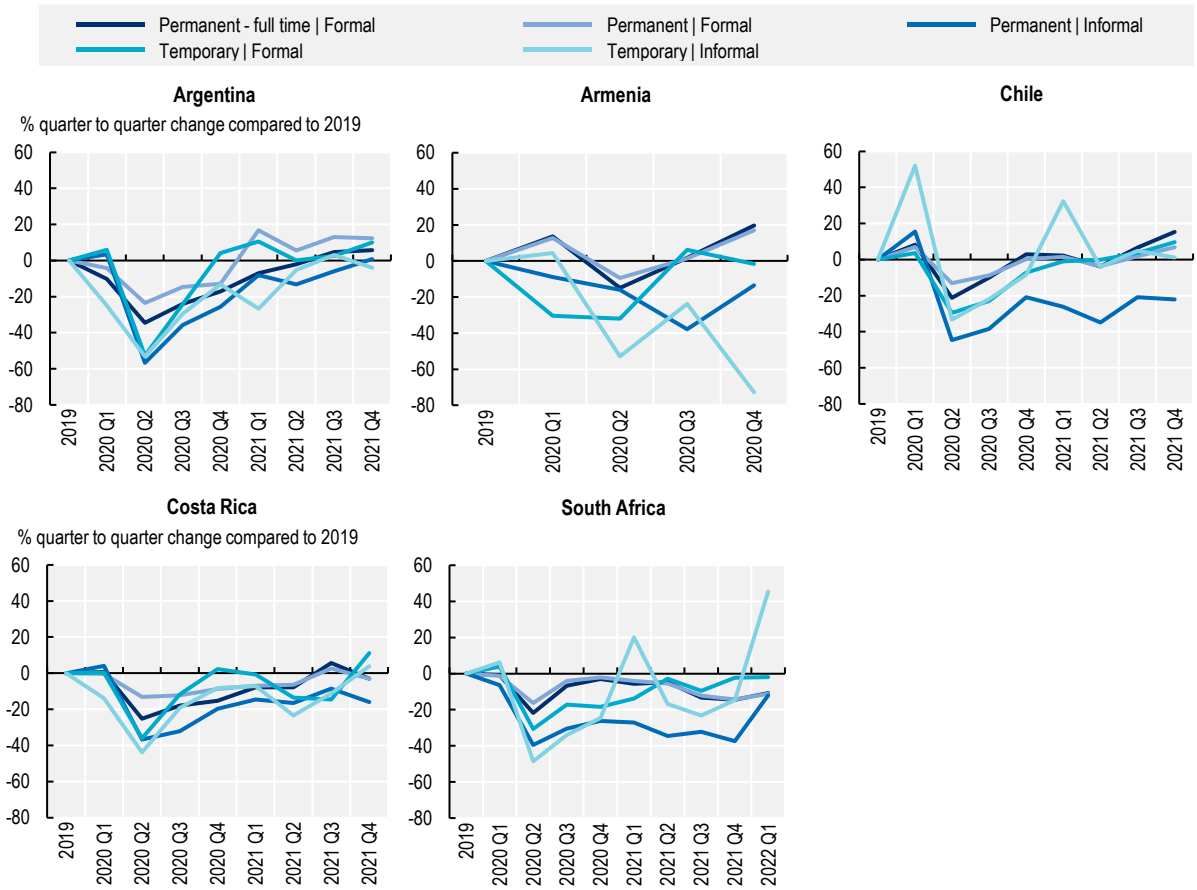
Due to the informal nature of informal employees' jobs, it can be assumed that for many the temporary or permanent nature of their employment relationship is not formally defined; rather, it is based on a tacit agreement or perception. Bearing this caveat in mind, three trends emerged during the COVID-19 crisis. First, at the onset of the crisis (through the second quarter of 2020), in Argentina, Chile, Costa Rica, South Africa informal employees were more adversely affected than formal employees, irrespective of whether they were employed on a temporary or permanent basis (Figure 2.10). Second, at the height of the crisis, formal temporary employees were significantly more affected than formal employees with a permanent job. Third, symptomatic of a climate of uncertainty, among informal employees, the recovery was primarily fuelled by abundance of temporary jobs, while the number of permanent informal jobs remained well below 2019 levels.

Another category of employment that is also sometimes considered as a form of non-standard employment is homework (ILO, 2016[19]). Globally, there were about 260 million home-based workers in the world in 2019 (ILO, 2021[29]).This included industrial home work (goods production undertaken by homeworkers either as part of, or replacing, factory production, but also artisanal production, such as in the making of handicrafts); telework (employees who use information and communications technologies to perform their work remotely on a regular or permanent basis); and home-based digital platform work (discussed in Chapter 5). Nearly 86% of home-based workers live in developing and emerging economies. In low- and middle-income countries, 90% of home workers work informally (ibid). The percentage of informality among home-based workers ranges from 98% in both Southern Asia and the Middle East and North Africa to 63% Eastern Europe, Southern Europe and Central Asia (Bonnet et al., 2021[30]).

Home-based workers have their homes as workplace, which has a significant bearing on the recognition of these workers and their workplaces, ensuring decent working conditions, and providing public support. During the COVID-19 crisis, homeworking related to teleworking has expanded. In contrast, home-based workers who do not use Internet in their work, including traditional self-employed and industrial outworkers, as well as the contributing family workers who depend on them for work, suffered the greatest loss of work and income, as compared to other categories of homeworkers (Bonnet et al., 2021[30]).

Figure 2.10. Trends in the number of permanent and temporary wage workers (informal and formal), compared to 2019

Percentage change



Source: (ILO, 2022[18]).

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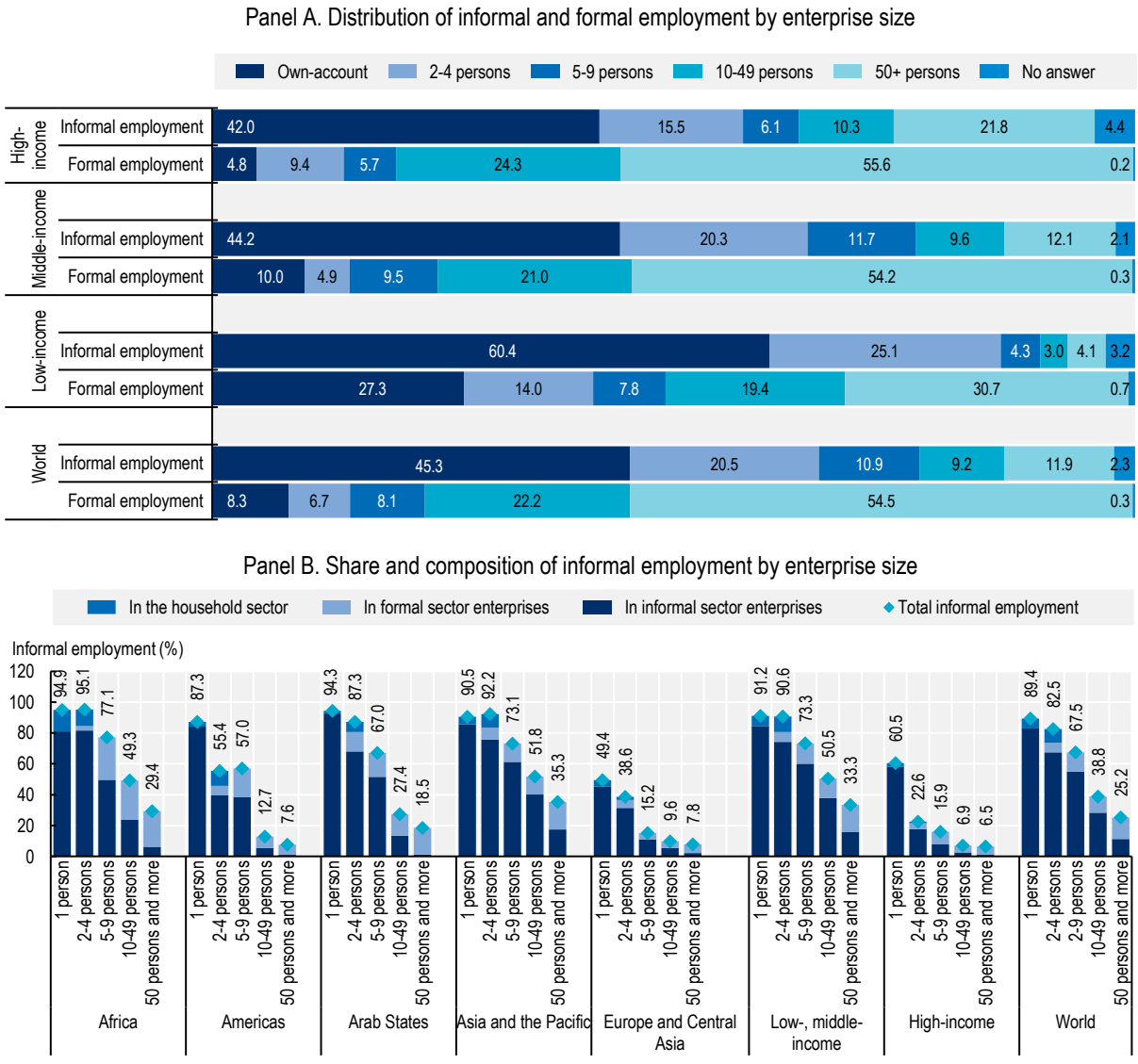
Most employment in small enterprises is informal, but informal employment in large formal enterprises is significant

Smaller enterprises, including own-account workers, constitute the bulk of total employment globally, but especially in low- and middle-income countries. Units with fewer than ten workers accounted for 55.5% of total employment globally and as high as eight out of ten workers or more in low- and lower-middle-income countries and in Africa. High-income countries as well as Europe and Central Asia show a different picture: enterprises with fewer than ten workers account for one-quarter and one-third, respectively, of total employment.

Turning to the share of informal employment by size of enterprise, employment in small economic units – as dependent workers or as business owners – is more likely to be informal than in larger enterprises. Globally, the share of informal jobs decreases as the size of an economic unit increases. While 89.4% of own-account workers operate informally, informal employment decreases to 82.5% in enterprises employing between two and five persons, and to 25.3% in enterprises employing 50 persons or more.

Figure 2.11. Most employment in small enterprises is informal, yet informal employment in large formal enterprises is significant



Note: Estimates based on data for 129 countries representing 86% of the world's employed population. Harmonised definition of informal employment and employment in the informal sector.
Source: (ILO, 2023[3]).

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As a result of small enterprises' greater use of informal employment, enterprises with fewer than ten workers account for 76.7% of total informal employment globally and up to 90% or more in low-income countries and in Africa. By contrast, in high-income countries or in Europe and Central Asia, these enterprises comprise about 65% of informal employment (Figure 2.11, Panel A). These results imply that informal jobs are also in larger enterprises, including in formal enterprises, despite these enterprises' greater ability to interact with government administration, and also despite their productivity and administrative capacities. Globally, one-quarter of people employed in large enterprises have informal jobs; the majority are employed by formal enterprises. These workers lack recognition of their employment relationship or a contract that provides social protection and other benefits. Excluded from this estimate is

the large number of informal economy workers employed through a disguised employment relationship, subcontracted by formal enterprises and misclassified as own-account workers (ILO, 2016[19]).

Informal employment has a strong sectoral dimension

Six sectors have informal employment rates that exceed the global average (58.2%): nine out of ten workers in agriculture; more than eight out of ten workers in the domestic work sector (ILO, 2021[21]) and household production for own use; close to three out of four workers in the construction sector; and three out of five in accommodation and food service activities, wholesale and retail trade, repair of motor vehicles and motorcycles, and other services activities (Figure 2.12, Panel A).

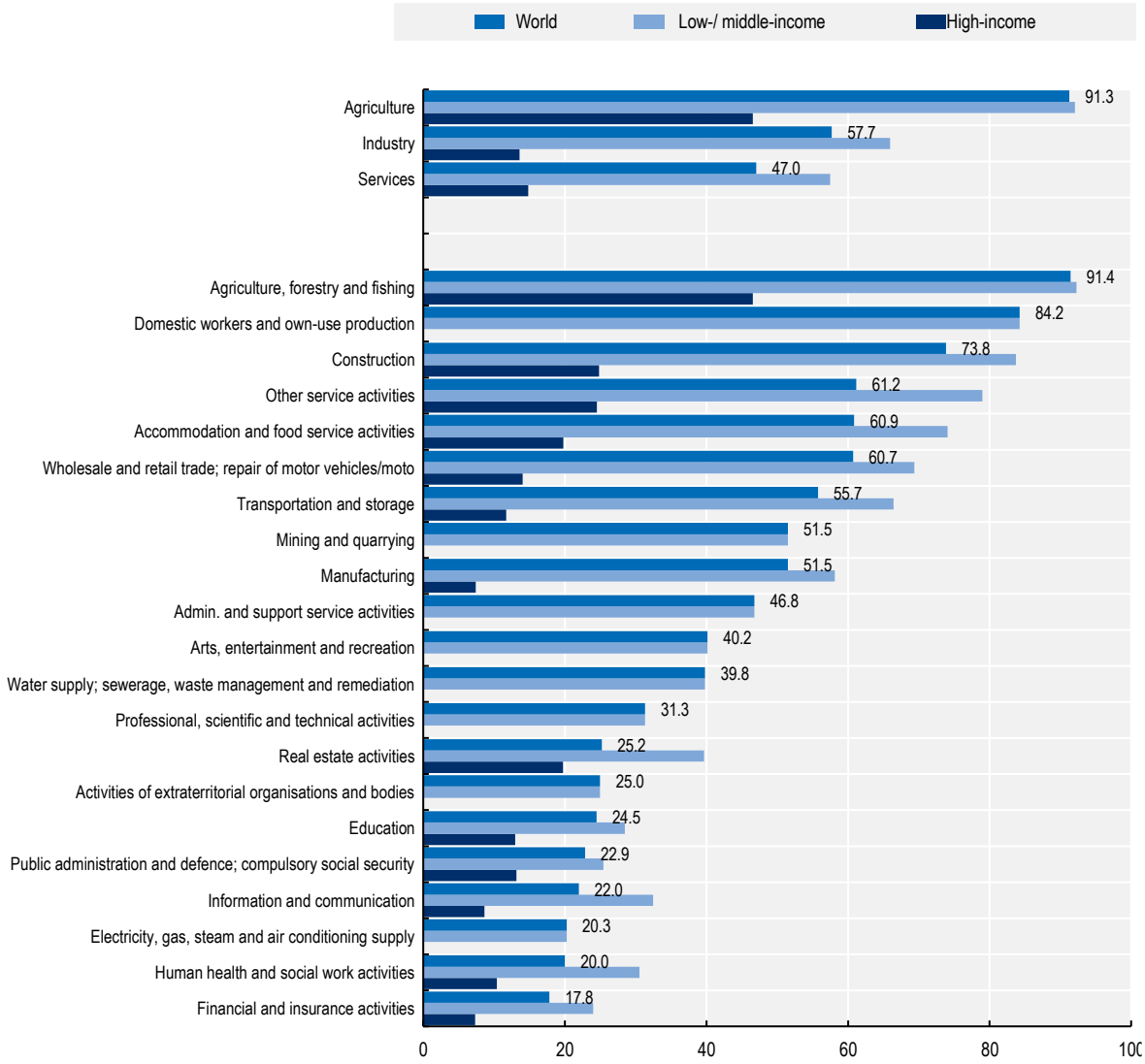
Some of those sectors also employ the largest number of informal workers (if not the majority). Globally, 33.0% of all informal workers work in agriculture. This proportion reaches 62.1% in low-income countries, 57.1% in Africa, but only 9.2% in high-income countries. The wholesale and retail trade sector employs the second largest number of informal workers. This sector includes the numerous street vendors, small shops and workshops in fixed or non-fixed places in most low- and middle-income countries (14.0% globally but one in five informal workers in the Arab States or in Latin America and the Caribbean). The manufacturing sector (12.3% of total informal employment but higher in Asia and Pacific) and the construction sector (11.5%) are also large sources of informal employment. In aggregate terms, agriculture's contribution to informal employment decreases, and the services sector's contribution to informal employment grows as a country's level of development increases (Figure 2.12, Panel B).

Figure 2.12, Panel C, shows the sectors where women (in formal or in informal employment) are over-represented, relative to men (see right-hand side of the figure), and those where men are over-represented, relative to women (see left-hand side of the figure). There are two key trends. First, there is clear evidence of gender segmentation in informal employment across the sectors. This is exemplified by the width of the bars, which would equal zero if gender segmentation was absent. Second, across the globe, public administration, education and health, accommodation and food service activities, wholesale and retail trade, domestic work, manufacturing and agriculture, are sectors where women in informal employment are over-represented in comparison to men. For example, the proportion of domestic work and own-use production sector among women in informal employment is 3.4 percentage points higher than the corresponding proportion among men informally employed. By contrast, men in informal employment are over-represented in the construction sector, transportation and storage, and other industries.

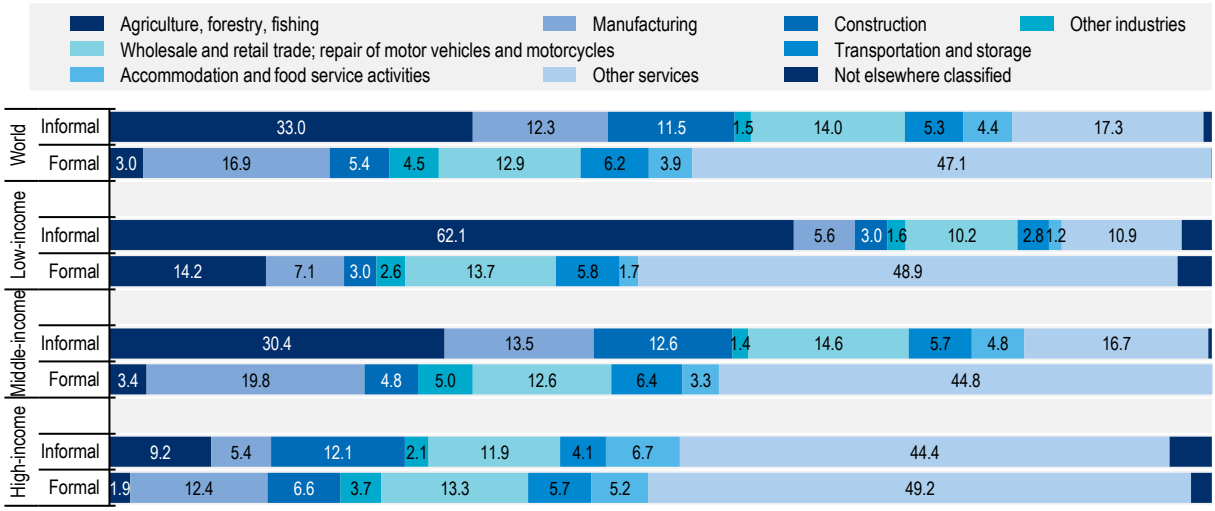
However, this global picture conceals differences by country income level. For instance, at the global level, agriculture and manufacturing represent higher shares among women informally employed (1.4 and 2.7 percentage points more respectively) relative to men employed informally. By contrast, in high-income countries, the opposite trend emerges; the representation of those two sectors among men informally employed exceeds (by 2.2-2.3 percentage points) the representation of women in the same sectors. In addition, similar to informal employment, gender segmentation also exists, to a lesser extent, in formal employment across the sectors. The greatest segmentation, however, occurs in high-income countries across formal and informal employment.

Figure 2.12. The sectoral dimension of informality

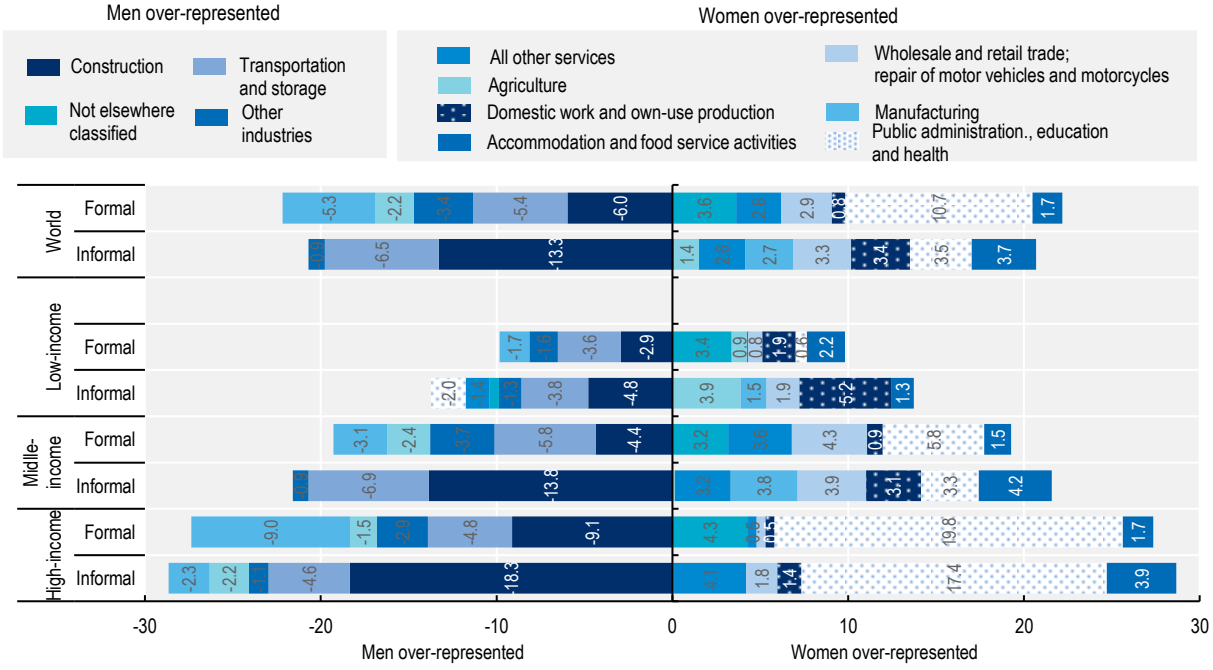
Panel A. Percentage of informal employment by sector



Panel B. Distribution by sector



Panel C. The sectoral distribution of employment through the gender lens



Note: Estimates by International Standard Industrial Classification (ISIC) at 1-digit level based on data for 102 countries representing 77% of the world's employed population. Harmonised definition of informal employment and employment in the informal sector. In Panel C, the length of bars shows the extent of gender segmentation, measured by the difference between women and men as a proportion of total (female or male) workers (in informal employment and in formal employment, respectively) in given sectors. A positive value (on the right-hand side of the figure) means that the proportion of women in employment in a particular sector is higher than the corresponding proportion of men employed in the same sector. By contrast, negative values as shown on the left-hand side of the figure reflect sectors in which men are over-represented.
Source: (ILO, 2023[3]).

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The effect of the COVID-19 crisis also had a strong sectoral dimension (Figure 2.13). Heavily affected sectors include those where informal workers tend to be disproportionately represented: the wholesale and retail trade sector, construction, manufacturing, accommodation and food service activities. Two of these

sectors – accommodation and food service activities – also form part of the broader tourism industry, which was disproportionately affected by the COVID-19 pandemic due to lockdowns and travel restrictions (ILO, 2022[31]). Workers in agriculture were also affected, as they faced difficulties selling their products in urban markets, despite being considered at lower risk and playing the role, in some countries, as the employer of "last resort sector" (ILO, 2020[32]).

Focusing on these sectors and analysing the respective situation of workers in formal and informal employment over time, between the second quarter of 2020 and the third and fourth quarter of 2021, the results from 22 countries present a picture of major upheaval (Figure 2.14).

At the beginning of the COVID-19 pandemic, in the second quarter of 2020, workers in informal employment were more affected by job losses than workers in formal employment, in 13 to 17 out of the 22 countries considered, depending on the sector. The percentage decline in the number of informal jobs was the largest in accommodation and food service activities (-36.5% decline in the number of informal jobs, compared to -26.8% for formal jobs), followed by construction and the wholesale and retail trade. In the early stages of the crisis, agriculture played the role of "employer of last resort" in only a few countries (such as Peru and Armenia); this may also have occurred in other low- and lower-middle-income countries where reliable data are unavailable for this period.

By the end of 2020 (Figure 2.14, Panel A), the situation varied between sectors and for workers in formal and informal employment. The impact of the COVID-19 pandemic on employment had persisted in accommodation and food service activities, relative to other sectors. Moreover, workers in both formal and informal employment were affected, even at the end of 2021.

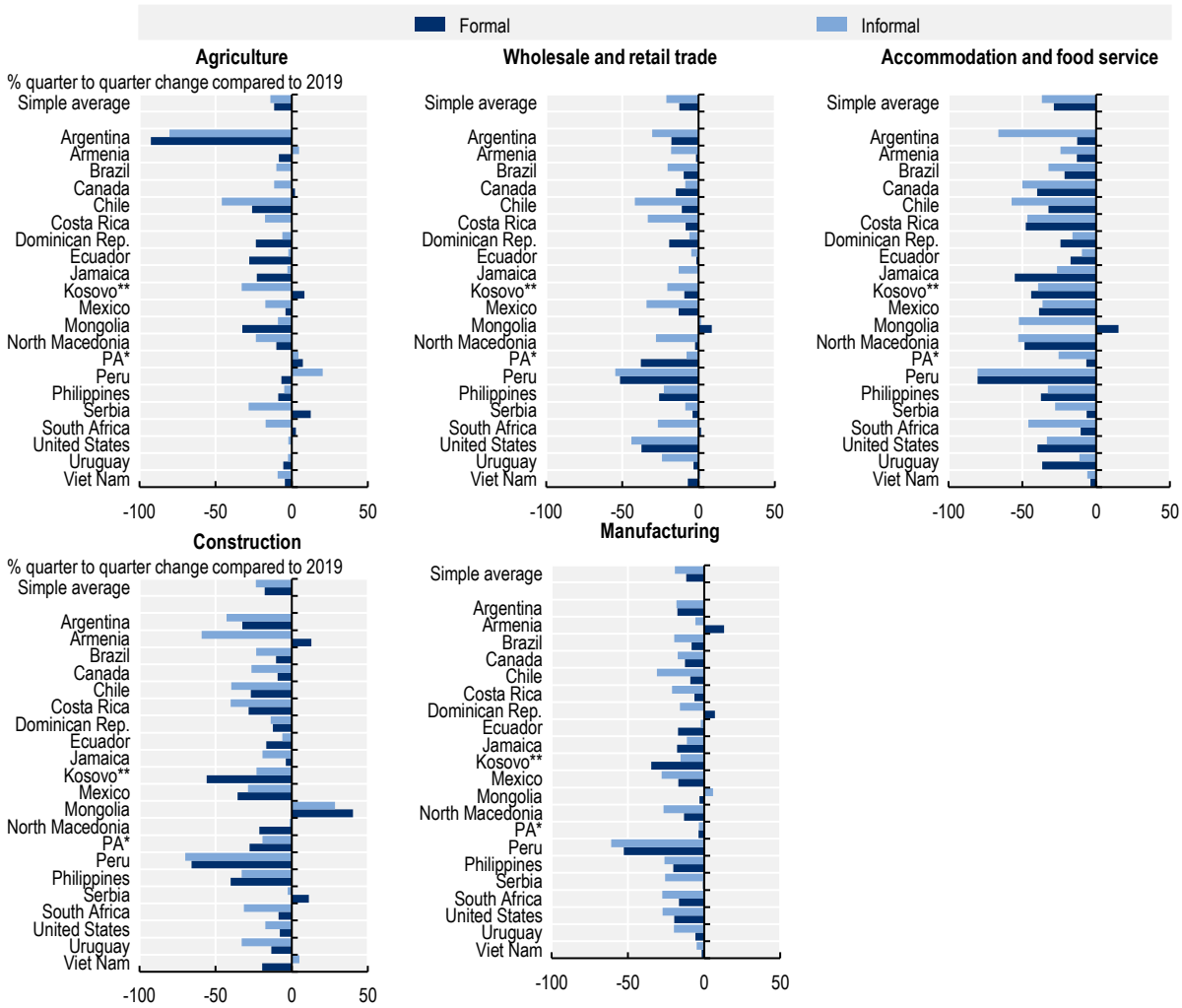
Some workers returned to work in the agricultural sector, mainly in formal jobs, which could be the result of strategies adopted to compensate for the disruption of food supply chains, especially in emerging countries (OECD, 2020[33]).

While trends towards informalisation remain uncertain at the national level, trends in some sectors are clear. For example, at the end of 2020, in the manufacturing and construction sectors in Serbia and Argentina, sectoral employment levels were equal to or exceeded those in 2019; however, the growth in informal jobs exceeded the increase in formal jobs, leading to informalisation of both sectors. Some signs of informalisation in the labour market further emerged in the last quarters of 2021 in Chile, the Dominican Republic and Peru, notably in the construction sector (Figure 2.14, Panel B).

The COVID-19 crisis has also revealed the extent to which our societies depend on "key workers" – those that provide essential goods and services that enable societies to function. "Key workers" include food systems workers; health workers; retail workers; security workers; manual workers; cleaning and sanitation workers; transport workers; and technicians and clerical workers. Globally, 51.0% of "key workers" are informal, and up to 64.0% in low-income countries (ILO, 2023[34]). Ensuring their protection is not only a matter of rendering societies more resilient, but is also a matter of social justice.

Figure 2.13. Trends in the number of jobs (informal and formal) in the second quarter of 2020 compared to 2019

Percentage change in selected sectors



Note: * PA refers to the Palestinian Authority. ** This designation is without prejudice to positions on status, and is in line with United Nations Security Council Resolution 1244/99 and the Advisory Opinion of the International Court of Justice on Kosovo's declaration of independence.

Source: (ILO, 2020[12]).

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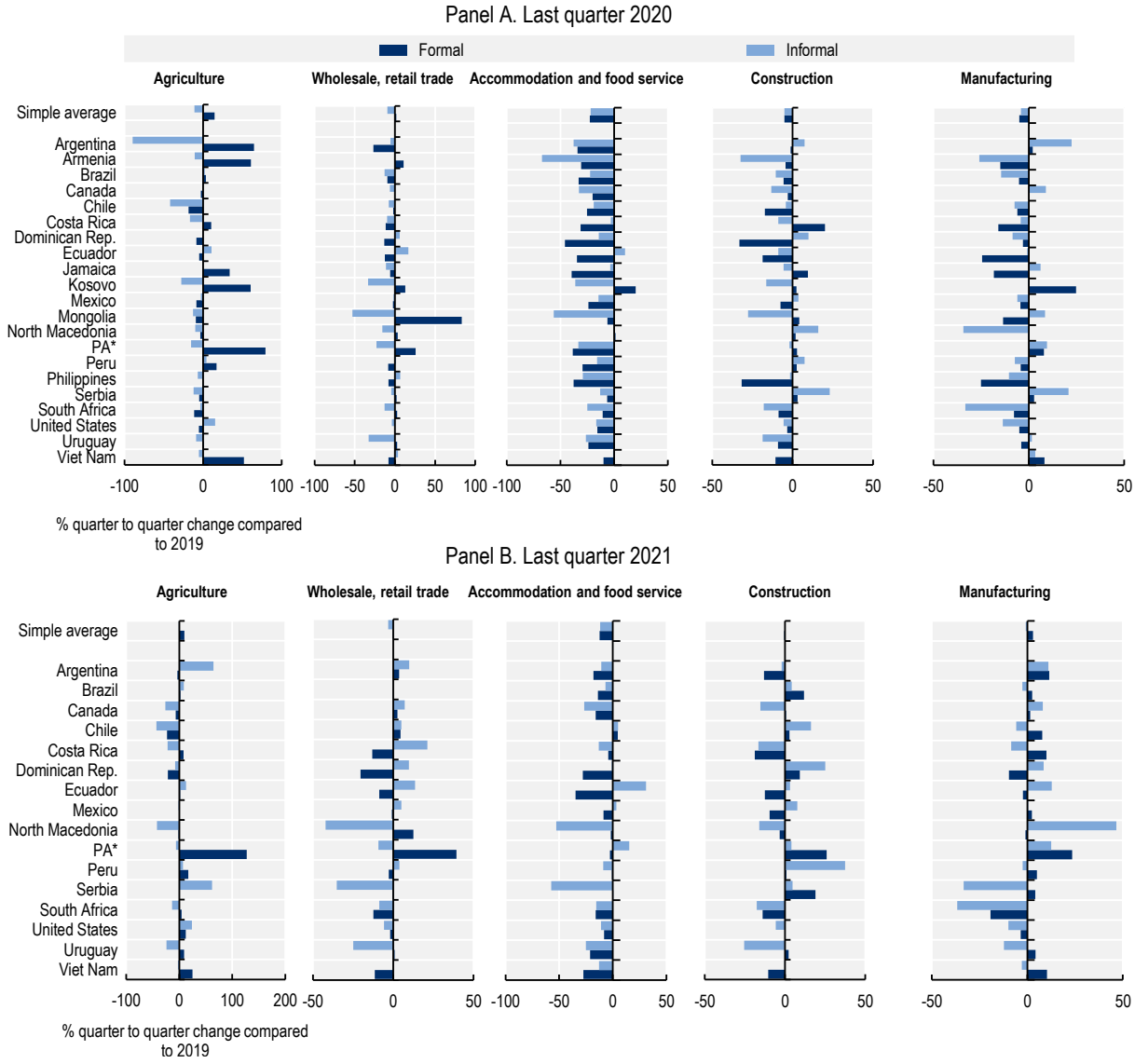
Figure 2.14. Trends in the number of jobs (informal and formal) after the second quarter of 2020 compared to 2019

Percentage change in selected sectors



Note: PA refers to the Palestinian Authority.
Source: (ILO, 2020[12]).

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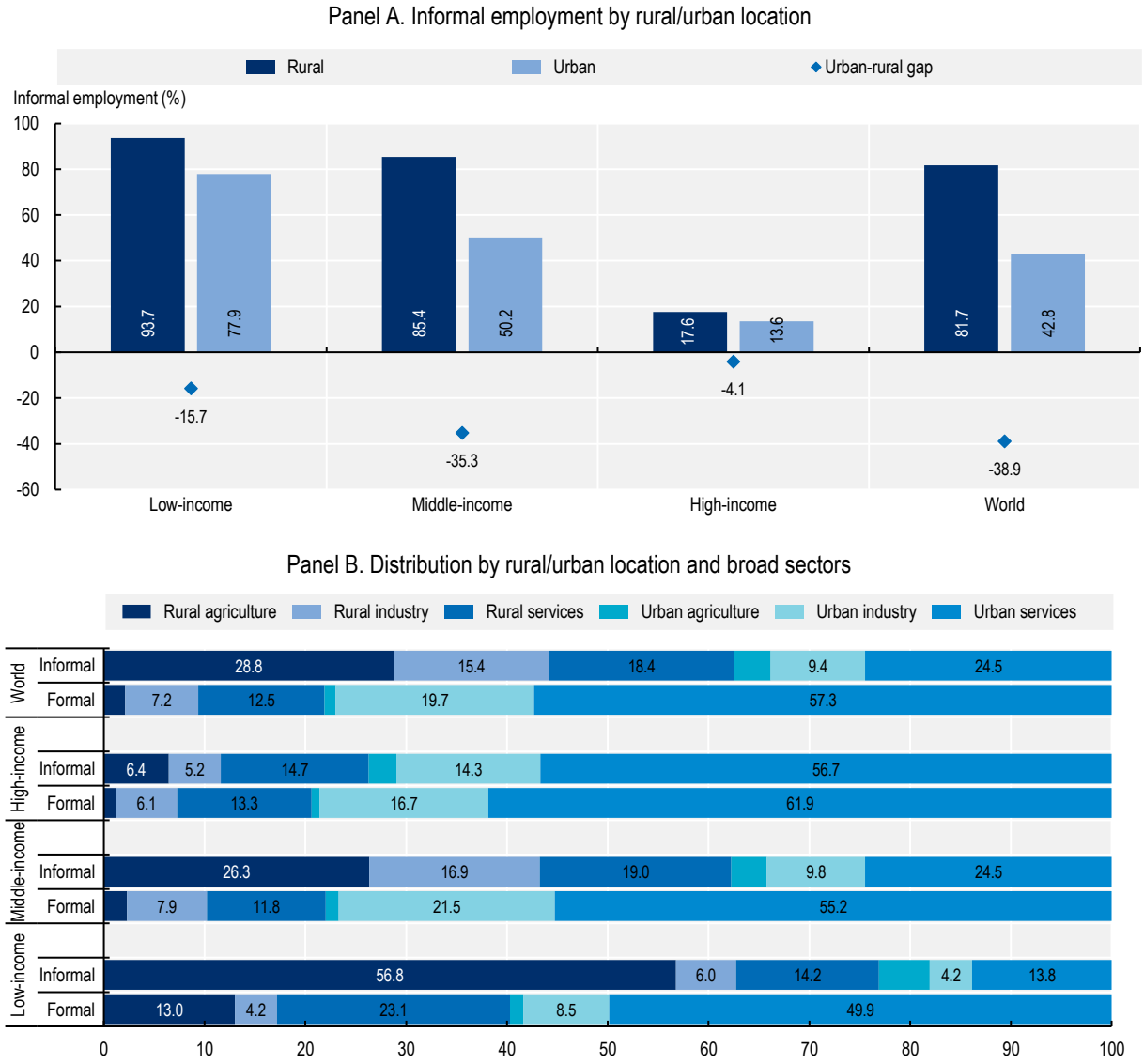
Informality has a strong rural dimension

Figure 2.15. Informality has a strong rural dimension



Note: Estimates based on data for 121 countries representing 88% of the world's employed population. Harmonised definition of informal employment and employment in the informal sector.
Source: (ILO, 2023[3]).

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People in rural areas are almost twice as likely as those in urban areas to be in informal employment: 81.7% versus 42.8% (Figure 2.15, Panel A). Moreover, 62.5% of workers in informal employment live in rural areas, while 78.1% of those in formal employment live in urban areas (Figure 2.15, Panel B). Workers in informal employment in agriculture represent just above 45% of global rural employment but as high as 73.8% of rural employment in low-income countries. However, the high rate of informality among agricultural workers only partially explains differences in the urban-rural informality rates. Other factors include the institutional and economic environment (e.g. limited access to public infrastructure and

services, and differences in quality of services and local governance); personal and employment characteristics of the rural population (including higher incidence of poverty, lower education levels or an over-representation of individuals with an employment status that is at high risk of informality); or traditions and rural actors' perceptions of laws and regulations and social norms (Jonasson, 2012[35]; Weng, 2015[36]). Activities in rural areas, in particular in agriculture, are often "regulated" by the co-existence of customary rules and formal rules, and strong social trust among producers and traders, which enables the creation of informal institutions. In this context, informal activities are perceived as equally or even more legitimate than formal practices. In the absence of strong organisations and effective consultation processes between the state and rural actors, formal arrangements (regulations, laws) perceived as an unwelcome imposition are likely to face some resistance or "deliberate ignorance".

Vulnerable groups are disparately exposed to informality

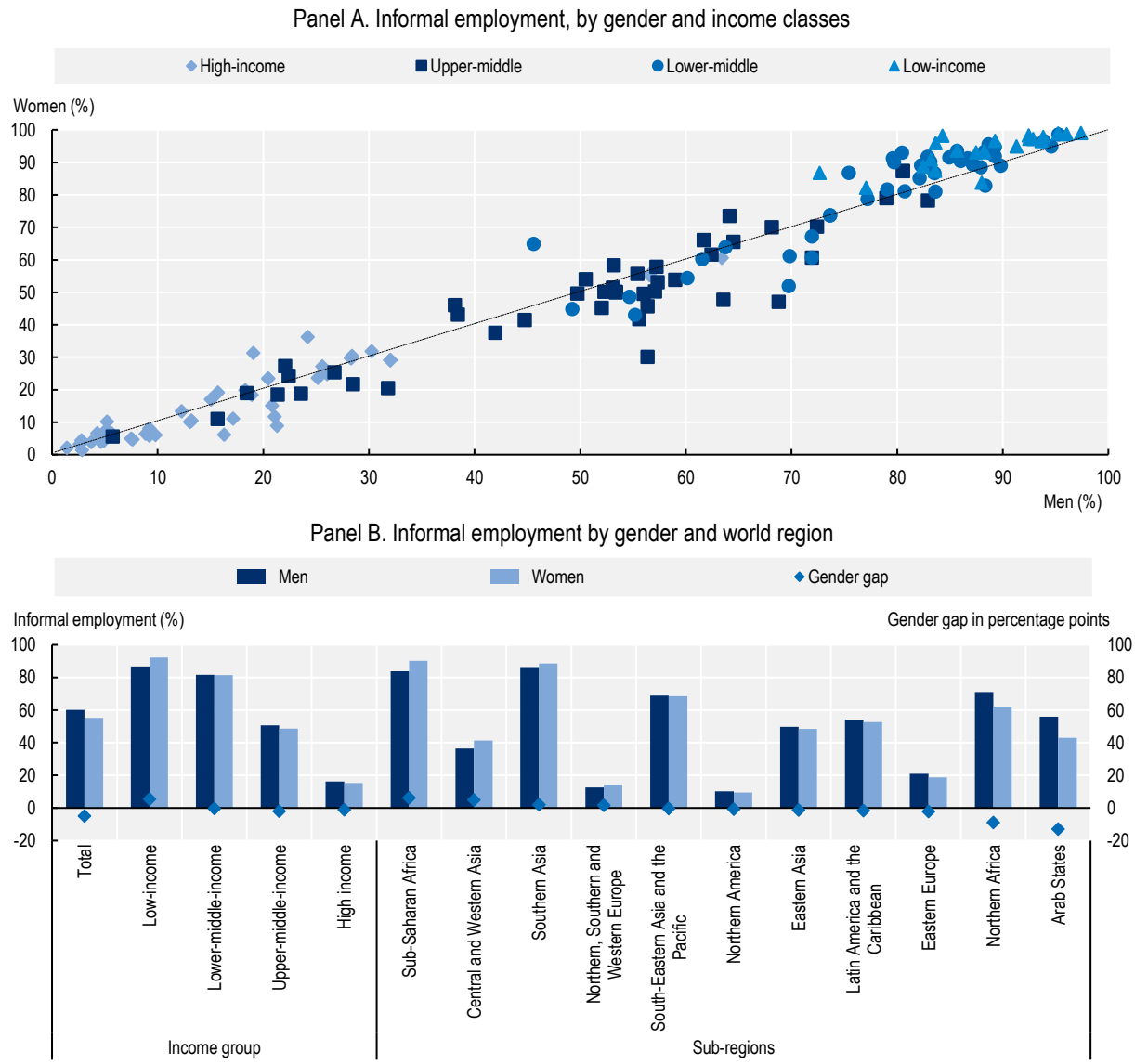
Certain individual characteristics can predispose an individual to informal employment, often due to factors outside of their control that usually precede entry into the labour market. Societal norms play a role in limiting access to education or participation in the labour market, particularly for girls and young women. Discrimination based on gender, age, religion or ethnicity further impede certain groups' access to the labour market, as well as opportunities for professional advancement that are disproportionately available in formal employment. This section analyses the differential impact that informality engenders based on individual characteristics.

Globally, informal employment is a greater source of employment for men, but there are large disparities across countries

Worldwide, informal employment is a greater source of employment for men (60.2%) than for women (55.2%) (Figure 2.16, Panel B). The global estimate, however, reflects the influence of major countries, such as China, where men face greater exposure to informality. The gender difference at the global level also results from structural effects associated with low female labour force participation rates in some countries (as seen in Pakistan or India), which attenuate the effect of their high female informal employment rates in the global and regional estimates.

At the country and regional levels however, there are large disparities by gender. In a small majority of countries for which data are available (56%), the share of women in informal employment exceeds that of men. Informal employment is a greater source of employment for women than for men in the following regions: sub-Saharan Africa, Central and Western Asia, Southern Asia and in Northern, Southern and Western Europe and in most low- and lower-middle-income countries. By contrast, the percentage of informally employed men is substantially higher than the percentage of women workers in the Arab States and North Africa, where the female employment-to-population ratio is much lower than the male ratio. In this region, the minority of women employed are over-represented in the public sector, as well as in occupations and types of enterprises that are more likely to be formal. In most regions, women who work in informal employment are among the most vulnerable groups in the informal economy.

Figure 2.16. Women are more at risk of informality than men in more than one-half of countries



Source: (ILO, 2023[3]).

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Women tend to be under-represented among informally working employers (1.5% as compared to 3.6% for men), and among informally working employees (31.7% as compared to 36.2 % for men). In contrast, they are over-represented among contributing family members (27.7% as compared to 9.1% for men). When informally employed, women are also more likely to work from home compared to men (20.7% as compared to 5.8% for men in low- and middle-income countries) with obvious consequences in terms of visibility and representation. More generally, these differences were among the main sources of lower average earnings, greater risk of poverty, and greater vulnerability for women in the informal economy, as compared to men well before the COVID-19 crisis (ILO, 2023[3]).

The overall trends in informal employment of men and women observed since early 2020 mask considerable differences between gender. Women working informally have been, and continue to be, disproportionately affected by the COVID-19 crisis, as shown in Figure 2.17, Panel A. The share of

informally employed women declined by 24% in the second quarter of 2020 Q2; during the same period, the comparable figure for men was 18%. However, among formally employed workers no such trend emerged; during the same period, formal employment declined by about 10% for men and women. These trends suggest that informality not only exacerbated workers' vulnerability to the COVID-19 shock but it also widened gender employment gaps during the pandemic.

Why have women in informal employment been more affected than their male counterparts? First, the over-representation of informally employed women in hard-hit sectors (ILO, 2020[32]; ILO, 2020[37]) explains their disproportionate employment losses. Second, meeting increased care demands, induced by the pandemic, while remaining in paid employment, required working arrangements such as telework, leave or temporary absences, that were harder for informal workers to access (Garrote Sanchez et al., 2021[38]). Given the larger proportion of time spent by women in unpaid care work, both before and during the pandemic (ILO, 2018[39]; UNWOMEN, 2020[40]), both factors drove women out of the labour force.

In contrast, trends in formal employment by gender reveal no such pattern (Figure 2.17, Panel B). The fact that globally 40% of formally employed women work in "low-risk sectors", compared to 34% of their male counterparts, certainly mitigated possible gender differences in other sectors. The findings suggest that better working conditions and improved access to flexible working arrangements have the potential to meaningfully reduce gender inequality in the labour market (ILO, 2022[14]).

Figure 2.17. Evolution of informal and formal employment by sex

Reference quarters in 2019 = 1

Note: Estimates based on trends in the number of formal and informal jobs in Argentina, Bolivia (Plurinational State of), Brazil, Chile, Costa Rica, Dominican Republic, Ecuador, Guyana, North Macedonia, Mexico, Palestinian Authority, Peru, Paraguay, Saint Lucia, South Africa, Uruguay and Viet Nam. See individual country results in (ILO, 2020[12]). *A review of country data. Impact of the Covid-19 pandemic on informality: Has informal employment increased or decreased?* Missing observations are imputed using time-fixed effects in a panel regression of countries without missing observations.
Source: Authors' computations.

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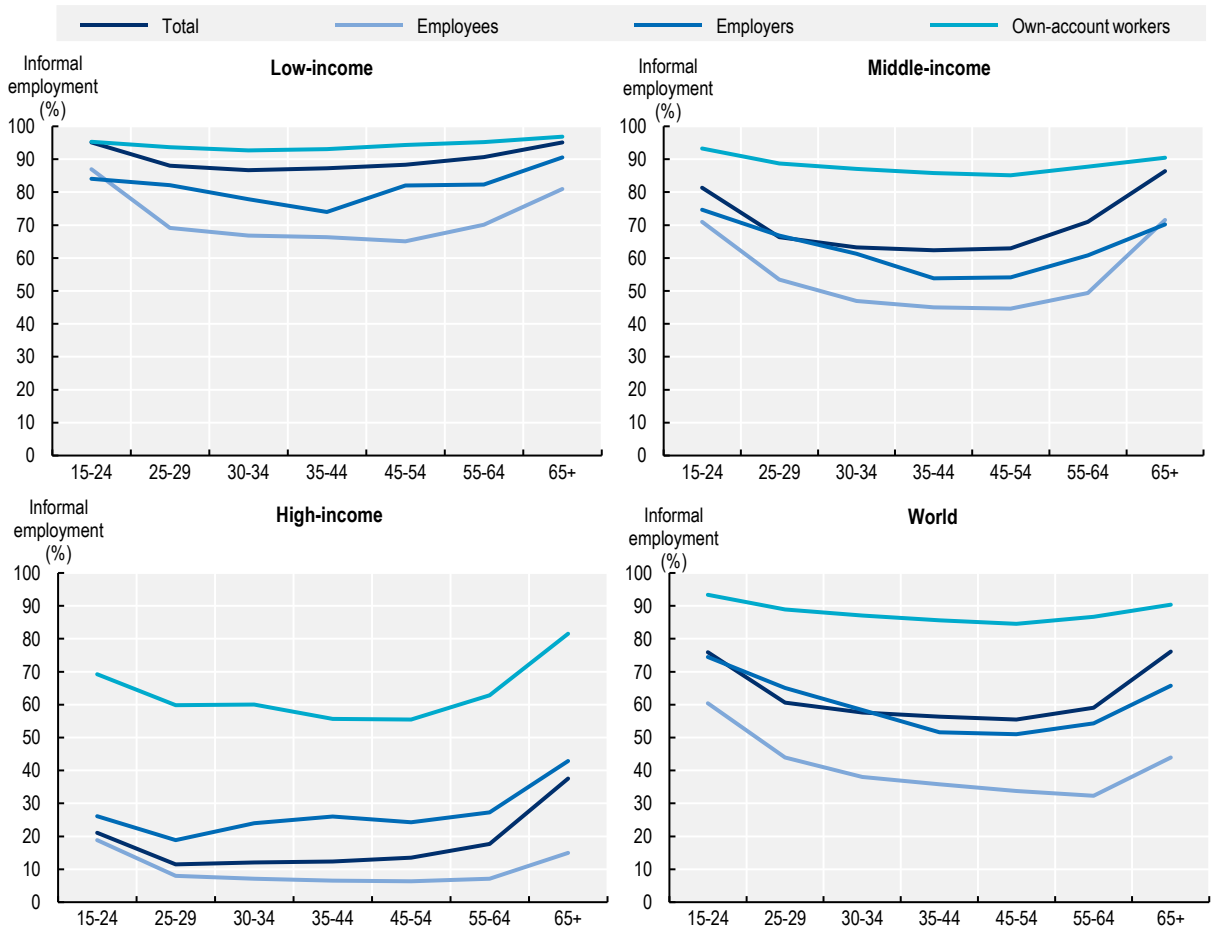
Young and older workers are more exposed to informality

There is substantial variation in the level of informal employment over the life cycle, with young and older workers disproportionately affected. Globally, more than three-quarters of young and older workers are in informal employment, compared with 55.1% of those aged 25-64. When employed, young people are

concentrated in types of work that make them particularly susceptible to income and job losses during a crisis. In 2019, 75.9%, or 429.7 million of the world's young workers were in informal employment. This implies that some 325 million young people are in informal employment worldwide, of which more than one-half are living in sub-Saharan Africa or Southern Asia. The proportion of informal jobs held by young people rises to 95.1% in low-income countries and to 90.3% in lower-middle-income countries (Figure 2.18). It is the highest in Africa (94.8%), Asia and Pacific (81.9%) and the Arab States (81.3%).

Figure 2.18. Informal employment rates are highest for young and older workers

Informality age profile by employment status – world and country income groups (2019)



Note: Global and regional estimates based on data for 146 countries representing 92.6% of the world's employed population and on country data for the latest available year. Contributing family workers are in informal employment, independently of the formal or informal nature of economic units and of age.
Source: (ILO, 2023[3]).

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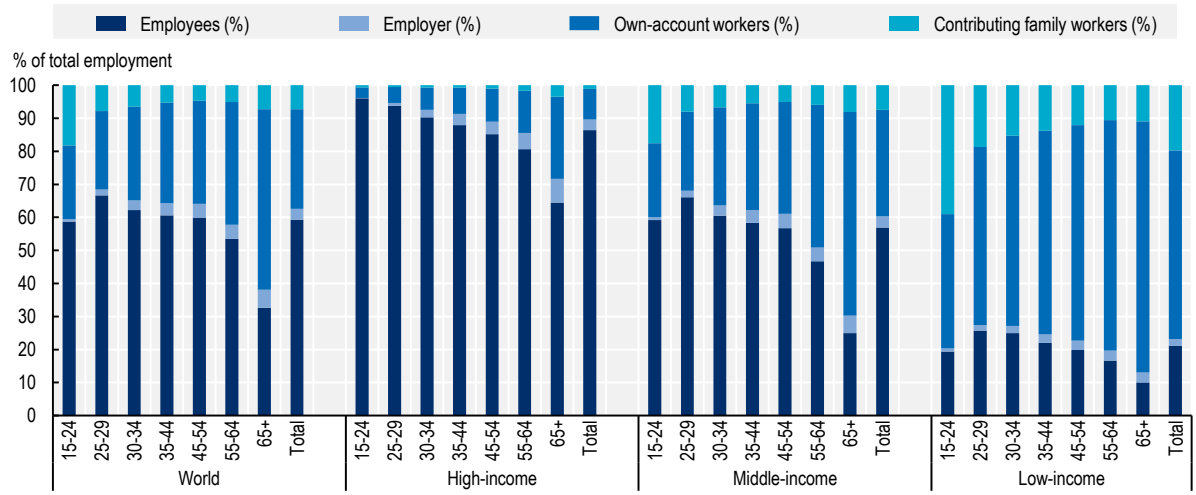
Figure 2.19. Distribution by employment status varies over the life cycle

Distribution of employment over the life cycle, by employment status (2019)



Note: Global and regional estimates based on data for 146 countries representing 92.6% of the world's employed population and on country data for the latest available year. Contributing family workers are in informal employment, independently of formal or informal nature of economic units and of age.
Source: (ILO, 2023[3]).

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The overall share of informal employment varies over the life cycle. The share of informal employment held by a given age group decreases rapidly with age, but then increases at older ages, notably after statutory retirement age (Figure 2.18). However, these rates also vary by employment status: rates of informality reach their lowest levels for employees and, to some extent, employers, whereas they remain almost flat and greater than 80% for own-account workers. These trends are intertwined (Figure 2.19); the youngest and oldest workers are over-represented in employment statuses at the highest risk of informality. For example, a disproportionate share of young people comprises contributing family workers, while own-account workers constitute a disproportionate share of older workers (aged 65+).

Trends in informality by age and employment status also vary by level of economic development. In developing countries, informality is largely influenced by own-account employment, which represents the majority of employment, and tends to offer limited opportunities for transition to formal employment; employee and employer categories tend to have more opportunities for formalisation. In emerging countries, there are also more opportunities among employees and employers as they age. By contrast, similar to the trend observed in developing countries, own-account workers' prospects for formalisation are more limited, in the absence of dedicated interventions or changes to the macroeconomic context. In developed countries, formality among employees is high overall. Among employers and own-account workers, there is also a clear transition towards formality that increases with age and experience (at least until retirement age) (Chacaltana, Bonnet and Leung, 2021[41]).

Not surprisingly, given the higher risk of informality among young and older workers, they were also disproportionately affected by job losses during the pandemic. By the second quarter of 2020, young people were among the most affected in all the countries under review (Figure 2.20), except the Dominican Republic; in most selected countries, young people in informal employment were affected even more than their formal counterparts. The COVID-19 crisis affected (and continues to affect) young people in three

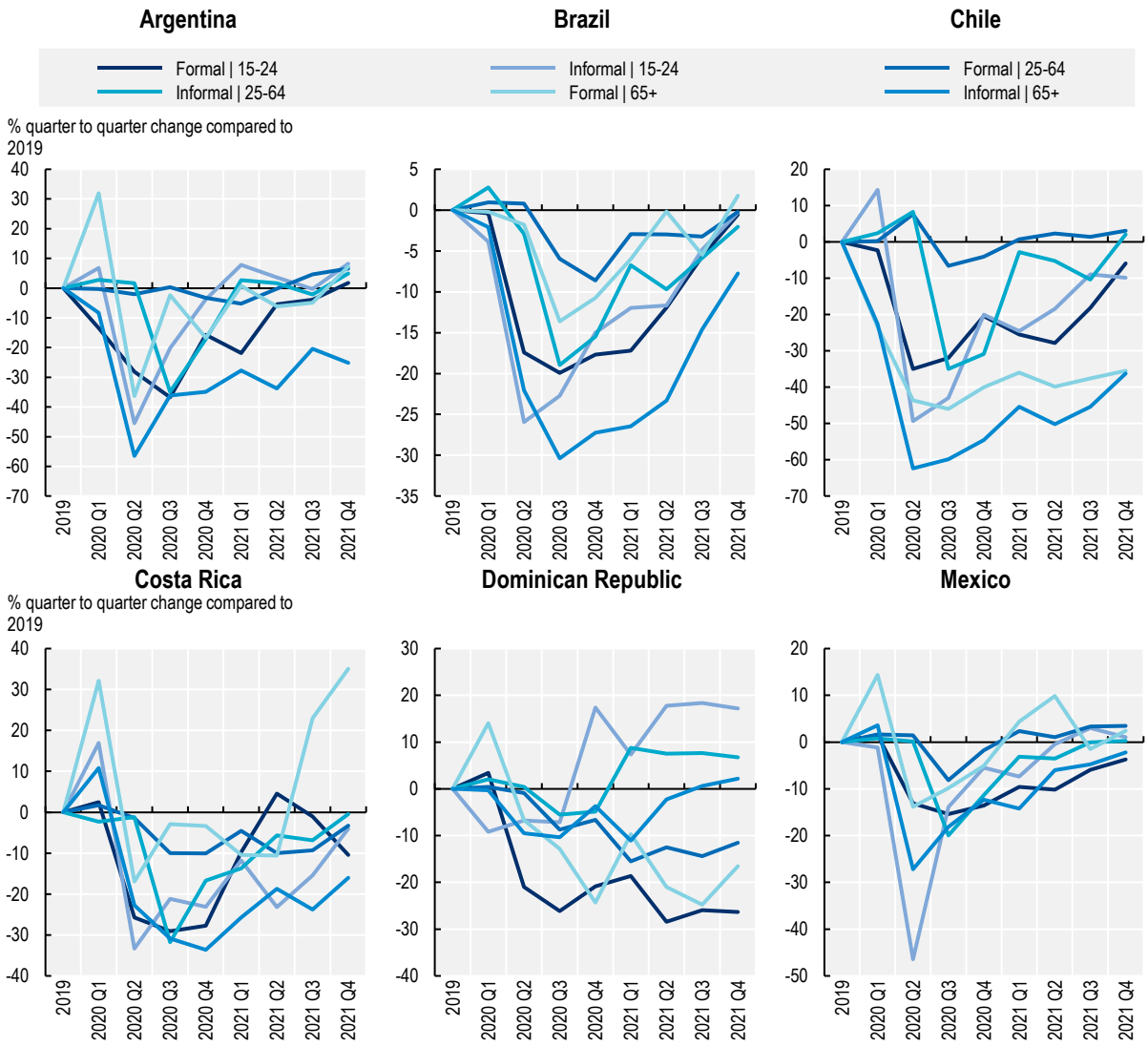
ways: (1) disruptions to education and training, reducing potential employment opportunities and earnings in the future (ILO-UNESCO-World Bank, 2020[42]); (2) massive job losses for those in employment, and (3) the emergence of greater obstacles to finding work, (re-)entering the labour market and trying to transition to better jobs. It is estimated that 178 million young workers around the world – more than four in ten young people employed globally – were working in hard-hit sectors when the COVID-19 crisis began. Already before the crisis, three in four young workers had informal jobs, implying that they lacked the requisite social and labour protection that would enable them to attenuate the impact of the pandemic-induced crisis on their incomes. In addition, more than 267 million young people were not in employment, education or training (NEET), including almost 68 million unemployed young people (ILO, 2020[13]).

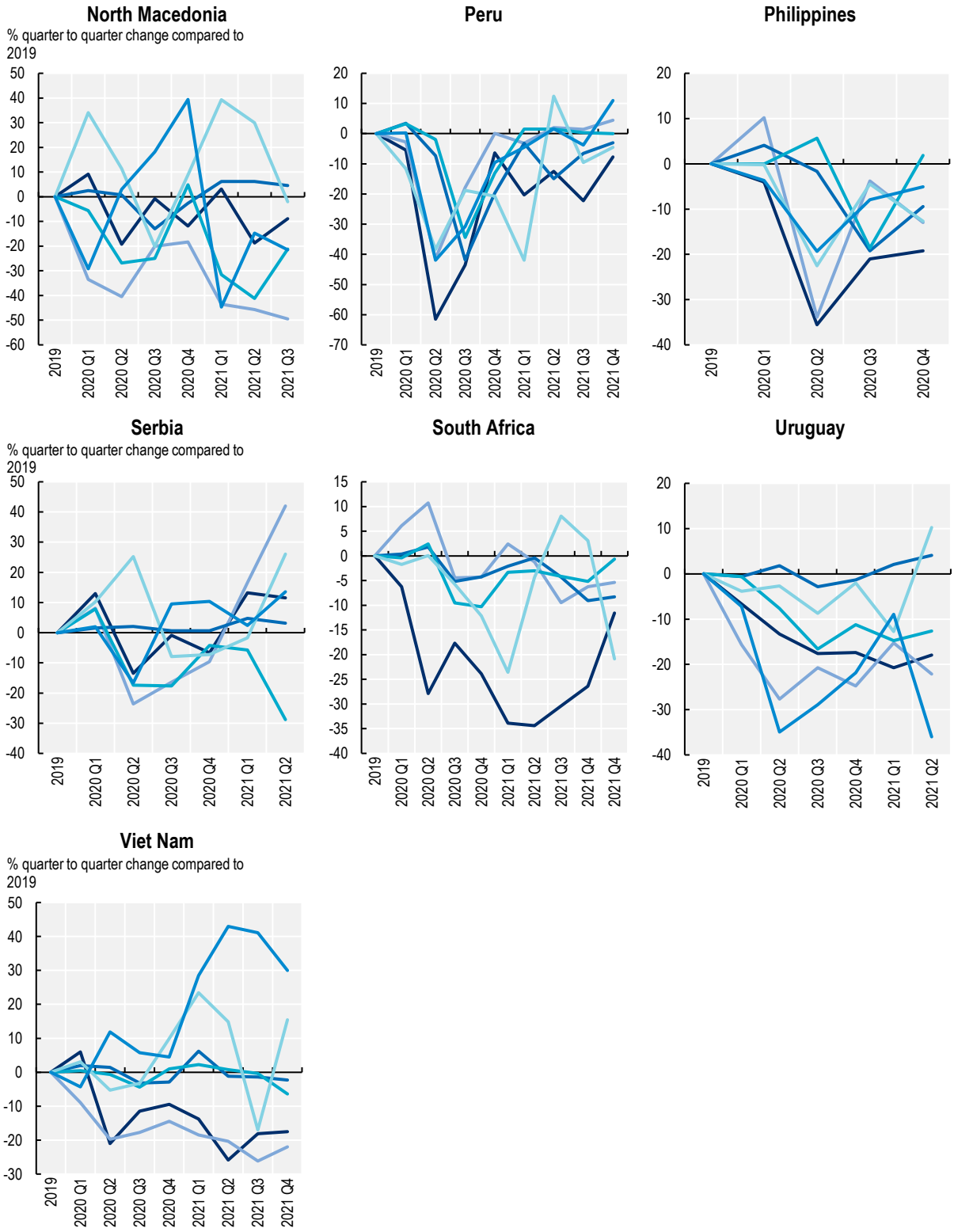
The subsequent stages of the crisis reveal trends which varied by country for young and older workers. In Argentina, Brazil, Mexico and Peru, both young and older workers in informal employment faced the greatest job losses at the height of the crisis. While the return to employment was relatively rapid among young people, reaching 2019 levels by 2021, the number of informal jobs for older workers remained well below pre-crisis levels, suggesting that some of them, discouraged, dropped out of the labour market. Drop-out and unemployment also affected young people in some countries, resulting in lower employment levels among young people at the end of 2021 in Costa Rica, Northern Macedonia, South Africa, Uruguay, and Viet Nam. In the latter three countries, this encompassed both informal and formal youth employment.

Finally, youth employment trends in the Dominican Republic, and to a lesser extent in Mexico, Peru, the Philippines, and Serbia, seem to indicate a transition towards informalisation of the labour market for young people. In these countries the growth of informal jobs exceeded that of formal jobs and, in addition, the absolute number of informal jobs surpassed that in 2019.

Figure 2.20. Evolution of informal and formal employment by age group in selected countries

Reference quarters in 2019 = 1





Source: Authors' compilation based on (ILO, 2020[13]; ILO, 2022[18]; Barford, Coutts and Sahai, 2021[43]).

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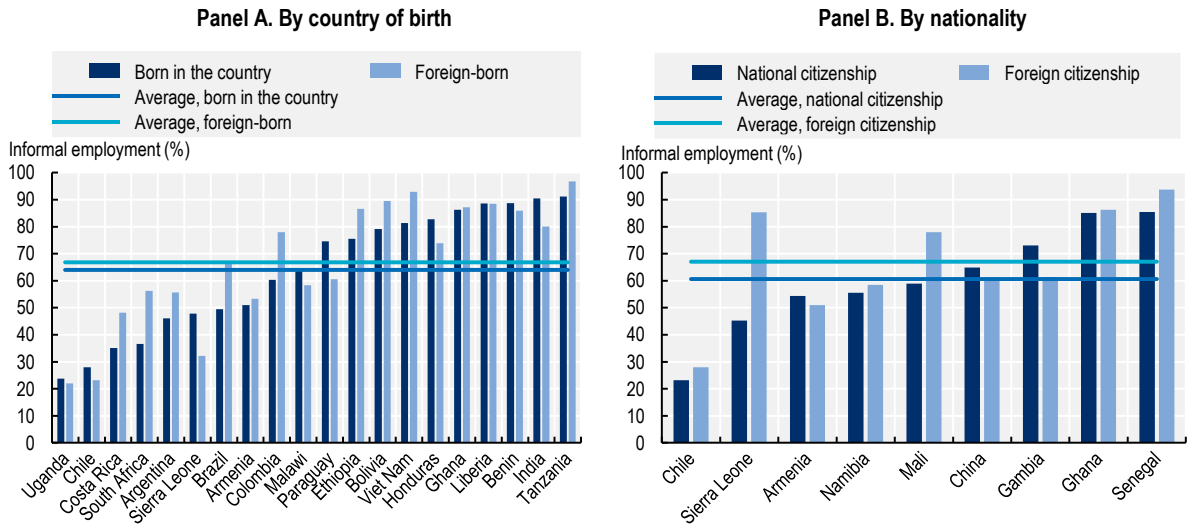
Informal employment is a greater source of employment for immigrants as compared to non-immigrants

The total number of international migrants increased by over 50% between 1990 and 2022, although they continue to constitute a tiny proportion of the world's population. In 2018, there were 164 million migrant workers worldwide (ILO, 2021[44]). The vast majority of them (67.9%) were living in high-income countries, 18.5% in upper middle-income countries, 10.1% in lower middle-income countries and 3.4% in low-income countries. Migrant workers constitute 18.5% of the workforce of high-income countries, but only 1.4-2.2% in lower-income countries.

Even if the situation differs across countries and their migration histories, migrant workers are typically more likely to be employed in informal jobs than workers in native-born populations. In developing countries with available data (Figure 2.21), the average incidence of informal employment is three percentage points lower for native-born workers than for foreign-born workers; it is seven percentage points lower for workers who are citizens of the country in which they live than for non-citizen workers. In some countries, such as Argentina, Bolivia, Brazil, Colombia, Costa Rica, Ethiopia, and South Africa, there is a more than a 10 percentage point difference in the informality rate among native-born and foreign-born workers. This is likely to reflect a relatively higher level of development in these countries than in neighbouring ones; it is also likely to reflect the higher share of migrant workers and refugees in the total pool of foreign-born workers than in other countries where the pool of foreign-born workers is more likely to be composed of family members.

Figure 2.21. Informality rates, by types of immigration status



Note: There are two complementary ways to infer a migration status of an individual. One is to look at whether individuals are native- or foreign-born, another is to look at their nationality or citizenship. Often, household data contain questions about only one aspect, but not the other. Cross-country disparities by nationality reflect not only the share of persons who are most likely to be foreign-born, but also the country-specific laws that allow acceding to citizenship and the working rights that are often associated with it.
Source: (OECD, 2021[45]), available at: https://www.oecd.org/dev/key-indicators-informality-individuals-household-kiibih.htm.

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Immigrants are more likely to be found in informal jobs for several reasons (ILO, 2016[46]; OECD/ILO, 2018[47]; ILO, forthcoming[48]). First, migrants who come as workers are often employed in seasonal jobs which are particularly prone to informality. Second, they are likely to be employed in sectors that feature a

higher share of informality, including agriculture, construction, or care and cleaning. Third, for migrant workers who crossed borders outside of formal migration work schemes, there is a great pressure to find work quickly to repay migration costs or remit money home, all while paying for their housing in the destination country – housing that they typically do not own. This increases the pressure to find any job available, including informal employment. For a particular type of migrants – refugees – the laws of the receiving countries often do not allow them to work, at least not immediately, which means that the only way to complement their income is often through informal jobs. Finally, there are also issues of work permits, language, skill transferability and discrimination which make it all the more difficult to find formal jobs in markets where formal jobs are already tight. In developing countries and certain sectors, formal jobs may mainly be reserved for those migrants who arrive with formal visa and work arrangements already in place.

Russia's war of aggression against Ukraine which has been waging since February 2022 is likely to increase the incidence of informal employment in Ukraine and in countries receiving Ukrainian refugees and lately also for Russians fleeing mobilisation.

The household perspective remains key to better understanding vulnerability in the informal economy

As highlighted in the OECD/ILO report (OECD/ILO, 2019[49]), a more detailed insight into the well-being consequences of informality can be obtained if not only the individual dimension but also the household dimension of informality is considered. A household perspective on informality enables us to understand how the informal status of its working members affects other households' members. This in turn enables us to assess the extent to which informal workers' vulnerability is passed on to their dependants. Conversely, the household perspective enables a better understanding of how varying degrees of formality can ensure better protection of other household members, and determine whether there is scope for protecting them through formalisation of the working adults.

If several members of a household are employed differently – formally or informally – households with more than one employed member may have varying levels of informality.

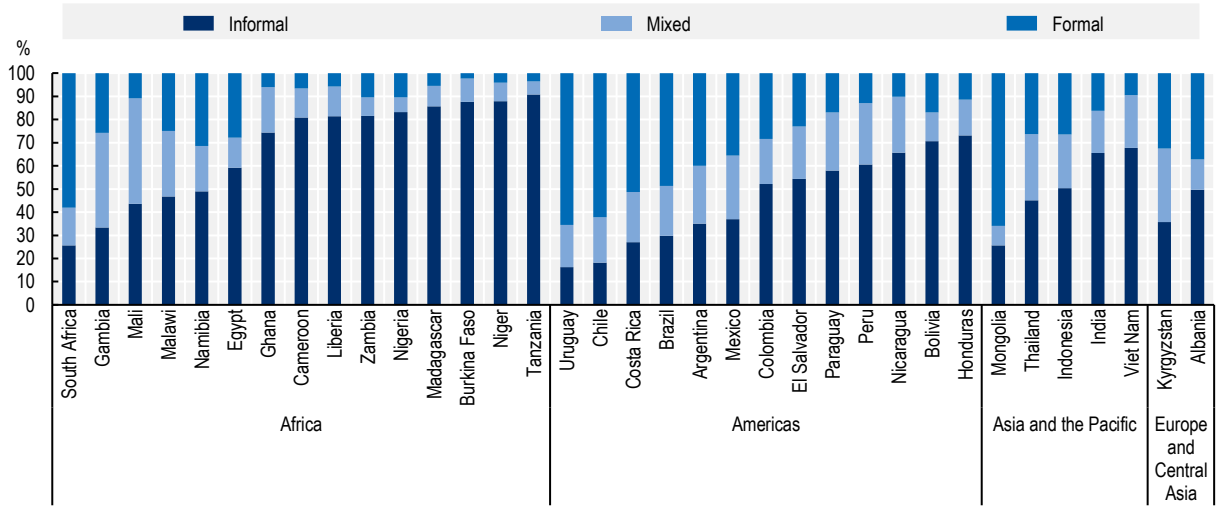
Formally employed workers are more likely than informal workers to be entitled to labour-based social protection. Formal employees have the right to employment-based benefits, such as paid sick leave and annual leave, retirement pensions, and in some countries where such benefit exists and depending on contract modalities, access to unemployment benefits. They also enjoy protection by labour laws, such as occupational safety, standard working hours, and minimum wages where these legal provisions exist. In turn, formal independent workers usually benefit from advantages associated with the legal recognition of their activity, including better income security.

Some of these benefits can protect dependents of formally employed household members either directly – such as by entitling them to, for instance, to medical insurance – or indirectly, through a spillover effect of more evenly spread incomes, lower risks of health and income shocks, and lower cumulated employment-related fatigue. During the pandemic, children of formally working parents also often benefitted from the fact that their formally employed parents had more opportunities to telework within reasonable working hours, thus also having the possibility of dedicating time resources to child education when schools were closed. All of these reasons combined provide a strong rationale for going beyond individual circumstances and for monitoring household-based indicators of informality.

On the eve of the pandemic, in 26 out of 37 developing countries with available data (Figure 2.22), the distribution of the overall population was dominated by completely informal households (i.e. with all working members employed informally). Mixed households were dominant in two countries only: the Gambia and Mali. The degree of informality of households varied across countries and regions was linked to the overall

rate of informality in an economy: it was highest in countries where overall informality was also high. Most of the households with all formally employed members were found in Latin America; and apart from there was only found in South Africa and Mongolia. In contrast, most of the households with all informally employed members were found in Africa: with up to 91% of the population living in households with all informally employed members in Tanzania; the comparable figure in Niger and Burkina Faso was 88%, and in Madagascar 86%. The disproportionate effects of the pandemic on informal workers is likely to have changed these distributions.

Figure 2.22. Distribution of overall population, by degree of informality of households (circa 2019)



Note: Includes all sampled households with at least one worker. Mixed households always have at least two workers.
Source: (OECD, 2021[45]), available at: https://www.oecd.org/dev/key-indicators-informality-individuals-household-kiibih.htm.

StatLink https://stat.link/l3re0p

Key policy messages

Formalisation is not an objective in itself but is a necessary condition for ensuring decent work, poverty reduction and greater equality among people. It is also a condition for fairer competition between more productive and sustainable enterprises. Formalisation also benefits society as a whole because it enhances government scope of action, notably by increasing public revenue and strengthening the rule of law. In so doing, it also contributes to building fairer societies by distributing rights and obligations among its members more equitably. This is a necessary condition, but is insufficient when transition to formal jobs does not translate into a transition to decent jobs. This chapter presented evidence on recent trends in informality and showed that it is a pervasive characteristic of labour markets across the world. While it represents the majority of employment in low- and middle-income countries, it represents about one-fifth of employment in high-income countries.

The chapter also presented evidence on the differential impact that the pandemic-induced crisis had on the informal economy. While at the beginning of the pandemic informally employed workers disproportionately lost their jobs, cross-country trends diverged as countries normalised to living with COVID-19. In some countries, informal employment drove overall employment recovery, while in other countries it lagged formal employment recovery and even contributed to total employment losses. Going beyond trends in the number of jobs, the COVID-19 crisis has amply highlighted and exacerbated the

vulnerabilities and deprivations of informal workers and enterprises, including the lack of social protection. The impact has been most extreme for female workers and has reinforced gender disparities, including in the distribution of unpaid care.

Some characteristics related to employment conditions and enterprises make workers more susceptible to informal employment. Own-account workers are most likely to be informally employed and constitute the largest share of informal employment globally; the majority of digital platform workers (see Chapter 5) and subcontracted workers employed in the lower tiers of supply chains (see Chapter 4) fall into this category. Other non-standard forms of employment, such as temporary employment, are also over-represented among informal jobs. Small enterprises, as well as agriculture and industry, employ a disproportionate share of informal workers. Furthermore, certain groups of individuals, such as young workers and older workers (aged 65+) are also more likely to work informally.

Widespread informality is often the result of the inability of the economy to create formal quality jobs. Moreover, it is a symptom of the inability of institutions to deliver and improve people's lives. It is also the symptom of the need for a renewed social contract built on trust, inclusion, protection and participation of all workers, including those in the informal economy (as further discussed in Chapter 3). Cross-country differences in informality are indeed also a function of the multiplicity of institutions, social norms, cultures, and levels of economic development across the globe. These differences are equally reflected in the diversity of policy responses required to address informality, as identified through the International Labour Organization's (ILO's) Theory of Change on the transition from the formal to the informal economy (ILO, 2021[15]) and the Transition from the Informal to the Formal Economy Recommendation, 2015 (No. 204).

Strategies to support transitions to formality should be grounded in an in-depth understanding of the informal economy and the impact of various policies within different groups of workers and forms of informality. The informal economy is not a monolith. There is a need to deepen the understanding of the factors and diversity of characteristics of the informal economy and it is important to consider the various levels of vulnerability (as well as protections) within the informal economy.

Integrated strategies aimed at addressing multiple drivers (institutional, policy and others) of informality work best. Decades of country experience have shown that multiple strategies can be applied to facilitate the transition to formality, including policies and measures that affect the environment/context, policies that affect the transversal drivers of informality, policies targeting specific sectors, technology choices, categories of enterprises or groups of workers, and types of informality. Effective formalisation strategies combine interventions to increase the ability of the formal economy to create decent work opportunities to absorb workers and economic units currently in the informal economy; and interventions to strengthen incentives as well as the ability of people and enterprises to enter the formal economy, including by increasing employability. This two-way logic presupposes actions at two levels: at the level of workers and enterprises in the informal economy, and also at the level of the political, policy and institutional environment. Actions at the two levels should be designed with the consultation and participation of informal economy actors (through organisation-building, voice and representation).

In this context, social protection policies have a key role to play. They should be developed with the objective of increasing employability and facilitating the transition to the formal economy while benefitting from it. Better access to decent employment and higher levels of social protection through contributory schemes increase domestic resources, including for the provision of basic social protection, which in turn constitutes an enabling factor for workers' transition to formality.

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Notes

[1] Unfortunately, due to the lack of large time-series data on informality, there is still little empirical evidence on this relationship, with some contrasted results depending on studies and contexts (Chacaltana, Bonnet and Garcia, 2022[52]). (Kucera and Xenogiani, 2009[52]) correlate GDP and share of non-agricultural informal employment and conclude that, "at least in the medium term, economic growth does not necessarily lead to a fall in informal employment". (Jütting and de Laiglesia, 2009[52]) present data by region over three decades from 1975 to 2007, for selected countries in Latin America and South and East Asia and conclude that, over this period, growth was accompanied by increasing, not falling, non-agricultural informal employment. Wu and Schneider use data from 158 countries from 1996-2015 and estimates of the shadow economy suggest that the relationship between the shadow economy and GDP is non-linear and instead they propose a U-shaped relationship. The implications if this non linearity, according to the authors, is that the shadow economy is able to coexist with different levels of development and does not disappear in the long term (Deléchat and Medina, 2021[4]).

[2] To ensure comparability across countries, and to avoid the gradual but not universal adoption of the more restrictive definition of employment (19th ICLS resolution) (ILO, 2013[7]) the global and regional estimates presented in this chapter follow the old definition of employment that notably include subsistence agriculture.

[3] Peru is one of the few countries with available data where informalisation has occurred since the start of the pandemic. The labour market has become more informalised as informal employment growth has exceeded formal employment growth throughout the period from mid-2020 to end-2021.

[4] Non-standard forms of employment comprise four employment arrangements that deviate from the "standard employment relationship" (i.e. other than full time, indefinite and part of a subordinate relationship between an employee and an employer) (ILO, 2016[19]).

[5] For example, in 2015 Brazil adopted a law that required employers to register domestic workers with social security schemes only if they worked for more than two days a week. In the Netherlands, households that employ domestic workers for fewer than four days a week are not required to pay taxes on wages or social insurance premiums, which means that domestic workers are excluded from social insurance (ILO, 2021[21]).

3 Informal employment and the social contract

This chapter proposes a holistic approach to understanding informality through the prism of the social contract. Social contracts have a procedural and a substantive dimension. The extent of informality in a given country may be linked to an underdeveloped procedural dimension, a weak substantive dimension, a misalignment between the two, or all of these situations at once. Linkages between informality and the substantive dimension are empirically shown by relating the level of corruption, mistrust in public institutions, and dissatisfaction with various public services to the extent of informality among different types of workers. Informality is also shown to positively correlate with lower public spending on public goods and services and with poorer social outcomes. The social contract approach to informality can unify previous theories of exit and exclusion. As such, it offers a novel look at tools to tackle informal employment and the vulnerabilities of informal workers and their families.

Informality is intimately linked to the notion of the social contract

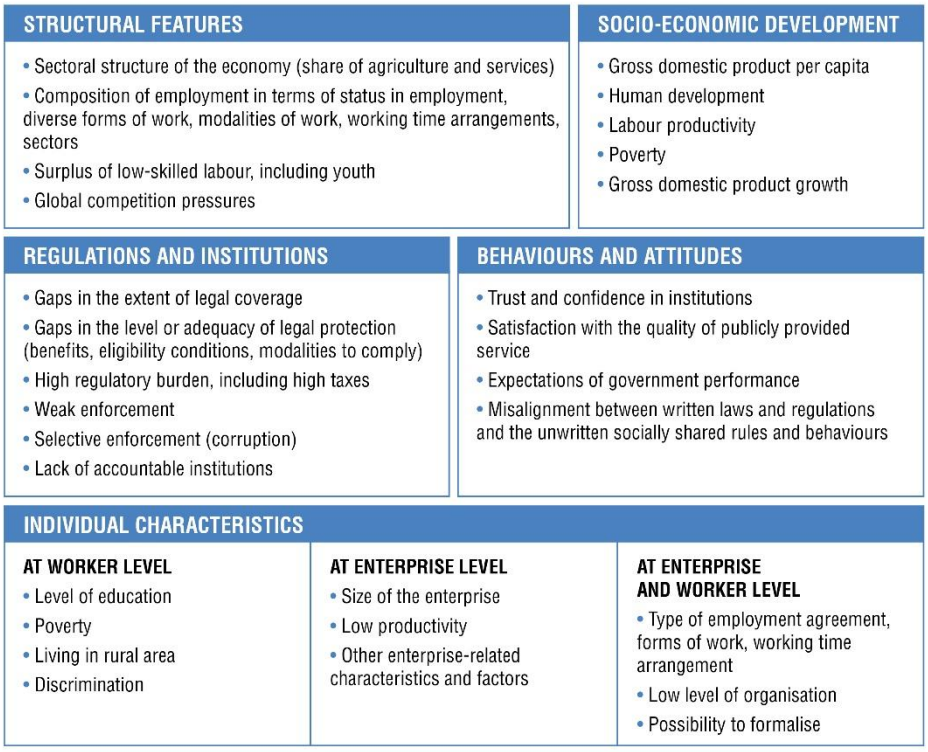
Informality is a complex, dynamic phenomenon, influenced by many factors (Figure 3.1). These include structural features of the economy; the level of socio-economic development; regulations and institutions; behaviours and attitudes; and drivers at the individual and enterprise level (OECD, 2009[1]; OECD/ILO, 2019[2]; IMF, 2021[3]; World Bank Group, 2021[4]). The linkages between structural, socio-economic and legal factors have been widely documented [see for instance (OECD/ILO, 2019[2])]; it has been shown that the relative importance of these factors varies across countries. Also, the importance of some factors may not hold in the dynamics within countries. For example, the decline of poverty, or long-term growth within countries is not always associated with the reduction of informality.

Notwithstanding these factors, informality is increasingly regarded as a manifestation of a weak or dysfunctional social contract (OECD, 2018[5]). The social contract is an implicit social agreement that takes the form of a broad set of social norms, conventions and mutual expectations from various actors in a society. It reflects a common understanding of how to distribute power and resources between such actors – citizens, the state, workers, and enterprises – in order to achieve common goals (ILO, 2016[6]). This implicit common understanding also provides the guiding principles for building political institutions and social and economic policies (UNRISD, 2022[7]).

The social contract has both substantive and procedural dimensions (ILO, 2016[6]).[1] The substantive dimension pertains to the manner by which common goals, such as equity, fairness, freedom and security, and eventually social justice, are framed and prioritised in a society. As such, it is an implicit pact between the state and the citizens, characterised by various rights and obligations regarding what individuals and different socio-economic groups give to and receive from the state (Shafik, 2021[8]). The procedural dimension pertains to the legal frameworks, institutions and procedures that help to make this implicit pact explicit, to legitimise the common goals, and to spell out the common understanding of mutual rights and obligations.

The question of formality arises only in relation to the existing laws and regulations, as well as their implementation in practice, with the protection, advantages and obligations that this entails. Informality is a phenomenon encompassing workers and enterprises that are either not covered by formal legal frameworks (procedural dimension), are insufficiently covered, or are not complying with them (for various reasons, including the lack of possibilities for doing so or the disagreement with the substantive dimension of the social contract). As such, informality is a symptom that the social contract is not functional for all citizens, or at least that its procedural dimension does not properly reflect the implicit substantial dimension or is simply lacking.

Figure 3.1. Drivers of informality on macro- and microeconomic levels



Source: Own elaboration based on (IMF, 2021[3]; OECD/ILO, 2019[2]; World Bank Group, 2021[4]) and literature review.

In some settings, informality is the norm as part of a social contract that has only a recent or an underdeveloped procedural dimension

The nature of social contracts, their strength, and their relevance differ widely across countries. Important differences are observed across regions of the world, across stages of economic and social development, and across democratic and authoritarian countries. But even in the poorest or in authoritarian countries, social contracts presuppose that certain socio-economic benefits exist, at least for some population groups, in return for political support (Hinnebusch, 2020[9]).

In some of the least developed countries, the logic for informal employment in relation to the social contract is profoundly different as compared with richer and more developed countries. In many instances, the procedural dimension of the social contract, which takes form of legal arrangements and frameworks, is not yet developed enough to reach out to all citizens or to be relevant to all of them, especially where castes or tribal traditions are still strong. It may not cover some specific sectors (such as agriculture or waste picking) or some specific workers (such as traditional farmers, fishers, indigenous communities, or domestic workers). When legal frameworks exist, governments do not always have the capacity to enforce them. Governments may also lack the infrastructure and the capacity to deliver the benefits of adherence to the formal social contract (such as education and health infrastructure), or the qualified specialists to deliver the services.

But this does not mean that no social contract exists in such settings. The substantive dimension may exist and function well, taking the form of social norms and arrangements at the community, neighbourhood or

village level, and is often related to the kinship. Often, such arrangements also act as a substitute for the poor or nonexistent provision of public services and goods. In these settings, informal employment is a social norm because labour markets are governed by implicit rather than explicit rules and behaviours. Work is often exchanged against other services delivered through non-state, intra-communal channels. This includes the informal provision of childcare and healing, as well as informal access to production means and informal skill acquisition and learning. In these settings, workers may also place less value on the "formalisation" prospects (adherence to the procedural dimension of the social contract) because the relative benefits from such formalisation are low. Unlike in more developed countries, formalisation may not necessarily give individuals an increased capacity to seize opportunities or to participate in and contribute to social and economic development. Workers may also perceive little value in their individual formalisation because throughout their work activities they are maximising collective rather than individual informal social protection, such as taking care of children or sick elderly people in their family or the neighbourhood.

From a policy perspective, this means that standard approaches to the individual formalisation of workers and enterprises in these settings may be neither appropriate nor attractive, since this would mean that newly formalised workers or enterprises would no longer fit into their informal system of aids and protections. In such contexts, broader collective solutions to formalisation are needed. For example, recognising the activity of waste pickers in developing countries as an occupation can help include them in cities' waste management systems, and thus not only serve as a one-off formalisation of individual workers but also change their collective relationship with the state and state-provided protections (Parra, 2020[10]).

In some settings, informality also persists because there is a misalignment between the procedural dimension (formal institutions) and the substantive norms of the society, as well as between institutional responses to the true needs of workers, their families, and citizens at large (Gërxhani, 2004[11]; Williams, 2015[12]). This misalignment may be historic, reflecting colonial legacies. It may also reflect the fact that the state is not catching up with the challenges that the evolving world presents – as is the case in countries undergoing substantial socio-economic and political transformation. This misalignment further justifies the existence of the informal economy, and legitimises informal practices in the eyes of the community, even if they are not seen as legitimate in relation to the state (Van Schendel and Abraham, 2005[13]).

In these settings, one of the ways to address informality is to ensure that the procedural dimension adequately reflects the substantive one. The most effective way to achieve this is through social dialogue involving all parties, including informal workers, in order to find the right solutions for restoring an adequate procedural dimension of the social contract.

In other settings, informality may be a symptom of the weakening of the procedural and substantive dimensions of the social contract

The development rhetoric since the 1960s led to the belief that economic development would rhyme with the improvement of social contracts in terms of both the substantive and procedural dimensions. As countries became more developed, they would also enact better laws and regulations, as well as provide better services from the state, reflecting the needs of all citizens.

However, this has not happened uniformly. Moreover, various economic, social and political challenges can present both opportunities and challenges to the effectiveness and relevance of both the procedural and substantive dimensions of a social contract. Prior to 2020, social contracts around the world had already been challenged by a variety of idiosyncratic factors, including rising inequality, heightened income insecurity, lower social mobility, and the weakening of social dialogue and institutions where previously they had been stronger. Among others, long-term structural factors such as globalisation and technological change (including digitalisation) were considered important game-changers for social contracts. At the

same time, there has been a stagnation (and sometimes an increase) of informality in several parts of the world, coupled with a growing resentment that the social contract does not work well for all citizens. The latter has manifested in a persistent, and often growing, dissatisfaction with public services, perceptions of corruption, and low confidence in public institutions.

For example, in Latin America and the Caribbean (LAC), according to Gallup surveys, public satisfaction with healthcare declined from 55% in 2007 to 49% in 2018, while satisfaction with the education system and schools dropped from 65% in 2007 to 53% in 2020 (OECD et al., 2021[14]; OECD, 2021[15]). In Africa, more people were dissatisfied than were satisfied with access to quality healthcare, public transport, roads and housing in the 2010-es (AfDB/OECD/UNDP, 2017[16]). Southeast Asia is the only region where the level of satisfaction with healthcare has increased over the first two decades of the 21st century. There, an average of 79% of respondents were satisfied with healthcare provision and 83% were satisfied with the education system and schools around 2018 (OECD/ADB, 2019[17]).

The three years since early 2020 have presented multiple new and cascading challenges – from the COVID-19 crisis, to the accelerated consequences of climate change, to the world-felt consequences of Russia's war of aggression against Ukraine – which have considerably eroded social contracts in many parts of the world. In many settings, the COVID-19 crisis underscored the extent to which social contracts were weak or even broken, often weakening them further (UNRISD, 2022[7]; Plagerson, Alfers and Chen, 2022[18]; Berkhout et al., 2021[19]). Strong feelings of exclusion and unequal treatment regarding the measures adopted during the COVID-19 crisis, especially as part of immediate responses, contributed to the feeling that social contracts do not work well for all citizens, and specifically for informal workers. Those in the informal economy felt "invisible" and left out (ILO, 2021[20]). Informal "essential" workers in many countries – those that allowed economies to run during the global pandemic and amidst the lockdowns – often resented social injustice as they did not feel sufficiently recognised (ILO, 2023[21]). The COVID-19 crisis also highlighted the massive economic costs of inadequate social protection (in terms of both coverage and access to good-quality services); the vulnerability of education and skills-provision systems and their financing; and the vulnerability of different actors to disruptions in global production, especially in global value chains built according to subcontracting models. In sum, the COVID-19 crisis highlighted the need to review and enhance the substantive dimension of social contracts in many countries.

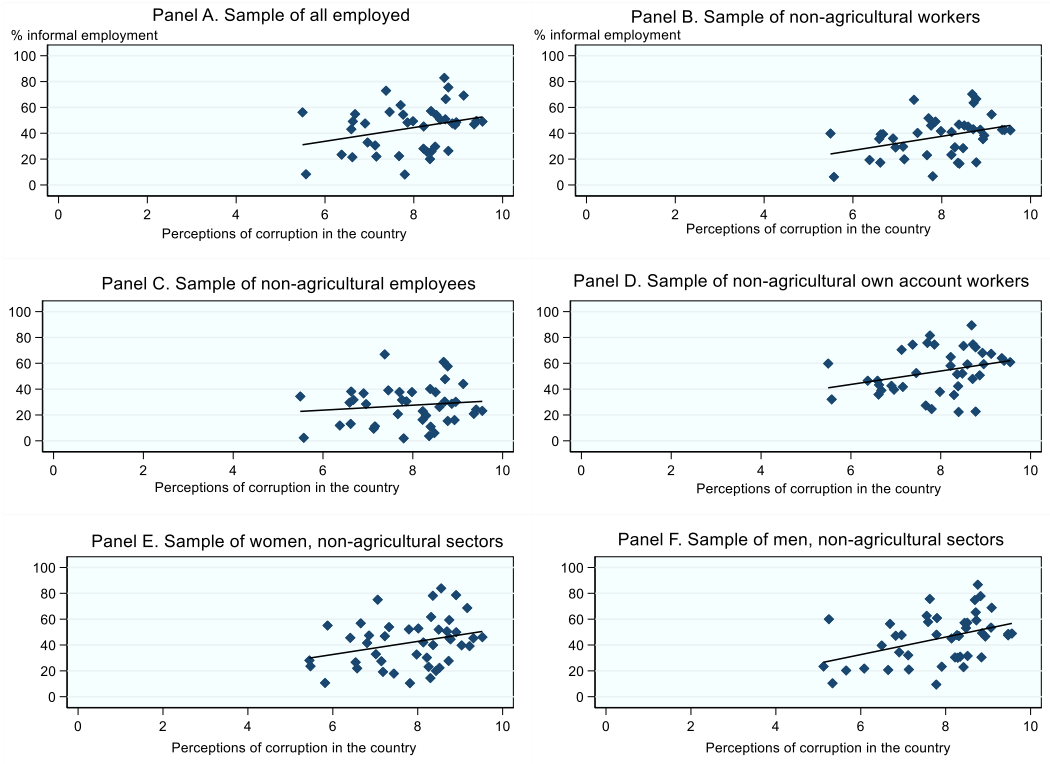
Persistent and growing informality goes hand in hand with corruption, mistrust in institutions and dissatisfaction with public services

The substantive dimension of the social contract is strong when the majority of citizens perceive that the pact with the state is reliable, beneficial for them, and fair (Shafik, 2021[8]). In such settings, individuals have a possibility to adhere to such social contracts and generally see value in doing so, by complying with the rules and regulations. A strong social contract between the state and its citizens is an essential condition for sustaining development over time (Bussolo et al., 2018[22]; OECD, 2011[23]). Conversely, the social contract is weak when most citizens see it as non-reliable, non-beneficial or unfair. The latter perception manifests in low satisfaction with access to and the quality of state-provided services, and low levels of trust and confidence in public institutions. Another key aspect of a strong social contract is the expectation that taxes and social security contributions are not misused. In other words, misuse of public funds and corruption weaken social contracts.

Indeed, several macroeconomic studies have also shown that informality is widespread when perceived corruption is high and when governance is poor (Buehn and Schneider, 2011[24]; Dreher and Schneider, 2009[25]; Dutta, Kar and Roy, 2013[26]; Friedman et al., 2000[27]; Schneider and Enste, 2000[28]), and when there is a lack of trust in public institutions (Iyanatul and Lapeyre, 2020[29]). That informality is one of the manifestations of the social contract has also been shown by linking informality to institutional quality (Schneider, 2010[30]); to taxes and political turnover (Elgin, 2013[31]); to direct democratic institutions (Teobaldelli and Schneider, 2013[32]); to political instability (Elbahnasawy, Ellis and Adom, 2016[33]); to the

business and political environments (Devine, 2021[34]); to tax morale (Alm and Torgler, 2006[35]; Torgler and Schneider, 2009[36]); or to several of these aspects at the same time (Torgler and Schneider, 2009[36]; Torgler and Schneider, 2007[37]).

Figure 3.2. Informality correlates positively with the perception of corruption



Note: Predicted values of informal employment (International Labour Organization (ILO) definition). Controls include seven geographical regions (sub-Saharan Africa; South Asia; North America; Middle East and North Africa (MENA); LAC; Europe and Central Asia; and East Asia and Pacific); gross domestic product (GDP) per capita, PPP constant 2017; income share held by the lowest-income 10% of the population; population growth; trade as a percentage of GDP; the Human Development Index (HDI); ease of doing business as of 2018; and political rights and civil liberties. Perception of corruption is computed as an average of individual responses to the question: "How much corruption is there in your country?" Answers ranged from 1 to 10, with 1 meaning "There is no corruption in my country" and 10 meaning "There is abundant corruption in my country". Then, averages were taken (by country) within subsamples of all workers (Panel A), non-agricultural workers (Panel B), non-agricultural employees (Panel C), non-agricultural self-employed workers (Panel D), women in non-agricultural work (Panel E), and men in non-agricultural work (Panel F). Informal employment: latest available data. The sample includes 34 countries (see Annex 3.A for the full list).

Source: For six measures of informal employment: (ILO, 2023[38]), *Women and Men in the Informal Economy: A Statistical Update*, https://ilostat.ilo.org/en/; for geographical regions, GDP per capita, population growth, and trade as a percentage of GDP: (World Bank, 2021[39]), *World Development Indicators* (database), www.data.worldbank.org/products/wdi; for ease of doing business: (World Bank, 2022[40]), *Doing Business Indicators* (database), www.doingbusiness.org; for political rights and civil liberties indices: (Freedom House, 2019[41]), *Freedom in the World* (database), freedomhouse.org/report/freedom-world; and for perception of corruption: own computations based on (World Values Survey, 2020[42]), *Wave 7* (database), worldvaluessurvey.org.

The majority of these studies were conducted at the macroeconomic level. These studies usually recognise that the causality may run both ways between informality, and perceptions of and attitudes towards institutions. However, these studies have been missing one key fact: that informal economies, as well as the informal workers that are part of them, are highly heterogeneous (OECD/ILO, 2019[2]; Plagerson, Alfers and Chen, 2022[18]). Indeed, an informal worker is not only characterised by their economic activity; they are also a citizen, a parent, a member of the household (which may have other informal or formal economy workers), and a member of the community. Individual informality status, as well as perceptions regarding

the social contract, can thus vary depending on these roles. Different individual characteristics, as well as other roles of the individual, can give a different perception of the relevance of different aspects of the social contract, and also determine the individual's informality status.

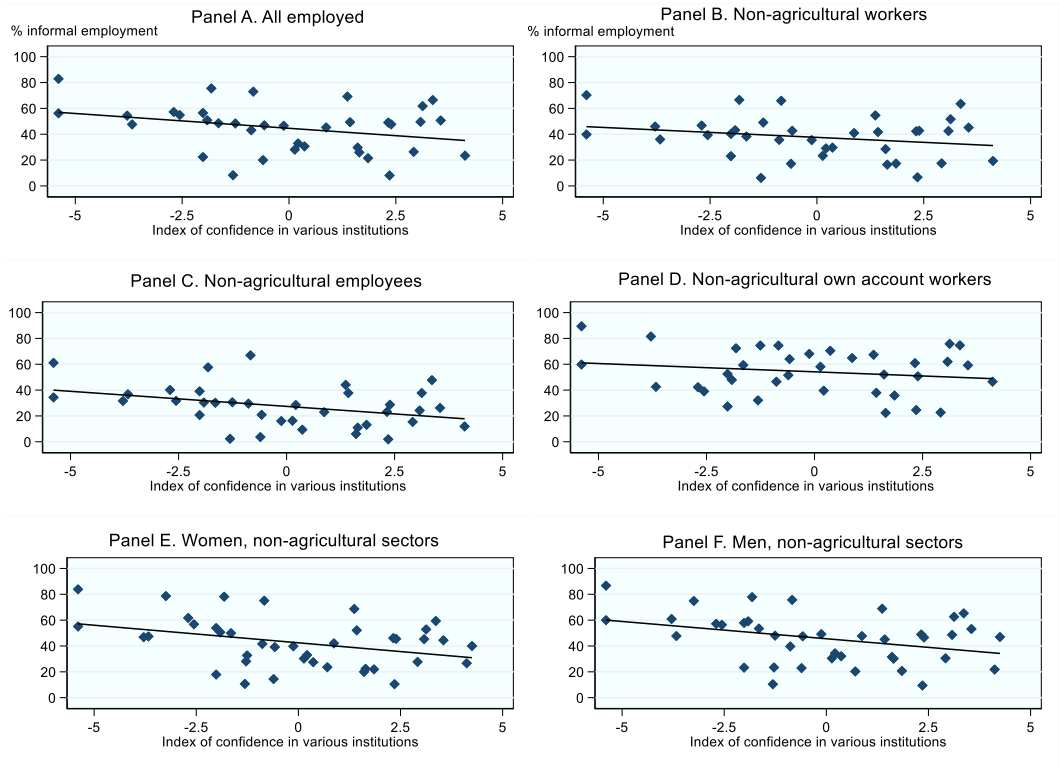
Accounting for this important heterogeneity means that informality and various aspects of the social contract should be examined within different heterogeneous groups. Figure 3.2 explores this heterogeneity. It includes shares of informality for all workers (Panel A), as well as separately for non-agricultural workers (Panel B), non-agricultural employees (Panel C), non-agricultural self-employed workers (Panel D), women in non-agricultural work (Panel E), and men in non-agricultural work (Panel F), and gives the averages of individual responses to the World Values Survey question: "How much corruption is there in your country?", computed within the same subsamples of workers in each country.

A positive correlation between informality and the perception of greater corruption is observed in each of these subsamples. This positive correlation is the strongest in the subsample of self-employed individuals and of men.

Similarly, informality is strongly negatively correlated with confidence in various institutions, including the armed forces, police, the justice system, the government, political parties, and parliament, as well as the press, labour unions, and the civil service (Figure 3.3). In particular, lack of confidence in the justice system and in the police have the strongest positive correlation with the share of informal employment. The correlation holds separately between the subsamples of men and of women, of employees and self-employed workers, and of all workers and non-agricultural workers.

Correlations at the macroeconomic level presented in Figure 3.2 and Figure 3.3 also hold at the individual level. Examples of this (which are available for a few selected countries) are presented in Box 3.1. Moreover, recent studies show that individual informality status not only correlates with a higher level of dissatisfaction with publicly provided services, but also that there is a causal relationship between these variables (Aleksynska and Wojcieszynski, 2022[43]). In other words, not only is it possible that lower confidence may lead to informality, but it also appears that informal workers are more likely to have lower confidence in institutions, and to have a lower level of satisfaction with publicly provided services. This further erodes the social contract from the point of view of those workers who were forced into informality rather than choosing it.

Figure 3.3. Informality correlates negatively with confidence in institutions



Note: Predicted values of informal employment. Controls include seven geographical regions (sub-Saharan Africa; South Asia; North America; MENA; LAC; Europe and Central Asia; and East Asia and Pacific); GDP per capita, PPP constant 2017; income share held by the lowest-income 10% of the population; population growth; trade as a percentage of GDP; the HDI; ease of doing business as of 2018; and political rights and civil liberties. Index of the confidence in institutions is first computed on an individual level using the principal component analysis (PCA) procedure, and extracting the first principal component. The PCA is applied to nine questions, asking about the degree of confidence the person has in: armed forces, the press, the labour unions, the police, the justice system, the government, political parties, parliament, and the civil service. The answers are measured on the scale from 1 to 4, where 1 refers to no confidence at all, and 4 refers to full confidence. Then, averages were taken (by country) within subsamples of all workers (Panel A), non-agricultural workers (Panel B), non-agricultural employees (Panel C), non-agricultural self-employed workers (Panel D), women in non-agricultural work (Panel E), and men in non-agricultural work (Panel F). The sample includes 34 countries (see Annex 3.A for the full list).

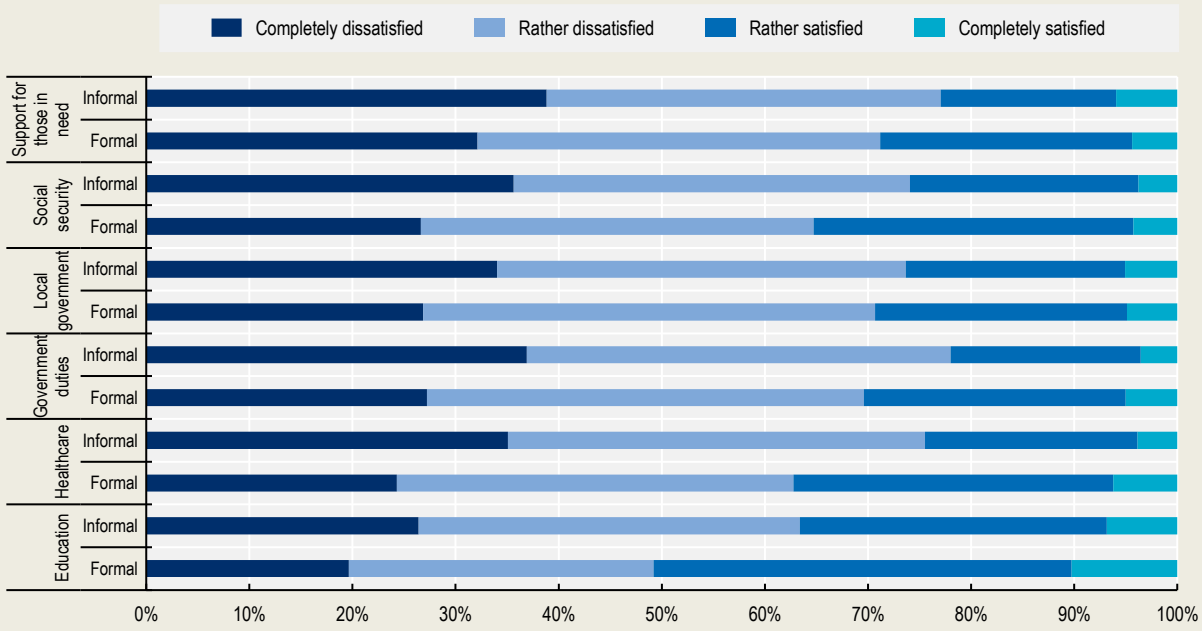
Source: For six measures of informal employment: (ILO, 2023[38]), *Women and Men in the Informal Economy: A Statistical Update*, https://ilostat.ilo.org/en/; for geographical regions, GDP per capita, population growth, and trade as a percentage of GDP: (World Bank, 2021[39]), *World Development Indicators* (database), www.data.worldbank.org/products/wdi; for ease of doing business: (World Bank, 2022[40]), *Doing Business Indicators* (database), www.doingbusiness.org; for political rights and civil liberties indices: (Freedom House, 2019[41]), *Freedom in the World* (database), freedomhouse.org/report/freedom-world; and for confidence in institutions: own computations based on (World Values Survey, 2020[42]), *Wave 7* (database), worldvaluessurvey.org.

Box 3.1. Weak social contract from an individual's perspective

The notion that a greater share of informality is a sign of a dysfunctional social contract can be better understood through a micro-level analysis. The advantage of this approach is that, if done within countries, it eliminates any possible cross-country differences and naturally incorporates country-specific contexts, such as the level of development, as well as structural, socio-economic, legal and institutional country features. It also allows accounting for the important consideration of heterogeneity across informal workers. A special module of the World Values Survey database, conducted just prior to the COVID-19 outbreak in four MENA countries (Egypt, Iraq, Jordan and Lebanon), enables such analysis.

Figure 3.4 and Figure 3.5 explore differences across formal and informal workers in the degree of satisfaction with their country's healthcare and education systems, the way the government performs its duties in the national office, the way the local authorities are responding to regional affairs, the system of social security, and state-provided support for those in need, as well as with the quality of healthcare, schools, roads and highways, air, water, housing, and the physical setting of the area in which they live. All answers to these satisfaction questions are measured on a scale from 1 to 4, where 1 means completely dissatisfied and 4 means completely satisfied.

Figure 3.4. Distribution of satisfaction with various aspects of public services, across formal and informal workers



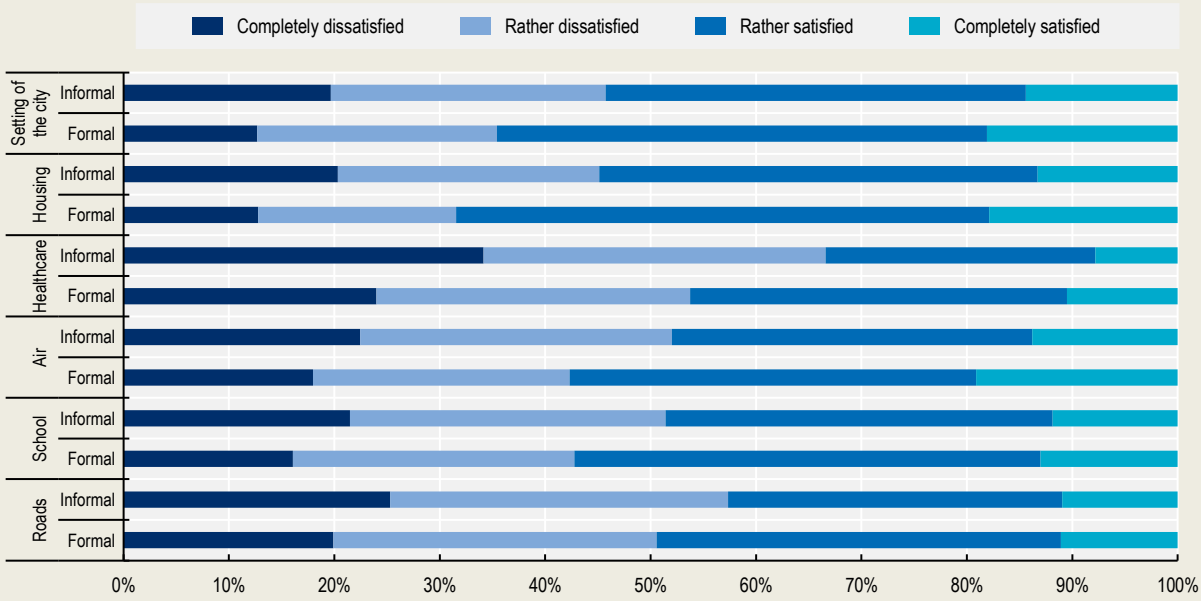
Note: Averages across countries: Egypt, Iraq, Jordan and Lebanon.
Source: Own computation based on (World Values Survey, 2020[42]).

StatLink https://stat.link/rf9nb5

A higher percentage of informal workers than formal workers were completely dissatisfied and rather dissatisfied with every aspect of the functioning of the public system. Very few individuals – whether formal or informal – were completely satisfied; however, the share of such individuals was higher among formal workers. There was also a higher rate of dissatisfaction with the quality of the provided services among

informal workers. The satisfaction gap is particularly pronounced with respect to the quality of healthcare: 67% of informal workers felt completely or rather dissatisfied compared with 53% of formal workers. There is a 10-percentage-point satisfaction gap (comparing completely and rather dissatisfied with completely and rather satisfied) between formal and informal workers in terms of satisfaction with the quality of schools, air, and city setting, and a 13-percentage-point gap in satisfaction with the quality of housing.

Figure 3.5. Distribution of satisfaction with the quality of services, across formal and informal workers



Note: Averages across countries: Egypt, Iraq, Jordan and Lebanon.
Source: Own computation based on (World Values Survey, 2020[42]).

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These linkages can be further explored using regression analysis, controlling for a range of individual socio-economic characteristics. Such analysis suggests that individual informality status is associated with lower satisfaction with the education system, the healthcare system, and the way the government performs duties in the national office, as well as less satisfaction with the quality of the healthcare system, housing, and the city setting. In other words, publicly provided services (including healthcare) and public institutions are not always responding to the demands and aspirations of many citizens, and particularly those of informal workers. Informal workers more acutely perceive injustice and are less satisfied with the system and its quality. As such, compared with formal workers, they more systematically consider the social contract to be weak.

In light of the continuing COVID-19 pandemic, reinforcing the social contract will mean dedicating a discernible effort not only to the recovery of health but also to that of work, including formal employment opportunities. It will also require rethinking institutions and publicly provided services in order to ensure that they are accessible, fair, reliable, predictable and trustworthy, placing the demands of all citizens, including informal workers, at the heart of the system.

Source: (Aleksynska and Wojcieszynski, 2022[43]).

Higher informality is associated with low public spending on public goods and services, and with inadequate social outcomes

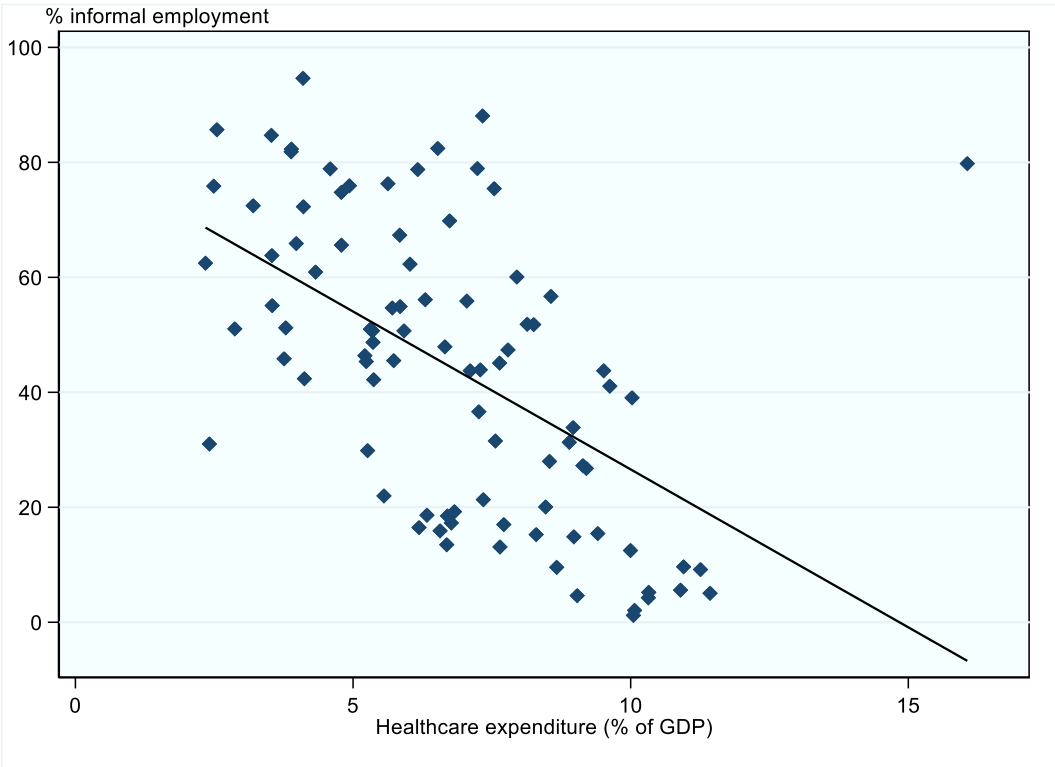
One of the main components of the social contract is the agreement that citizens comply with laws (including labour and social security laws), pay taxes and make social security contributions. But another no less important component of the social contract is that, in exchange for this, citizens receive good-quality public goods and services, such as education, healthcare, security and a clean environment. Access to good-quality public goods and services is also one of the key components of redistribution and of promoting equality of opportunity.

Low, or declining, satisfaction with the quality of publicly provided services can set a spiral of higher informality – lower quality of services – higher informality. The mechanism for this dynamic is as follows (Perry et al., 2007[44]; World Bank, 2017[45]; Oviedo, Thomas and Karakurum-Ozdemir, 2009[46]; OECD, 2011[23]; Hujo and Bangura, 2020[47]): individuals as well as businesses with high income who are dissatisfied with the quality of the provided services have a lower incentive to fulfil their obligations to the social contract through paying taxes or social security contributions. They may opt out of contributing to and consuming state-provided services, and substitute them with private services. In so doing, they may choose to demand and to perform informal activities (including under-reported, undeclared, or partially declared activities), and consider this rational and justifiable, in order to avoid double-paying for both the public and private services. This, in turn, leads to a decline in state receipts and undermines the state's capacity to improve the quality of public services, such as access to good-quality water and air, healthcare, education, or justice. As a result, there is also a growing dissatisfaction among those individuals and businesses who cannot afford to opt out of public services. This further enhances fracturing in the society, and further erodes trust and the social contract (Ferreira et al., 2013[48]; Hujo and Bangura, 2020[47]). Moreover, as the tax base narrows, the state may be obliged to levy higher taxes in order to cover the non-compliant, at the risk of rendering compliance too costly for poor and vulnerable workers and enterprises. The resulting outcome is an inconsistency between workers' demands and the institutional supply of social protection and high-quality public services. It is a narrow-based equilibrium of low tax receipts, high inequality, low satisfaction with the quality of publicly provided services, low trust, and high informality. Greater informality, along with its wider acceptance and tolerance, threatens and challenges existing social contract models (Plagerson, Alfers and Chen, 2022[18]).

To illustrate the association between low public spending on public goods and services and informality, Figure 3.6 and Figure 3.7 relate the share of informal employment to government healthcare expenditure and government education expenditure. The reason for highlighting these public services in particular is that access to better healthcare services comes first in the ranking of demands for state services in many developing countries, especially where the gaps in healthcare protection coverage are the highest. This is followed by better education (Traub-Merz et al., 2022[49]). In order to isolate these relationships from other confounding factors, predicted values of country-level informal employment, obtained from multivariate analysis and controlling for other factors associated with informality, are reported instead of actual values.

Both figures show that, when comparing otherwise similar countries, there is a strong negative correlation between the share of informality and the share of healthcare or education expenditure. In countries where social expenditures on healthcare and education are higher, informality is lower.

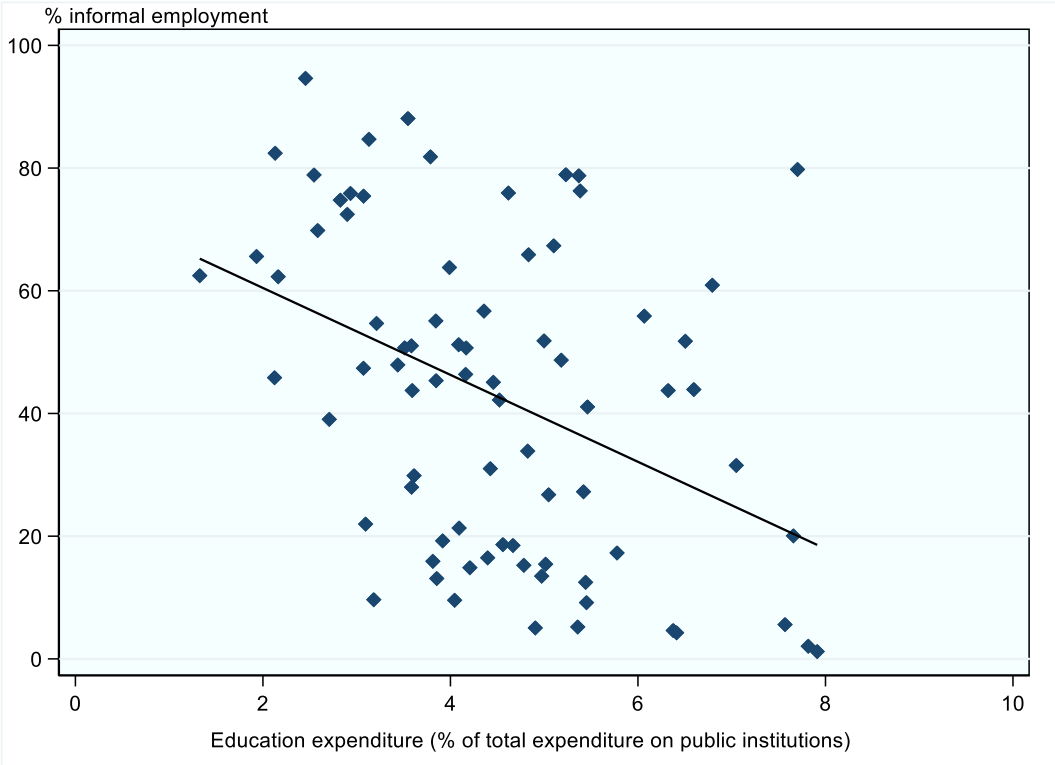
Figure 3.6. Informality negatively correlates with greater healthcare expenditure



Note: Own computation. Predicted rather than actual values of informality are reported. They are obtained from multivariate analysis controlling for seven geographical regions (sub-Saharan Africa, South Asia, North America, MENA, LAC, Europe and Central Asia, and East Asia and Pacific); GDP per capita (2017 PPP); life expectancy; population growth; age dependency ratio; 2018 ease of doing business; and trade. Informal employment: latest available data. For the full list of countries, see Annex 3.A.

Source: Informal employment: (ILO, 2023[38]), *Women and Men in the Informal Economy: A Statistical Update*, https://ilostat.ilo.org/en/; for GDP per capita (2017 PPP), life expectancy, population growth, age dependency ratio, trade and healthcare expenditure: (World Bank, 2021[39]), *World Development Indicators* (database), www.data.worldbank.org/products/wdi; for ease of doing business: (World Bank, 2022[40]), *Doing Business Indicators* (database), www.doingbusiness.org.

Figure 3.7. Informality negatively correlates with greater education expenditure



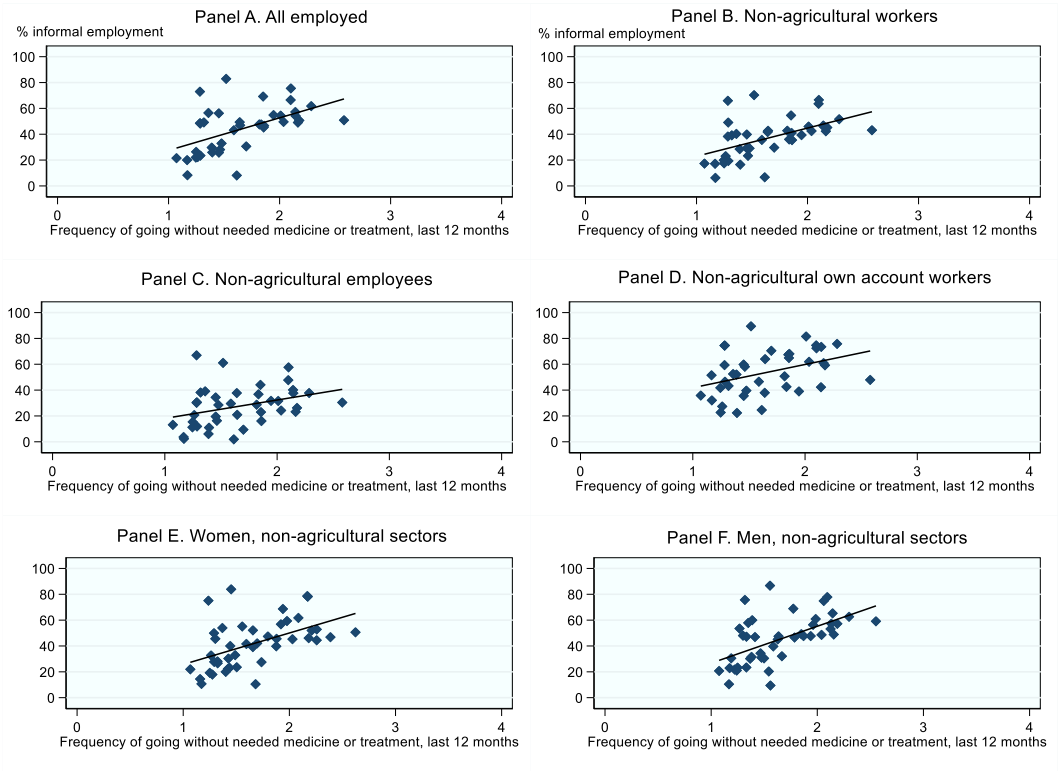
Note: Own computation. Predicted rather than actual values of informality are reported. They are obtained from multivariate analysis controlling for geography, GDP per capita (2017 PPP), life expectancy, population growth, age dependency ratio, 2018 ease of doing business, and trade. Informal employment: latest available data. For the full list of countries, see Annex 3.A.
Source: Informal employment: (ILO, 2023[38]) *Women and Men in the Informal Economy: A Statistical Update*, https://ilostat.ilo.org/en/; for GDP per capita (2017 PPP), life expectancy, population growth, age dependency ratio, trade, and education expenditure: (World Bank, 2021[39]), *World Development Indicators* (database), www.data.worldbank.org/products/wdi; for ease of doing business: (World Bank, 2022[40]), *Doing Business Indicators* (database), www.doingbusiness.org.

The link between informality and poor public service delivery is also visible when looking at social outcomes – either actual or perceived. Access to services, as well as perceptions about their quality, is what matters for political support as well as for voicing concerns (OECD, 2021[50]).

Figure 3.8 and Figure 3.9 relate informality to individual responses to the following questions: “How often you or your family have gone without needed medicine or treatment in the past 12 months” and “To what extent do you worry about not being able to give one’s children a good education?”. Reflecting the need to account for informal worker heterogeneity, the answers to these questions are averaged within subsamples of men and women, of employees and self-employed workers, and of all workers and non-agricultural workers, and are related to the share of informal employment within the same population subgroups.

The share of informality, regardless of the subgroup within which it is computed, shows a strong positive correlation with medical treatment deprivation within the same population subgroup (Figure 3.8). The distinction between employees and self-employed workers with regard to access to healthcare is important: self-employed workers may forego medical treatment more often if they have to forego work in order to travel to healthcare facilities or use care services without receiving compensation. Yet, correlations between the share of informal employment and medical treatment deprivation are equally high among employees and self-employed workers. The lack of employment protection and fear of losing jobs or pay may equally preclude informal wage employees from undergoing medical treatment while foregoing wage work.

Figure 3.8. Informality strongly correlates with medical treatment deprivation



Note: Predicted values of total informal employment, and of informal employment among non-agricultural workers, non-agricultural employees, non-agricultural self-employed workers, women in non-agricultural sectors and men in non-agricultural sectors. Controls include seven geographical regions (sub-Saharan Africa; South Asia; North America; MENA; LAC; Europe and Central Asia; and East Asia and Pacific); GDP per capita, PPP constant 2017; income share held by the lowest-income 10% of the population; population growth; trade as a percentage of GDP; the HDI; ease of doing business as of 2018; and political rights and civil liberties. Frequency of going without necessary medicine or treatment is computed as an average of individual responses to the question: "How often you or your family have gone without needed medicine or treatment in the past 12 months", with answers measured on a scale from 1 to 4, where 1 means never and 4 means often. Averages were taken (by country) within subsamples of all workers (Panel A), non-agricultural workers (Panel B), non-agricultural employees (Panel C), non-agricultural self-employed workers (Panel D), women in non-agricultural work (Panel E), and men in non-agricultural work (Panel F). The sample includes 34 countries (see Annex 3.A for the full list).

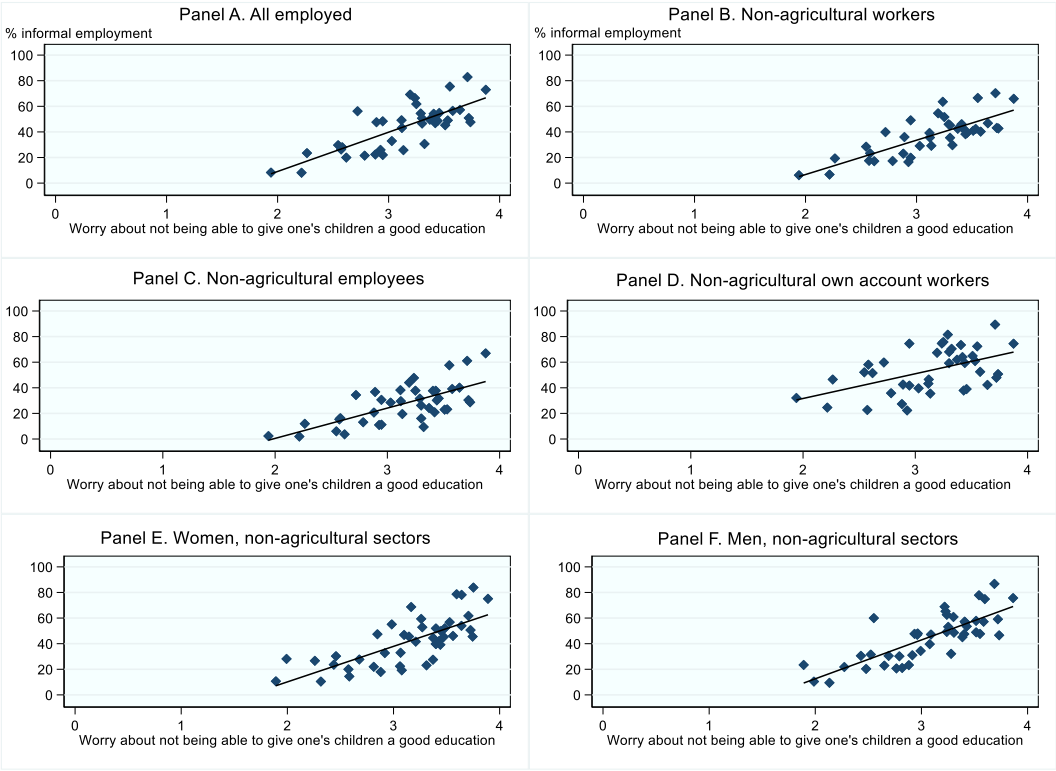
Source: For six measures of informal employment: (ILO, 2023[38]), *Women and Men in the Informal Economy: A Statistical Update*, https://ilostat.ilo.org/en/; for geographical regions, GDP per capita, PPP constant 2017; income share held by the lowest-income 10% of the population; population growth; trade as a percentage of GDP; the HDI: (World Bank, 2021[39]), *World Development Indicators* (database), www.data.worldbank.org/products/wdi; for ease of doing business: (World Bank, 2022[40]), *Doing Business Indicators* (database), www.doingbusiness.org; for political rights and civil liberties indices: (Freedom House, 2019[41]), *Freedom in the World* (database), freedomhouse.org/report/freedom-world; and for frequency of going without necessary medicine or treatment: own computations based on (World Values Survey, 2020[42]), *Wave 7* (database), worldvaluessurvey.org.

More generally, these high correlations in all subgroups of workers, including men and women, reflect poorer access of informal workers to many public health facilities. Even if healthcare may be available generally in a country, it may be unavailable to informal workers specifically for numerous reasons. They may be excluded from health insurance programmes; they may not be able to afford health insurance; they may live in remote areas; their access to healthcare may be linked to their place of residence rather than their place of work where they spend most of their time; or they may have specific occupational health needs (Alfers, 2015[51]; Traub-Merz et al., 2022[49]). Even within Organisation for Economic Co-operation and Development (OECD) member countries, rural regions, where informality is more widespread, "tend to be equipped with fewer hospital beds (…) In 2018, regions close to metropolitan areas had almost twice as many hospital beds per 1 000 inhabitants than remote regions. This gap has grown significantly since

2000" (OECD, 2020[52]). In many instances, out-of-pocket medical expenses are simply unaffordable to poor informal workers. For example, in Bangladesh, despite progress towards universal health coverage, 72% of current healthcare expenditure comes from out-of-pocket spending (Oliveira, Islam and Nuruzzaman, 2019[53]).

The combination of these factors made it particularly difficult to contain the spread of COVID-19. It also resulted in the double burden of the crisis for informal economy workers, who disproportionately suffered both from employment and income losses due to lockdown measures, and from inadequate access to healthcare.

Figure 3.9. Informality strongly correlates with poor education prospects



Note: Predicted values of informal employment. Controls include seven geographical regions (sub-Saharan Africa; South Asia; North America; MENA; LAC; Europe and Central Asia; and East Asia and Pacific); GDP per capita, PPP constant 2017; income share held by the lowest-income 10% of the population; population growth; trade as a percentage of GDP; the HDI; ease of doing business as of 2018; and political rights and civil liberties. Worry about not being able to give one's children good education is computed as an average of individual responses to the question: "To what extent do you worry about not being able to give one's children a good education", with answers measured on a scale from 1 to 4, where 1 means not at all and 4 means very much. Averages were taken (by country) within subsamples of all workers (Panel A), non-agricultural workers (Panel B), non-agricultural employees (Panel C), non-agricultural self-employed workers (Panel D), women in non-agricultural work (Panel E), and men in non-agricultural work (Panel F). The sample includes 34 countries (see Annex 3.A for the full list).
Source: For six measures of informal employment: (ILO, 2023[38]), Women and Men in the Informal Economy: A Statistical Update, https://ilostat.ilo.org/en/; for geographical regions, GDP per capita, PPP constant 2017; income share held by the lowest-income 10% of the population; population growth; trade as a percentage of GDP; the HDI: (World Bank, 2021[39]), World Development Indicators (database), www.data.worldbank.org/products/wdi; for ease of doing business: (World Bank, 2022[40]), Doing Business Indicators (database), www.doingbusiness.org; for political rights and civil liberties indices: (Freedom House, 2019[41]), Freedom in the World (database), freedomhouse.org/report/freedom-world. For frequency of worry about not being able to give one's children a good education: own computations based on (World Values Survey, 2020[42]), *Wave 7* (database), worldvaluessurvey.org.

The share of informality within various population subgroups also strongly correlates with poor education prospects of future generations perceived within the same population subgroups, and measured by the

degree of worry that individuals express regarding the education of their children (Figure 3.9). This worry relates to both the quality of available schooling and the unequal access to education between children from vulnerable and non-vulnerable households, including those where the primary wage earners are in informal employment. Even where schooling is compulsory, for many informal workers in poor households the burden of household expenditure on education may be particularly heavy, leading to their children dropping out of school at higher rates and impeding the intergenerational transition out of poverty and out of informal employment (UNESCO, 2017[54]; OECD/CAF/ECLAC, 2016[55]). Government education subsidies to these families, such as in-kind or cash transfers to the families (specifically intended for school meals, school materials and clothing), even if schooling is free, may not be provided in an inclusive manner, or may be insufficient. Again, the COVID-19 crisis presented unique challenges to education prospects in many developing countries. School closures over 2020-21, the lack of broadband connectivity in the rural areas, the lack of computers, and unequal preparedness of teachers have particularly compromised education in rural areas, of children from vulnerable backgrounds (including those from households where the primary wage earners are in informal employment), and of girls (De Giusti, 2020[56]).

Exit and exclusion co-exist as important drivers of informality and often reflect the nature of the social contract

Until now, much of the debate about informality has focused on whether informality is a result of an "exclusion" or an "exit" strategy from formal working arrangements. According to the "exclusion" view, workers are in informal employment not by choice but because of either legal exclusions or the inability to comply with existing regulations (involuntary non-compliance). Some workers may be excluded from specific regulations by the regulations' design. For example, this has historically been the case of domestic workers in many countries (ILO, 2021[57]). In practice, even if laws are applicable, compliance with them may be prohibitively costly (De Soto, 1989[58]), thus leading to the de facto exclusion of those workers who in principle would wish to be formal. For many workers, especially poor self-employed workers with few options outside the informal economy, the choice of becoming formal is so constrained that it can be considered as non-existent, leading to their de facto exclusion. For workers who are employees, limited bargaining power also means that their formality status often depends on the employer.

The "exit" view of informality presumes that workers consciously choose informal arrangements and prefer to stay informal because they see more benefits to this. As pointed out by Perry et al. (Perry et al., 2007[44]), "there is a continuum in the relative importance of exclusion and exit among individual workers and firms within countries" (p. 2). Indeed, even within the same country, there may be workers choosing informality because they view it as superior to formality, just as there may be workers with no other options but to remain informal. Knowing whether informality is the result of a choice or of an exclusion is important, as it would trigger different policy responses to address informality (Perry et al., 2007[44]).

Cross-country evidence on the reasons for informal employment is slim and inconsistent. Most of it dates back prior to the 2008 economic crisis. Examples show that voluntary informal employment is most often found among self-employed as compared with salaried workers. It is relatively frequent in LAC (Table 3.1). Still, in the vast majority of countries with available data, including in LAC, the main or the most frequently stated reason for being in informal employment is because the worker could not find a different job (Table 3.2).

Table 3.1. Reason for being in informal employment: a choice

Region	Country	Year of study	Surveyed workers	Finding
LAC	Argentina	2005-06	Independent workers	28.5%
LAC	Argentina	2005-06	Salaried workers	19.5%
LAC	Plurinational State of Bolivia (hereafter: Bolivia)	2005-06	Independent workers	40.2%
LAC	Bolivia	2005-06	Salaried workers	4.8%
LAC	Colombia	2005-06	Independent workers	51.1%
LAC	Colombia	2005-06	Salaried workers	7.0%
LAC	Dominican Republic	2005-06	Independent workers	52.0%
LAC	Dominican Republic	2005-06	Salaried workers	15.0%
LAC	Brazil	2003	Entrepreneurs	16.5%

Note: Own compilation. For Argentina, Bolivia, Colombia, and the Dominican Republic, "choice" for independent workers includes any of the following answers: having autonomy/no boss; having flexible hours/less responsibility; family tradition; higher earnings; and/or better mobility/benefits/prospects; for salaried workers, "choice" includes any of the following answers: less responsibility; more earnings; or better mobility/benefits/prospects. For Brazil, "choice" refers to "having independence" as the reason for informal work.
Source: For Argentina, Bolivia, Colombia, and the Dominican Republic: (Arias and Monserrat, 2007[59]; Arias, Landa and Yáñez, 2007[60]); for Brazil: (Williams and Youssef, 2013[61]).

Table 3.2. Reason for being in informal employment: could not find a different (formal or salaried) job

Region	Country	Year of study	Surveyed workers	Finding
LAC	Argentina	2005-06	Salaried workers	48.4%
LAC	Argentina	2005-06	Independent workers	43.0%
LAC	Bolivia	2005-06	Salaried workers	64.2%
LAC	Bolivia	2005-06	Independent workers	25.3%
LAC	Colombia	2005-06	Salaried workers	43.0%
LAC	Colombia	2005-06	Independent workers	55.3%
LAC	Dominican Republic	2005-06	Salaried workers	38.9%
LAC	Dominican Republic	2005-06	Independent workers	44.3%
LAC	Brazil	2003	Entrepreneurs	Main reason; 31.1%
Asia	Pakistan	2012-13	Informal sector workers	53.4%
Asia	India	2007-10	Women entrepreneurs	Main reason
Africa	Ethiopia	1996-2003	Informal sector workers	Main reason
Africa	Ghana	2009	Informal business owners	Main reason
Africa	Kenya	2009	Informal business owners	Main reason
Africa	Lesotho	2019	Informal business owners	24.7%
Africa	Mauritania	2017	Informal business owners	29.6%
Africa	Nigeria	2009	Informal business owners	Main reason
Africa	South Africa	2013	Informal business owners	Main reason
Africa	Uganda	2021	Independent workers	36.2%
Africa	Uganda	2021	Informal independent workers	37.1%

Note: Own compilation.
Source: For Argentina, Bolivia, Colombia, and the Dominican Republic: (Arias and Monserrat, 2007[59]; Arias, Landa and Yáñez, 2007[60]); for Brazil: (Williams and Youssef, 2013[61]); for Pakistan: (Williams, Shahid and Martínez, 2016[62]); for India: (Williams and Gurtoo, 2011[63]); for Ethiopia: (Siba, 2015[64]); for Ghana, Kenya, Nigeria, and South Africa: (Benzing and Chu, 2009[65]); for Lesotho: own computations based on Enquête Nationale sur l'Emploi et le Secteur Informel (ENE-SI); for Mauritania: own computations based on labour force survey; for Uganda: own computation based on labour force survey.

While some workers may engage in the informal economy because of a constraint, while others as a voluntary choice, what is remarkable is that in all cases informality mirrors the nature of the social contract. If too many individuals are excluded from the social contract, it means that the procedural dimension of the social contract is weak or misaligned with the substantive dimension. If too many individuals choose not to comply, it is likely that both the procedural and the substantive dimensions of the current social contract are weak (or are weakening).

Moreover, the social contract framework also embraces other reasons for informality, including reasons with direct reference to the social contract and the role of the state, and which cannot be classified as a "choice" in a binary way. For example, 15.4% of Bolivian independent workers are informal because of the lack of trust in public institutions (Arias and Monserrat, 2007[59]; Arias, Landa and Yáñez, 2007[60]). In Pakistan, 21.6% of workers operate informally because of the corruption of public authorities, and 44.3% of workers find it socially acceptable (Williams, Shahid and Martínez, 2016[62]).

Key policy messages

The social contract approach to informality allows us to think differently about the tools to address this old phenomenon. It allows us to step out of the blaming rhetoric, such as shaming non-compliant workers and businesses, and suggests the need for holistic and coherent policy solutions to render the procedural dimension of the social contract more adequate and relevant, and to ensure that the substantive dimension is strong and inclusive of all.

In this regard, country-specific reviews and tailored policy solutions are important in order to diagnose the exact nature of informality and the extent to which it is influenced by inadequacies in either the procedural or substantive dimensions.

Depending on the country, strengthening social contracts and making them inclusive of informal workers would require continuous efforts to strengthen the procedural dimension by expanding coverage of formal legal frameworks, by ensuring sufficiency of protections, and by improving compliance with formal arrangements. Strengthening the substantive dimension can be achieved by improving access to and the quality of those services that are most valued by all workers, such as healthcare, education and skills development. Moreover, in light of high prevalence of informality, this should be done in accordance with the needs and conditions of the informal economy workers, who are predominant in rural areas and often disregarded by urban planning. Fighting corruption, strengthening the trustworthiness of the judiciary system and the police, and improving how the government performs its duties, including towards informal workers, are equally important long-term efforts that should continue. To build trust, governments also need to recognise informal workers' organisations where they exist, help them become more visible, engage in constructive dialogue with these organisations, and ensure their participation in the construction of a new social contract that is inclusive, adequate, relevant and fair for informal workers and their families (Chen et al., 2022[66]).

Indeed, this chapter showed that in many developing countries, public institutions and publicly provided services, such as healthcare and education, are often not responding to the demands and aspirations of citizens in general, and even less so to those of informal workers specifically. Informality goes hand in hand with lower social spending. At the same time, informal workers – whether they are informal voluntarily or not – are more dissatisfied with the public systems and the quality of provided services than formal workers. Involuntary informal workers perceive injustice more acutely than formal workers, and are less satisfied with the public system and its quality. In certain settings, those who can choose their type of employment (formal or informal) do not perceive sufficient benefits linked to formality, and may see fewer incentives to engage in the obligations associated with the social contract, fuelling their disengagement from public institutions in a feedback loop. Reinforcing the social contract in the post-COVID-19 era in order to make it more resilient to new crises will mean dedicating a continuous effort to the recovery of

people's livelihoods and their trust in society. Importantly, it will require rethinking institutions and publicly provided services in order to ensure that they are accessible, fair, reliable, predictable and trustworthy, placing the demands of all citizens, including informal workers, at the heart of the system.

The strength and relevance of any social contract may be influenced not only by internal factors, but also by the international environment (UNRISD, 2022[7]; Plagerson, Alfers and Chen, 2022[18]). Changes in the world of work, globalisation, uneven spread of technologies, and the emergence of new forms of employment (including through digital labour platforms) have been continuously shifting financial and economic risks onto individual workers' shoulders. In many instances, these changes have also undermined the quality of the social contract and called for its reimagining (World Bank, 2019[67]). In all countries, regardless of their level of development, governments should remain vigilant about the concurrent weakening of the social contract and informality as its manifestation.

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Annex 3.A. Lists of countries included in the analysis of selected figures

List of countries included in Figure 3.2, Figure 3.3, Figure 3.8 and Figure 3.9:

Argentina
Bangladesh
Bolivia
Brazil
Chile
People's Republic of China
Colombia
Cyprus[2]
Ecuador
Egypt
Germany
Greece
Guatemala
Indonesia
Iraq
Japan
Kazakhstan
Korea
Kyrgyzstan
Mexico
Myanmar
Nicaragua
Pakistan
Peru
Philippines
Republic of Türkiye
Romania
Serbia
Tajikistan
Thailand
Tunisia
United States
Viet Nam
Zimbabwe

List of countries included in Figure 3.6 and Figure 3.7:

Albania
Angola
Argentina
Armenia

Austria
Bangladesh
Belgium
Benin
Bolivia
Bosnia and Herzegovina
Botswana
Brazil
Brunei Darussalam
Bulgaria
Burkina Faso
Cabo Verde
Cambodia
Cameroon
Chad
Chile
People's Republic of China
Colombia
Comoros
Costa Rica
Croatia
Cyprus
Czech Republic
Denmark
Dominican Republic
Ecuador
El Salvador
Estonia
Finland
France
Germany
Ghana
Greece
Guatemala
Honduras
Hungary
Iceland
India
Indonesia
Iraq
Italy
Japan
Jordan
Latvia
Liberia
Lithuania
Madagascar
Mali
Malta
Mexico
Mongolia

Morocco
Myanmar
Namibia
Nepal
Nicaragua
Niger
Nigeria
Norway
Pakistan
Panama
Paraguay
Peru
Poland
Portugal
Republic of Türkiye
Romania
Rwanda
Samoa
Senegal
Serbia
Sierra Leone
Slovenia
South Africa
Spain
Sri Lanka
Sweden
Tajikistan
Timor-Leste
Togo
Tunisia
Uganda
United Kingdom
Uruguay
Viet Nam
Zambia

Notes

[1] Some authors single out four dimensions: procedural, substantive, participatory and recognition-related (Loewe, Trautner and Zintl, 2019[68]) (Plagerson, Alfers and Chen, 2022[18]).

[2] Note by the Republic of Türkiye

The information in this document with reference to “Cyprus” relates to the southern part of the Island. There is no single authority representing both Turkish and Greek Cypriot people on the Island. Türkiye recognises

the Turkish Republic of Northern Cyprus (TRNC). Until a lasting and equitable solution is found within the context of the United Nations, Türkiye shall preserve its position concerning the “Cyprus issue”.

Note by all the European Union Member States of the OECD and the European Union

The Republic of Cyprus is recognised by all members of the United Nations with the exception of Türkiye. The information in this document relates to the area under the effective control of the Government of the Republic of Cyprus.

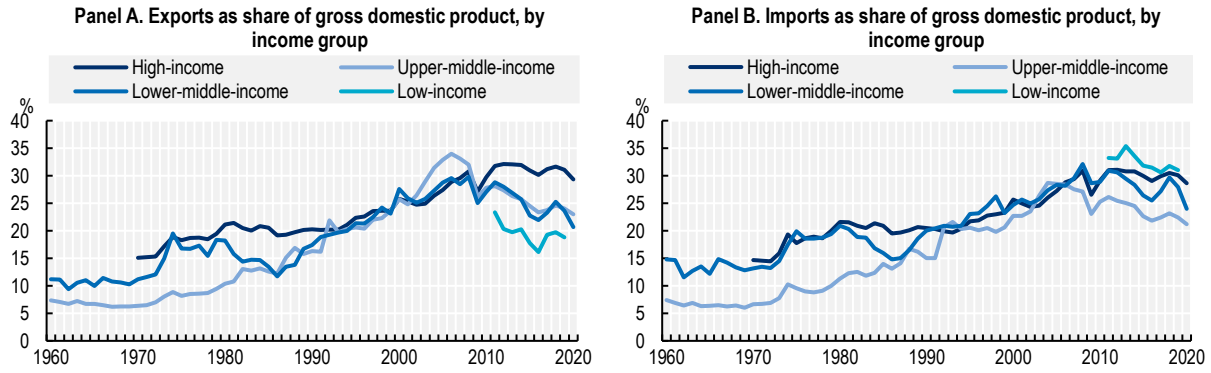
4 Informal employment in the global economy

This chapter analyses the relationship between informal employment and economic globalisation. First, it shows that economic globalisation does not necessarily translate into more formal jobs, especially in the least developed countries. It documents that the effects of global trade on informal employment depend on whether greater integration into the world economy is led by import or export liberalisation. These effects also depend on the type of industry, on geographical location, and on type of affected workers and enterprises. Second, this chapter examines informality within global value chains (GVCs), showing that its prevalence is affected by the types of linkages (backward or forward), production organisation within the value chain, purchasing practices, possibility of upgrading, and the sector of activity. Finally, the chapter discusses the role of public and private actors in ensuring that globalisation brings formalisation benefits and improves working conditions for all workers, including informal workers.

Economic globalisation does not automatically translate into more formal employment

Economic globalisation – the interconnectedness of countries through international flows of goods, services and capital – reached unprecedented levels around the beginning of the 21st century. On the eve of the COVID-19 pandemic, developing countries were much more integrated into the global economy than was the case previously. Many developing countries conducted deliberate large-scale trade liberalisation, including within the General Agreement on Tariffs and Trade (GATT), or the World Trade Organization (WTO), liberalised trade within regional trade blocs, or integrated regional and global value chains. Despite international trade – one of the components of globalisation – slowing down since the economic recession of 2008 in both developed and developing countries (Figure 4.1), the technological change continued reducing transportation, communication and financial transaction costs. As such, increasing interdependence between countries and regions continued throughout the beginning of the 21st century.

Figure 4.1. International trade grew steadily between 1960 and 2020



Note: Income group weighted averages, based on World Bank national accounts data and Organisation for Economic Co-operation and Development (OECD) National Accounts data files.
Source: World Bank (2021[1]), *World Development Indicators* (database), data.worldbank.org/products/wdi.

StatLink https://stat.link/ao17mk

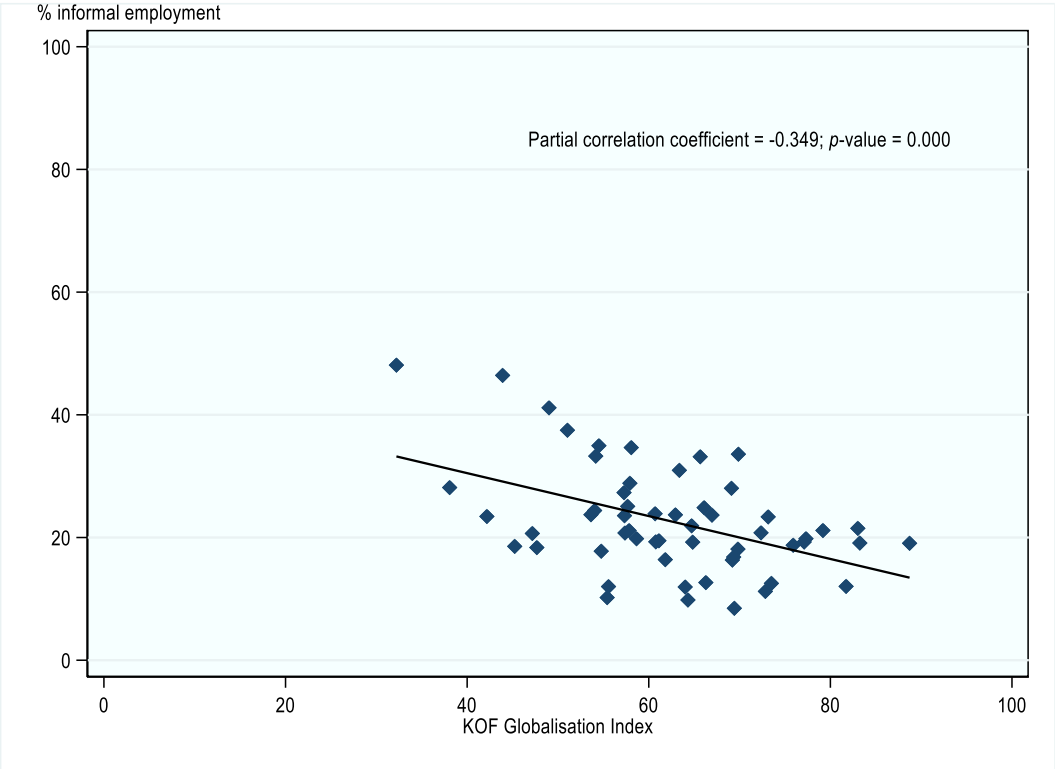
The period 2020-2023, marked by the COVID-19-induced crisis followed by Russia's war of aggression against Ukraine, underscored the high degree of this interconnectedness but also disrupted it. The consequences of these crises on trade varied across regions. During the pandemic, Africa's exports declined by more than the global average of countries with similar export composition (AUC/OECD, 2022[2]). In Asia, trade rapidly rebounded from 2021 onwards, with merchandise exports in the People's Republic of China (hereafter: China), India, Indonesia, Malaysia, Thailand and Viet Nam quickly exceeding their pre-pandemic levels (OECD, 2022[3]). Yet, until late 2022, the zero-COVID policy in China continued to disrupt GVCs. In Latin America and the Caribbean, economies such as Brazil, Chile, Peru and Uruguay, where China is a crucial trading partner, saw a substantial drop in trade, which negatively affected these economies (OECD et al., 2022[4]). The Russian invasion of Ukraine also disrupted trade in fertilisers and several types of crops and oils, and led to soaring prices in energy and agro-food crops and products throughout the world (OECD, 2022[5]).

Increased economic globalisation is not associated with greater formalisation in less developed countries

Globalisation can be a powerful promoter of economic growth, and can enhance productivity and efficiency. However, its impact on job creation in developing countries, and especially on the quality of jobs, including their formality aspect, remains unclear. Since the 1980s, for much of the developing world, integration with the global economy created significant challenges in terms of handling the adjustment dynamics and distributional consequences of formal and informal employment. On the one hand, branches of multinational enterprises in developing countries tend to offer better working conditions than local companies, including hiring workers formally and promoting skills development. Access to foreign markets and partners often led to the establishment of local formal enterprises, skills and technology transfer, and promoted the formalisation of informal enterprises, thus leading to the growth of formal employment. On the other hand, globalisation also results in more intense competition, which pushes some local enterprises out of the market and forces workers who lose their jobs into informal employment. It can also incentivize other enterprises to rely increasingly on lower-cost informal workers, whether through subcontracting or through informal employment relationships within formal establishments (Bacchetta, Ernst and Bustamante, 2009[6]; Chen and Alter, 2002[7]; Cisneros-Acevedo, 2021[8]). Vulnerabilities to the disruptions of GVCs, including the supply of intermediate inputs, put further pressure on enterprises to cut costs and reorient their production to local, and often informal, markets.

As a result, the overall effect on informal employment is frequently ambiguous; moreover, the effect is not uniform across countries. Generally, a higher degree of globalisation is associated with lower informality in upper-middle-income and high-income countries (Figure 4.2). However, this relationship does not hold for lower-middle-income and low-income countries (Figure 4.3). The partial correlation coefficient between informality and globalisation is substantially lower in the sample of poorer countries than in the sample of richer countries, and is not significantly different from zero, keeping other confounding factors constant. In other words, globalisation does not seem to benefit poorer countries in terms of formal employment as much as it benefits richer countries.

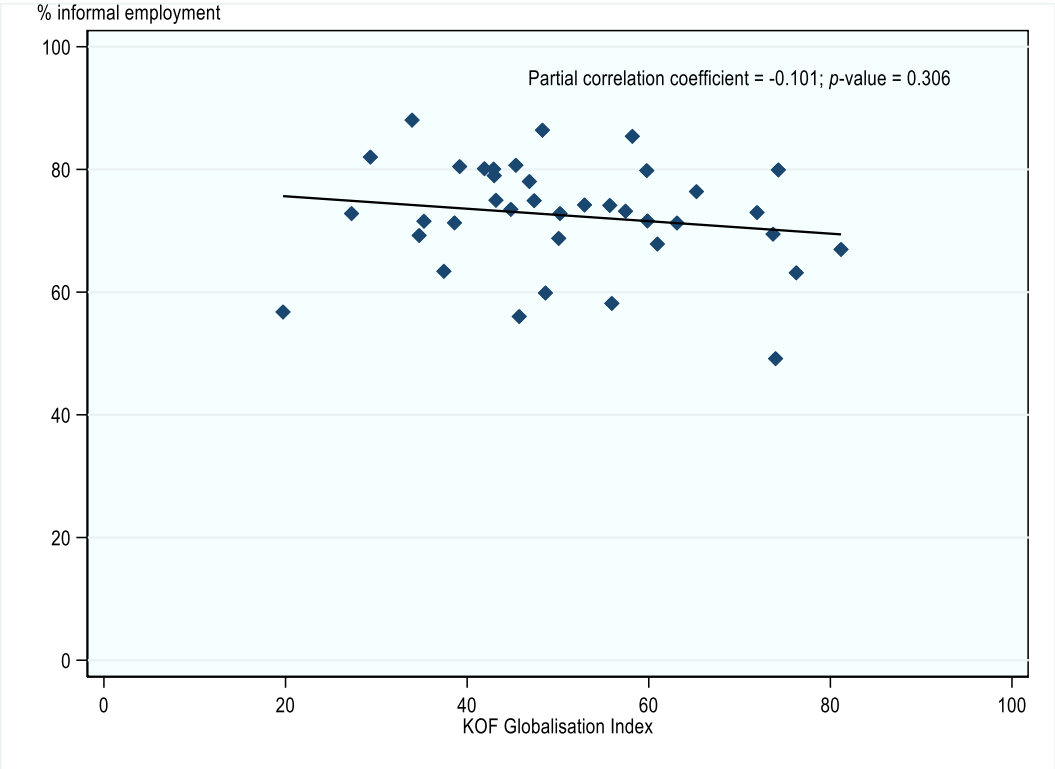
Figure 4.2. Globalisation and informal employment in upper-middle-income and high-income countries are negatively correlated



Note: Globalisation is measured by the KOF Globalisation Index, which includes the following components: trade in goods, trade in services, trade partner diversification, foreign direct investment, portfolio investment, international debt, international reserves, and international income payments. For both variables, residual rather than actual values are reported (note that the mean of each variable is added to its residuals). Thus, the figure can be interpreted as the relationship between the two variables keeping a set of controls constant. Those controls are: gross domestic product (GDP) per capita (2017 PPP), life expectancy, population growth, age dependency ratio, and the World Bank 2017 Ease of Doing Business Index. The sample includes 56 countries with available data for 2018.

Source: Informal employment: ILO (2018[9]), *Women and Men in the Informal Economy: A Statistical Picture*, www.ilo.org/global/publications/books/WCMS_626831/lang--en/index.htm; for GDP per capita (2017 PPP), life expectancy, population growth, and age dependency ratio: World Bank (2021[1]), *World Development Indicators* (database), www.data.worldbank.org/products/wdi; for ease of doing business: World Bank (2021[10]), *Doing Business* (database), www.doingbusiness.org; for the KOF Globalisation Index: Gygli et al. (2019[11]), https://kof.ethz.ch/en/forecasts-and-indicators/indicators/kof-globalisation-index.html.

Figure 4.3. Globalisation and informal employment in lower-middle-income and low-income countries are virtually unrelated



Note: Globalisation is measured by the KOF Globalisation Index, which includes the following components: trade in goods, trade in services, trade partner diversification, foreign direct investment, portfolio investment, international debt, international reserves, and international income payments. For both variables, residual rather than actual values are reported (note that the mean of each variable is added to its residuals). Thus, the figure can be interpreted as the relationship between the two variables keeping a set of controls constant. Those controls are: GDP per capita (2017 PPP), life expectancy, population growth, age dependency ratio, and the World Bank 2017 Ease of Doing Business Index. The sample includes 39 countries with available data for 2018.

Source: Informal employment: ILO (2018[9]), *Women and Men in the Informal Economy: A Statistical Picture*, www.ilo.org/global/publications/books/WCMS_626831/lang--en/index.htm; for GDP per capita (2017 PPP), life expectancy, population growth, and age dependency ratio: World Bank (2021[1]), *World Development Indicators* (database), www.data.worldbank.org/products/wdi; for ease of doing business: World Bank (2021[10]), *Doing Business* (database), www.doingbusiness.org; for KOF Globalisation Index: Gygli et al. (2019[11]), https://kof.ethz.ch/en/forecasts-and-indicators/indicators/kof-globalisation-index.html

This chapter examines the reasons for this disparity. It shows that the linkages between informality and globalisation are complex. They are related to the nature of trade and trade liberalisation asymmetries (whether in exports or in imports), the organisation of trade through GVCs, and the specificities of particular sectors. All of these reasons also relate to specific characteristics of economies at various income levels. In poor countries with a low-skilled workforce, enterprises operate in a more extractive mode, exporting raw commodities with limited added value, and not necessarily relying on a large formal labour force. Deficiencies in infrastructure to support higher value-added industries contribute to this dynamic.

The higher degree of informality in a specific country in turn may also preclude it from greater participation in the global economy. This is due to various reasons. The large informal economy can prevent countries from developing a sizeable and diversified export base, and limit their ability to benefit fully from their integration into the world economy (Bacchetta, Ernst and Bustamante, 2009[6]). Informality also limits enterprise size and productivity growth: enterprises operating in the informal economy are often small and face numerous barriers to growth, such as access to finance and to information, limited or inadequate training, inability to attract and build talent, and susceptibility to shocks. This prevents them from achieving

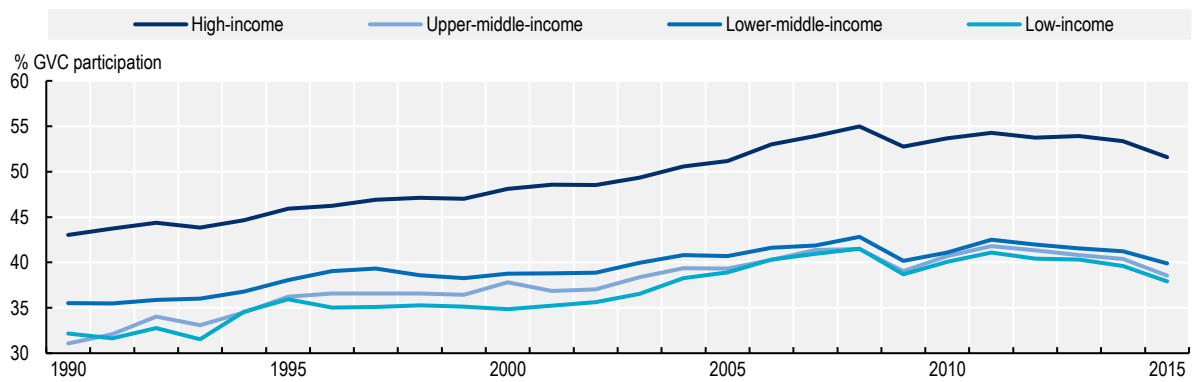
high productivity and from offering high-quality goods and services, leading to a low capacity to export. Informality may prevent the successful reallocation of resources within the informal economy. Informality is also strongly linked to income inequality, which in turn restricts access to education and health, and eventually blocks access to capital and skills, and as a result, decreases trade. A high informality rate limits the generation of public revenue, limits government resources to expand and create infrastructure, technology and so on; lack of fiscal space means that capacity to act is lower. In short, informality in itself is an obstacle to countries' full and fruitful participation in the world economy.

GVCs originating from India and Indonesia exhibit some of the highest risks of linkages between trade and informal employment

International production and trade are increasingly organised through GVCs. By 2020, international trade in final products represented only about 30% of all trade, whereas up to 70% of international trade involved a variety of production processes and exchanges spanning multiple countries, before being incorporated into final products (OECD, 2020[12]).

GVC participation can be measured as a situation where value added crosses at least two borders. Applying this definition, such complex processes also substantially grew in importance (Figure 4.4). The size of GVCs, which corresponded to 43% of gross exports in high-income economies and roughly 35% in middle-income economies in 1990, increased to 53% and roughly 40%, respectively, by 2015.

Figure 4.4. GVC integration is a defining factor of globalisation



Note: GVC participation is defined as exported value added which crosses at least two borders. Here, it is expressed as share of gross exports.
Source: Authors' computation based on Eora26 data obtained in Belotti, Borin and Mancini (2020[13]).

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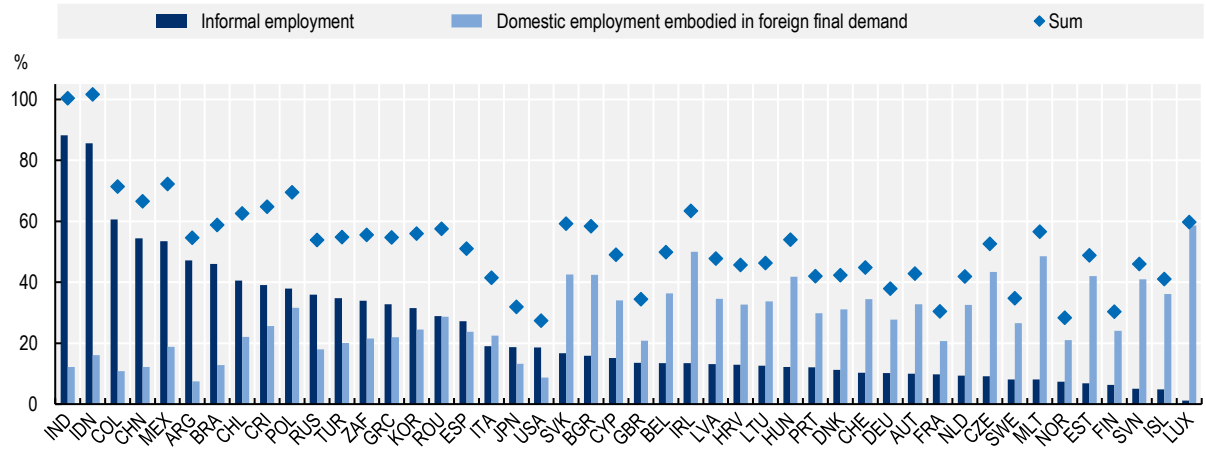
Measuring informal employment in GVCs is not easy, as it presupposes disentangling employment in jobs related to GVCs from those that are not. The best place to collect such information is enterprise-level, job-specific statistics. In the absence of such information, it is also possible to compare, on a more aggregate level, the share of informal employment in a country with the share of trade-related employment. Inter-country input-output analysis (an analysis based on linkages between industries within and across countries) allows estimation of the percentage of total employment that is embedded in foreign final demand. If the sum of the informal employment rate and of the trade-related employment rate in a given country is greater than 100%, then at least some of the GVC-related employment is definitely informal. Also, the greater the sum, the higher the probability that at least some GVC-related employment is informal. As shown in Figure 4.5, one cannot rule out that informal employment and GVCs are related. GVCs

originating from India and Indonesia exhibit the highest risk of informality footprint. In more advanced economies, where law enforcement and state institutions may be stronger, it is possible that all GVC-related jobs are formal, while informality is found elsewhere in the economy.[1]

Figure 4.5. Informal employment and GVC-related employment, by country



Note: Both informal and domestic employment embodied in foreign final demand are expressed as a share of total employment. If the sum of these indicators is larger than 100%, one can interpret these results as evidence of overlap between informal employment and trade-linked employment.

Source: Informal employment: ILO (2018[9]), *Women and Men in the Informal Economy: A Statistical Picture*, www.ilo.org/global/publications/books/WCMS_626831/lang--en/index.htm; domestic employment embodied in foreign final demand (%): OECD (2019[14]), *Trade in employment (TiM): Principal indicators* (database), https://stats.oecd.org/Index.aspx?DataSetCode=TIM_2019_MAIN.

StatLink https://stat.link/sw89xb

The effects of global trade on informal employment are context-specific

Trade liberalisation, as one of the aspects of economic globalisation, is often seen as beneficial for the overall economy, favouring economic growth, efficiency and innovation (OECD, 2018[15]; Goldberg and Pavcnik, 2016[16]). However, not everyone benefits from trade equally. Trade-induced changes in production activities require reallocation of resources, which in turn leads to economy-wide adjustments in terms of employment quantity and quality, generating winners and losers from trade liberalisation not only across countries but also within countries.

With respect to informal employment specifically, from a theoretical point of view, trade liberalisation can either increase or decrease informal employment in a specific country permanently, depending on the models' assumptions (Goldberg and Pavcnik, 2003[17]; Goldberg and Pavcnik, 2004[18]). Empirically, the key difference appears to be in the nature of the trade liberalisation – whether it concerns imports or exports. Trade liberalisation induced by the reduction of export tariffs, and therefore the expansion of export opportunities, seems to decrease informal employment share in the affected sectors and regions. In contrast, trade liberalisation caused by the reduction of import tariffs, and therefore the expansion of imports, tends to increase the share of informal employment in the affected sectors and regions.

Increased export opportunities tend to boost formal employment opportunities

Several country studies show that a reduction in tariffs imposed on a country's exports by its trading partners leads to a reduction in the share of informality (Table 4.1).

Table 4.1. Effect of a reduction in trading partner tariffs on informal employment

Country covered	Empirical study	Time period	Focus	Data used to measure informal employment	The reduction in partner tariffs leads the informality share to…
Botswana	McCaig and McMillan (2020[19])	1995-2006	Entire economy, mining and manufacturing	Labour force survey (Central Statistics Office of Botswana)	Decrease, in the clothing industry
Brazil	Paz (2014[20])	1989-2001	Tradable sectors	Household survey (PNAD)	Decrease
Mexico	Aleman-Castilla (2006[21])	1989-2002	Entire economy, urban areas only	Labour force survey (ENEU)	Decrease, for export-oriented industries, less so for industries facing high import competition
Mexico	Ben Yahmed and Bombarda (2020[22])	1993-2001	Manufacturing, services, urban areas only	Labour force survey (ENEU)	Decrease, for women
Viet Nam	McCaig and Pavcnik (2018[23])	1993-2004	Entire economy, tradable sector, manufacturing	Household survey (VHLSS)	Decrease, influenced by movements from informal microenterprises to formal larger enterprises within manufacturing

Note: This table includes non-exhaustive examples of empirical evidence published in peer-reviewed academic journals. In all studies, the effect of trade liberalisation is isolated from other confounding factors.
Source: Authors' compilation.

For instance, in the case of Botswana, informal employment in the clothing sector decreased as a result of the elimination of US duty fees, mandated by the 2000 African Growth and Opportunities Act in the United States (McCaig and McMillan, 2020[19]).

Tariff reductions by Brazil's partners on the country's exports throughout the 1990s resulted in a decrease in the informal employment share in manufacturing, as well as an increase in formal employees' wages (Paz, 2014[20]).

In Mexico, following the entry into force of the North American Free Trade Agreement (NAFTA), lower tariffs imposed by the United States on Mexican exports led to a decrease in informality (Aleman-Castilla, 2006[21]; Ben Yahmed and Bombarda, 2020[22]). The effects of export opportunities, however, differed across workers and enterprises. The most export-oriented industries (such as textiles, apparel and leather), as well as women, benefitted the most from lower tariffs imposed on national exports (Aleman-Castilla, 2006[21]; Ben Yahmed and Bombarda, 2020[22]).

For Viet Nam, the United States-Vietnam Bilateral Trade Agreement reduced export tariffs for Viet Nam. This induced a positive export shock from Viet Nam, and led to a substantial reallocation of workers from informal microenterprises to formal sector enterprises in manufacturing. Such reallocation was mainly induced by the expansion of existing formal enterprises, and a new entry of enterprises directly into the formal sector, rather than the formalisation of informal microenterprises (McCaig and McMillan, 2020[19]).

In contrast, import competition can increase informal employment

Trade liberalisation induced by a country's own tariff reductions on imported goods is generally found to increase informality due to increased foreign competition. Numerous studies (reviewed in Table 4.2) show that import competition may lead to formal employment losses, and subsequent reallocation of labour to sectors and occupations where informality is more prominent. This may happen for a variety of reasons, including the fact that local industries may not be mature enough to compete with the influx of better-established enterprises and brands. Import competition may also increase pressure on enterprises to cut costs and therefore cut corners on labour protections, either inducing them to employ labour informally, or outsource their activities to informal enterprises, home-based workers and self-employed micro-entrepreneurs.

Indeed, in Argentina, tariff cuts throughout the 1990s led to an increase in informality in some of the most exposed sectors (Acosta and Montes-Rojas, 2014[24]; Cruces, Porto and Viollaz, 2018[25]). For example, between 1992 and 2003, the import tariff on clothing dropped by 8 percentage points, while the sector's informality rate increased by 30 percentage points. The detrimental effect was concentrated among small enterprises (Cruces, Porto and Viollaz, 2018[25]), whereas industries with high investment rates were able to neutralise and reverse this effect (Acosta and Montes-Rojas, 2014[24]).

Similarly, a reduction in import tariffs was also found to increase informality in Botswana following trade liberalisation within the Southern African Customs Union in the 1990s (McCaig and McMillan, 2020[19]).

In Brazil, recent studies identified an increase in the overall informality level following important trade liberalisation (Bosch, Goñi-Pacchioni and Maloney, 2012[26]; Paz, 2014[20]), including in the medium and long term (Dix-Carneiro and Kovak, 2019[27]), even if formal employment changes within the manufacturing sectors specifically were less affected (Goldberg and Pavcnik, 2003[17]).

In Colombia, although the increase in informal employment was modest (Attanasio, Goldberg and Pavcnik, 2004[28]) and occurred in the setting of rigid labour markets, it dissipated following labour market liberalisation reforms (Goldberg and Pavcnik, 2003[17]).

Two exceptions stand out: Egypt (Selwaness and Zaki, 2015[29]; Ben Salem and Zaki, 2019[30]) and Mexico (Aleman-Castilla, 2006[21]; Ben Yahmed and Bombarda, 2020[22]). These countries experienced a decrease in informality following their own reductions to import tariffs in the trading sector in urban areas. The informality reduction effect in Mexico was, however, observed only among large enterprises with more than 50 employees, with the strongest effect observed in enterprises employing more than 250 people (Ben Yahmed and Bombarda, 2020[22]). Informality reduction occurred due to the formalisation of the existing informal workforce of large enterprises, rather than increased hiring of formal workers by large enterprises.

In South Africa, tariff reductions implemented since 1995 reduced both formal and informal employment among the most exposed workers, thus resulting in an adverse labour market effect but not in a relative increase in informality (Erten, Leight and Tregenna, 2019[31]).

Table 4.2. Effect of a reduction of own import tariffs on informal employment

Country covered	Empirical study	Time period	Focus	Data used to measure informal employment	The reduction in own import tariffs leads informality to…
Argentina	Acosta and Montes-Rojas (2014[24])	1992-2003	Tradable sectors	Household survey (EPH)	Increase on aggregate; decrease for sectors with high investment rates
Argentina	Cruces, Porto and Viollaz (2018[25])	1981-2001	Entire economy	Household survey (EPH)	Increase in sectors most exposed to liberalisation, particularly if the sector is dominated by small enterprises. General equilibrium counteracting effect at aggregate level. Increase in informality also in non-tradable sector.

Botswana	McCaig and McMillan (2020[19])	1995-2006	Entire economy, mining and manufacturing	Labour force survey (Central Statistics Office of Botswana)	Increase
Brazil	Bosch, Goñi-Pacchioni and Maloney (2012[26])	1983-2002	Entire economy	Labour force survey (PME); household survey (PNAD)	Increase
Brazil	Menezes-Filho and Muendler (2011[32])	1986-2001	Tradable sectors	Household survey (PME)	Remain unchanged
Brazil	Goldberg and Pavcnik (2003[17])	1987-98	Tradable sectors	Labour force survey (Monthly Job Survey)	No effect within the manufacturing sectors
Brazil	Paz (2014[20])	1989-2001	Tradable sectors	Household survey (PNAD)	Increase
Brazil	Dix-Carneiro and Kovak (2019[27])	1992-2010	Tradable sectors	Census (IBGE)	Increase, and the effect increases across time, suggesting no reallocation
Colombia	Goldberg and Pavcnik (2003[17])	1984-98	Tradable sectors	Household survey (NHS)	Increase, but a labour market liberalisation cancels the effect
Colombia	Attanasio, Goldberg and Pavcnik, (2004[28])	1984-98	Tradable sectors	Household survey (NHS)	Increase
Egypt	Selwaness and Zaki (2015[29])	1998-2006	Tradable sectors	Egyptian Labor Market Panel Survey (ELMPS)	Decrease
Egypt	Ben Salem and Zaki (2019[30])	1998-2012	Manufacturing sectors	ELMPS	Decrease
Mexico	Aleman-Castilla (2006[21])	1989-2002	Entire economy, urban areas only	Labour force survey (ENEU)	Decrease, but the opposite is true for sectors facing high import competition, unless these sectors also benefit from lower tariffs on their inputs
Mexico	Ben Yahmed and Bombarda (2020[22])	1993-2001	Manufacturing, services, urban areas only	Labour force survey (ENEU)	Decrease, especially for men; increase for low-skilled women in services. Reallocation within and between sectors.
South Africa	Erten, Leight and Tregenna (2019[31])	1994-2004	Entire economy	Labour force survey (PALMS)	Remain unchanged, but overall negative effect on employment (formal and informal)

Note: This table includes non-exhaustive examples of empirical evidence published in peer-reviewed academic journals. In all studies, the effect of trade liberalisation is isolated from other confounding factors.
Source: Authors' compilation.

The aggregate effects hinder important heterogeneity across industries, geographical regions, workers and enterprises

Several studies show that the effect of trade liberalisation is not uniform across the economy, because it usually does not concern all sectors in the same way; because production is often clustered geographically; and because capital reallocation is slow, and labour market mobility is imperfect. Likewise, its effect on the informal economy varies across workers, enterprises, industries, and geographical regions within the same country.

Given that labour mobility between industries is usually low because of worker protection and industry-specific skills, the within-industry effects of trade liberalisation are often larger than the between-industry effects (Attanasio, Goldberg and Pavcnik, 2004[28]; Ben Yahmed and Bombarda, 2020[22]; McCaig and McMillan, 2020[19]). It is the workers in sectors and industries most affected by trade liberalisation who experience more intense competition the most (Goldberg and Pavcnik, 2007[33]).

Workers living in regions with a high concentration of industries that are more involved in trade than others are also affected differently than less exposed regions (Kovak, 2013[34]; Topalova, 2010[35]). For example, in Brazil, regions most exposed to the growth of imports, following trade liberalisation in the early 1990s, experienced more prolonged declines in formal sector employment and earnings relative to other regions (Dix-Carneiro and Kovak, 2017[36]). These regions also saw the greatest rise in the share of informal employment over time. Moreover, the regional dynamics of informal employment were shaped by the interplay of employment in tradable and non-tradable sectors. Formal workers displaced by trade either moved to formal employment in low-paid non-tradable sectors, or – and this is a more systematic effect – first entered non-employment, and then transitioned to informal employment, including in the non-tradable sectors. In fact, if employment fully recovered over time from the trade shock in regions most exposed to trade, this recovery seems to be fully accounted for by the regional increase in informal employment (Dix-Carneiro and Kovak, 2019[27]). Overall, in Brazil, the long-lasting negative impact of import shocks at the regional level can be explained by the combination of a trade shock with a very low level of mobility between regions (Dix-Carneiro and Kovak, 2017[36]). In other words, when facing an import shock, workers are more likely to transition to lower-quality jobs (informal and/or with lower pay) in the same region than to move to another region. The deeper cause of this lack of geographical mobility is not well understood, although it could be related to slow reallocation of capital across regions (Dix-Carneiro and Kovak, 2017[36]). This pattern of low mobility is common in developing economies: internal mobility is generally much weaker in low- and middle-income countries than in high-income countries, according to World Bank research (Grover, Lall and Maloney, 2022[37]). Trade liberalisation may also affect the nature of informality. For example, in the case of Peru, increased import competition pushed informal enterprises out of the market because their productivity was too low to sustain foreign competition. However, at the same time, formal enterprises started hiring workers informally on a more systematic basis as a result of the pressure of the same competition. As the latter effect dominated, the overall share of informally employed workers in the economy increased, even if the share of informal enterprises decreased (Cisneros-Acevedo, 2021[8]).

The expansion of global value chains comes with additional challenges to formal and informal employment

Existing evidence suggests that GVCs have the potential to create opportunities for both higher productivity and better-quality employment, including for women and young workers, by allowing workers to access employment requiring a higher level of skill and knowledge; to move to higher-value activities and markets; and to benefit from better practices of suppliers and employers from multinational companies (Horvát, Webb and Yamano, 2020[38]). The extent to which this is actually happening depends on many factors, however. Challenges to the improvement of working conditions, including formalisation, include the type of linkages that predominate for a specific country (backward or forward), the way production and contractual relationships are organised, the extent to which suppliers and employers comply with national regulations and international labour and quality standards (ILO, 2016[39]), and the possibilities of upgrading within a value chain. For the new entrants into a GVC from the least developed countries, an additional challenge also lies in their limited productive capacities [especially for artisanal and small-scale players; see (McQuilken and Perks, 2021[40])]; in inadequate or the simple lack of infrastructure; in finding their niche in GVCs dominated by a few players from advanced economies; and in obtaining a significant share of the total value added produced along the GVC (OECD, 2018[41]). Given these challenges, the potential for GVCs to improve the quantity and quality of jobs in the least developed countries has, so far, remained limited (AfDB/OECD/UNDP, 2014[42]).

Expansion of forward linkages has the potential to decrease informal employment, whereas the expansion of backward linkages has an ambiguous effect

Expansion of forward linkages, understood in the broad sense as exported intermediate products, would have similar effects to the expansion of total exports. It has significant potential to decrease informal employment, similar to the mechanism outlined in Table 4.2.

The expansion of backward linkages, understood in the broad sense as imports of intermediate products, may have a more ambiguous effect on informality. On the one hand, empirical studies show that the effect of tariff reductions on intermediate products is substantially larger than the effect of tariff reductions on final products, in what concerns enterprise-level productivity and industry growth and innovation [for a review, see Goldberg and Pavcnik (2016[16])]. Not only can such trade liberalisation enable domestic enterprises to buy more of the cheaper intermediate products, but they may also buy a cheaper and higher-quality variety of intermediate products that was not previously available on the domestic market. Foreign technology embedded in these intermediate products has significant potential to increase the productivity of enterprises using them as inputs into their products [as was the case in Indonesia; see Amiti and Konings (2007[43])]. In India, trade liberalisation that encompassed intermediate products enabled domestic enterprises to introduce new products, particularly in sectors that had experienced the largest tariff reductions on their imported intermediates (Goldberg et al., 2010[44]; Topalova and Khandelwal, 2011[45]). The improved access to intermediate products can allow enterprises to preserve and expand activities, as well as employment. The composition of this employment effect – more formal or more informal – is unclear.

On the other hand, these effects are not uniform across formal and informal enterprises. Indeed, providing tariff reductions on intermediate goods seems to be of more benefit to existing formal enterprises; additionally, it leads to the expansion and new entry to the market of formal enterprises that use intermediate goods as inputs for either their final goods or as part of a larger GVC [see Nataraj (2011[46])]. However, if this increases competition with domestic enterprises (whether formal or informal) that are also producing the same type of input, some enterprises may be pushed out of the market. This would lead to loss of employment as well as an increase in informal employment in the non-tradable sector, which would absorb people who are unemployed [an effect similar to that observed in Brazil; see Dix-Carneiro and Kovak (2019[27])].

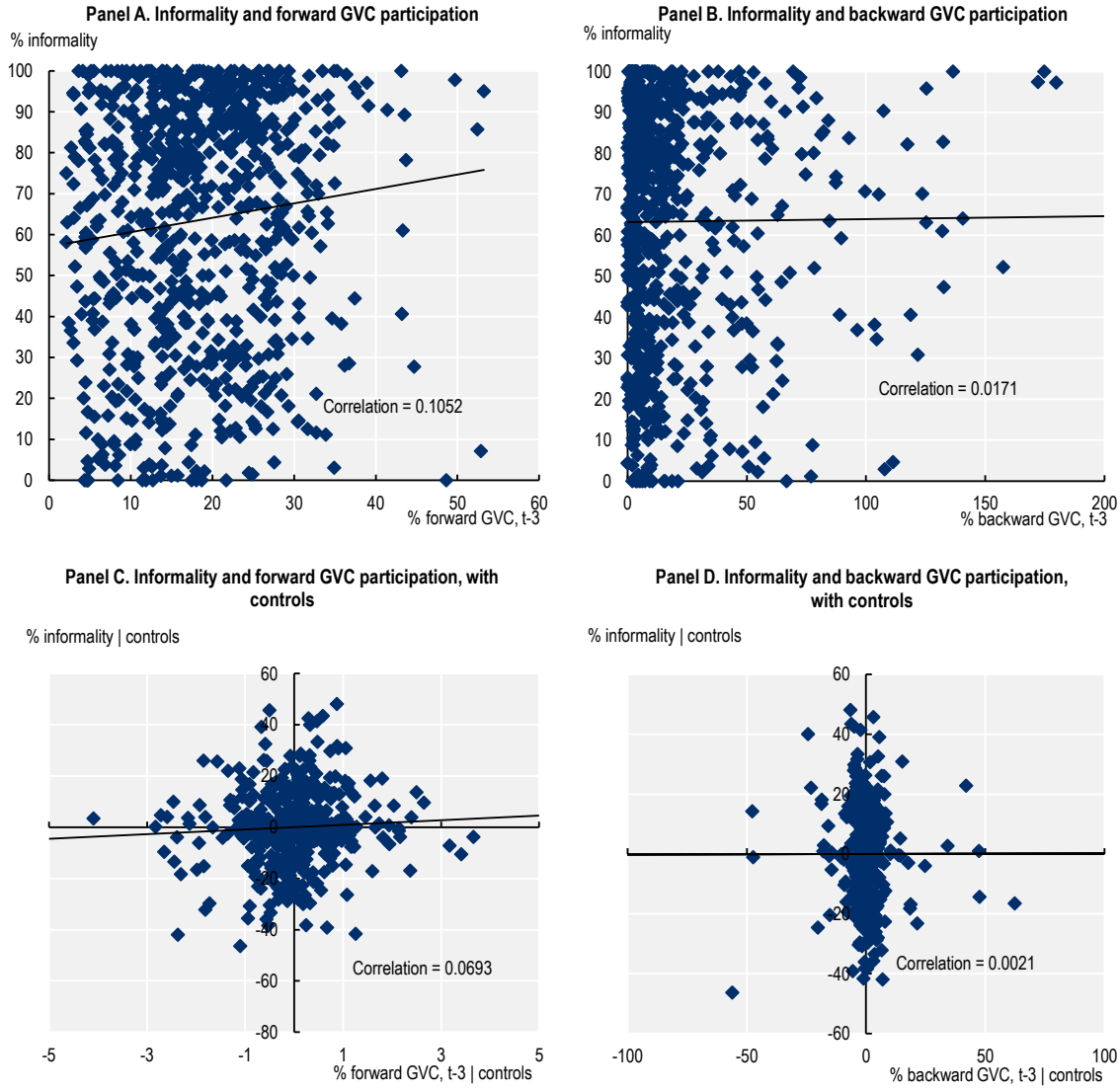
Informal enterprises are usually smaller than formal enterprises, and have a lower rate of using imported goods as intermediate goods. In comparison to formal enterprises, they are less affected by tariff reductions on intermediate goods. For informal enterprises, the reduction in final goods tariffs can increase average productivity by causing the smallest, least productive informal firms to close [e.g. Nataraj (2011[46])]. This again can decrease the share of informal enterprises among enterprises that produce final goods; however, this might not automatically lead to a decrease in informal employment if displaced workers take up informal jobs elsewhere in the economy.

Evidence from Brazil and Mexico shows that lower tariffs on imported inputs indeed lowered the informality share of the industries using those inputs, with the effect concentrated among enterprises facing the highest import penetration with regard to their final products (Menezes-Filho and Muendler, 2011[32]; Aleman-Castilla, 2006[21]). Expansion of backward linkages increased the share of formal enterprises that used cheaper intermediate goods as inputs for final goods production. In the case of Mexico, a likely explanation is that lower Mexican import tariffs reduce costs for US companies operating in Mexico, as it is cheaper to open a plant in Mexico and import intermediate inputs from the United States (Aleman-Castilla, 2006[21]).

This heterogeneity of country-specific findings reported by the academic literature is also confirmed more globally. Figure 4.6 shows the share of informal employment and lagged GVC indicators for more than 900 country/sector/year observations. It shows that there is no clear, strong link between the expansion of

GVCs and informality, whether one considers forward or backward linkages looking at simple correlations or controlling for confounding factors.

Figure 4.6. The relationship between informality and GVC participation is weak



Note: GVC participation is defined as exported value added which crosses at least two borders. Forward GVC participation is the exported value added of the reference country that is re-exported by at least one trading partner. Backward GVC participation is exported value added which is imported by the reference country. Here, forward and backward GVC participations are expressed as a share of the sector's exports and imports, respectively. In Panels A/B, simple correlations are reported. In the lower panel, residual values of informality and GVC participation are reported, controlling for sector-country and year fixed effects, as well as the logarithm of total trade at the sector/country level. Country coverage (multiple years): Argentina, Armenia, Brazil, Burkina-Faso, Cameroon, Chile, Colombia, El Salvador, Gambia, Ghana, Liberia, Madagascar, Malawi, Mali, Mexico, Namibia, Nicaragua, Niger, Peru, Senegal, Thailand, United Republic of Tanzania (hereafter: Tanzania), Uganda, Uruguay, Viet Nam and Zambia.

Source: For the percentage of informal employment at the sector level: OECD (2021[47]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)*, https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm. For GVC indicators: Belotti, Borin and Mancini (2020[13]) based on Eora26 data.

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Production organisation within GVCs may have additional, unique effects on informality

Throughout the world and throughout different value chains, the quality of employment in jobs linked to GVCs depends on many factors. While the amount and type of trade is one factor, the way production is organised, and, relatedly, the employment status of workers are other key factors shaping working conditions in GVCs generally and the formality of employment more specifically.

In a GVC, production activity can be organised in two main ways: (i) lead firms co-ordinate production along the supply chain through direct ownership of their overseas subsidiaries and affiliates; and (ii) outsourcing, where lead firms (buyers) do not have ownership or a direct contractual relationship, except with first-tier suppliers (Abramovsky and Griffith, 2006[48]; ILO, 2016[39]). Increasingly, outsourcing without direct ownership is overtaking lead firms' ownership, and is spreading to sectors where it was not present previously.

In the first scenario, workers are hired in the wholly owned subsidiaries and affiliates of the lead firms. This creates an employment relationship, with lead firms or their subsidiaries and affiliates having a direct responsibility for employees. Lead firms have a high chance of complying with labour regulations in host countries; they can also co-ordinate and control the standards of production and of employment conditions across their subsidiaries. Some multinational lead firms may also have dedicated strategies to ensure decent working conditions through private standards and codes of conduct, as well as training and skills development; in addition, they may offer working conditions more akin to working conditions in their home countries. All enterprises in OECD member countries are in effect encouraged by their countries to operationalise the recommendations of the OECD *Guidelines for Multinational Enterprises* (OECD, 2011[49]). As a result, employment relationships with locally based workers have a higher chance of being formal and of providing decent working conditions. Numerous studies have found that foreign affiliates of multinational enterprises offer better employment conditions than those offered by domestic enterprises, and such affiliates also pay higher wages [for more information, see (Javorcik, 2015[50]; ILO, 2015[51])]. They are also more likely to employ formal labour. At the same time, it is often hard to assess whether there is a causal effect of GVC participation on better working conditions, as enterprises participating in GVCs are usually more productive than non-participating enterprises, and may have already been offering better working conditions before participating in GVCs as lead or supplier firms (ibid).

In the second scenario, that of outsourcing and subcontracting without ownership, buyers do not enter into an employment relationship, and therefore do not have formal responsibility for the supplying company or workers in subcontracted enterprises. The subcontracting practices involve recourse to numerous small and medium-sized enterprises (SMEs), workshops, dependent contractors and home-based workers, often unbeknownst to the lead firms (ILO, 2016[39]). In principle, businesses, regardless of the level of control and ownership, are expected to exercise responsible business conduct and risk-based due diligence, and to use their leverage to change corporate behaviour along the value chain for the better. They have the responsibility to identify, prevent and address risks that negatively affect workers, as they are linked with the suppliers by a business relationship. However, in practice, the lead firms find it challenging to control and enforce compliance with labour regulations in all smaller production units. Workers also cannot necessarily benefit directly from the good practices of the lead firms. Moreover, these smaller production units are excluded – de jure or de facto – from the local labour and social security laws and regulations (Aleksynska and Eberlein, 2016[52]), either because of their size, or because of the particularity of their status (i.e. dependent contractors or home-based workers).

Increased fragmentation of production contributes to the creation and entrenchment of the practice of small-scale production. When SMEs and other small units of production join a GVC, there are often several layers of enterprises that separate them from the lead firm, with the first-tier supplier or even a second-tier supplier mediating the inclusion of the production unit within the GVC (Navas-Alemán and Guerrero, 2016[53]). This "distance" to the lead firm is key with regard to the opportunity to benefit from the good practices of the lead firm with respect to labour protections. This is because the lead firm has fewer

chances to know about the existence of more "distant" production units, and also because of the pressure exercised by the intermediary enterprises in order to reduce costs and deliver quickly (Barrientos, 2013[54]; Navas-Alemán and Guerrero, 2016[53]). In these settings, there is a more frequent recourse to informal work, or to non-standard employment arrangements that are partially or not fully covered by labour regulations. Moreover, low barriers to entry in labour-intensive low-skilled sectors have the potential to increase price competition between suppliers, with a race to the bottom in profits, wages, and working conditions, including formality (ILO, 2016[39]).

Even if the development of GVCs through outsourcing and subcontracting contributes to income generation and employment creation, with SMEs being the primary sources of job creation (including for women and youth), it will not necessarily lead to formalisation or the improvement of working conditions. Suppliers in the lowest tiers risk having the lowest chances of upgrading their working conditions, including formalisation, when compared with suppliers in other tiers.

Purchasing practices in GVCs are one of the main sources of informal employment

The rate of informality among those in temporary employment is five to six times higher, on average, than among workers on open-ended contracts. But is temporary employment itself a possible way for a supplier to adapt to certain purchasing practices? A series of case studies, based on interviews, was carried out by the International Labour Organization (ILO) in five major markets (Bangladesh, China, India, South Africa and Türkiye) across ten sectors in 2017-18 in order to investigate this question. Among surveyed suppliers, 62% confirmed that purchasing practices contributed to their decision to hire temporary workers. Such practices included those that put suppliers in a position where they had no other choice but hiring temporary labour: inappropriate lobbying (71%), poor forecasting, and excessive sampling, among others (ILO, 2021[55]). Since many company initiatives are related to brands, and brands are the ones that, to a large extent, define the purchasing practices, understanding the role of purchasing practices in informality is one of the keys to tackling informality.

Possibilities of upgrading in GVCs can improve formalisation as well as the living standards of informal workers; however, they are not automatic

Increased participation in GVCs, as well as their proliferation and evolution, have created expectations of economic as well as social upgrading of regions and of workers employed by developing country suppliers and subcontractors (ILO, 2017[56]). Social upgrading through participation in GVCs is viewed as a combination of employment growth and improvement in wages and other working conditions (Milberg and Bernhardt, 2013[57]). Social upgrading is often linked to upgrading within the value chains, and this upgrading falls into one of three categories: upgrading of processes, upgrading of products, and upgrading of functions (Humphrey and Schmitz, 2002[58]; Humphrey and Schmitz, 2000[59]; Navas-Alemán, 2011[60]). Process upgrading involves doing certain tasks better, and can be measured by better management techniques, worker training and skill upgrading, and adopting better social practices, among others. Product upgrading means producing a product of better quality and of higher value. Functional upgrading happens when the supplier acquires new functions in the value chain activity that it did not possess previously, such as internalising product design, launching a new brand, or co-ordinating its own supply chain.

Process upgrading has the greatest potential to result in social upgrading (ILO, 2017[56]).[2] Notably, better working conditions (such as OSH), but also wages, written contracts and formal arrangements, can all be part of process upgrading. Unfortunately, if product upgrading remains limited for many least developed countries (OECD, 2018[41]), process upgrading is even rarer. This is because process upgrading represents an additional cost to the lead firm, but is not visible to the final consumer, whereas product upgrading responds to consumer demand for better-quality products. This is especially true in sectors such as agro-food. Dedicated policy efforts to increase consumer awareness, including with the support of local and

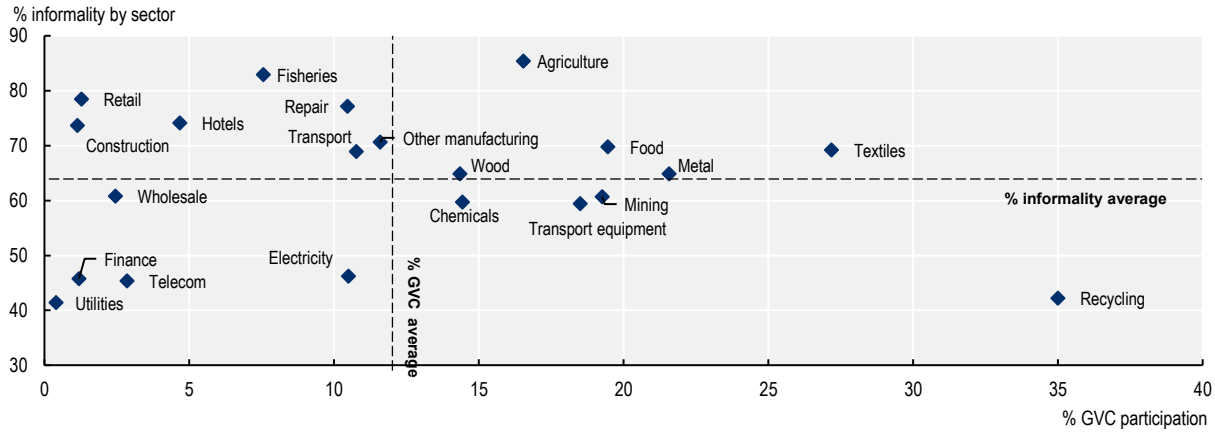
international non-governmental organisations (NGOs), may be a powerful way of ensuring that both product quality and employment quality issues are considered seriously throughout the GVC.

Informality in GVCs remains highly sector specific

The amount of trade, the way production is organised, upgrading process and governance issues also differ tremendously from one sector to another. In addition, inherent specificities of each sector continue to leave a major footprint on the share of informal employment in a specific GVC. Figure 4.7 relates total GVC participation to the percentage of informal employment in 26 sectors, averaged over 25 developing countries with the most recent available data. Figure 4.8 also looks separately at forward and backward linkages. Considering this relationship, one can identify four types of sectors: (i) sectors with higher-than-average levels of informality and of GVC participation (agriculture, food and beverages, textiles, wood, and metals); (ii) sectors with lower-than-average levels of informality and of GVC participation (utilities, electricity, and certain higher-value-added services such as finance and telecommunications); (iii) sectors with higher-than-average informality but lower-than-average GVC participation (fishing; lower-value-added service sectors such as retail, hotels, repair, construction, transportation and other manufacturing); and (iv) sectors with lower-than-average informality but higher-than-average GVC participation (chemistry, transportation equipment, mining and recycling).

Employment across sectors and occupations also varies greatly for men and women. Given this situation, integration into the GVC, coupled with the informality footprint in each specific value chain, can have a differentiated effect for men and women (ILO, 2015[51]). In many countries, women tend to be more concentrated than men in lower-wage, lower-status forms of employment. In addition, whether and how women benefit from possible GVC-induced employment depends on the specific sector, occupation and production mode therein.

Figure 4.7. Total GVC participation and informality, by sector

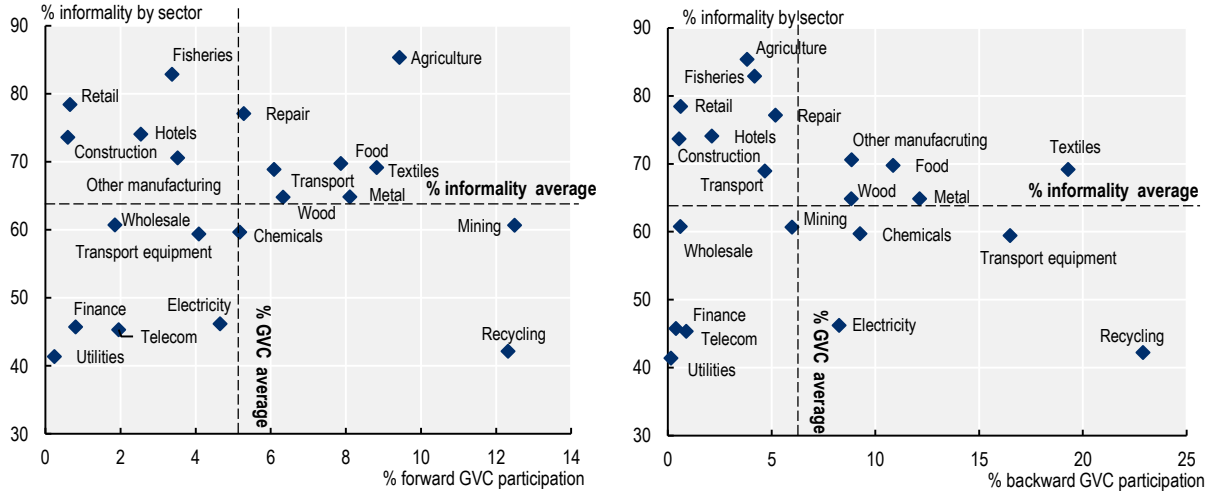


Note: GVC participation is defined as exported value added which crosses at least two borders. Here, GVC participation is expressed as a percentage of value added. Country coverage: Argentina (2018), Armenia (2016), Brazil (2018), Burkina-Faso (2014), Chile (2017), Colombia (2018), El Salvador (2018), Gambia (2015), Ghana (2013), Liberia (2016), Madagascar (2012), Malawi (2016), Mali (2012), Mexico (2018), Namibia (2015), Nicaragua (2014), Niger (2014), Peru (2019), Senegal (2011), Tanzania (2014), Thailand (2017), Uganda (2015), Uruguay (2018), Viet Nam (2016) and Zambia (2015).

Source: For the percentage of informal employment at the sector level: OECD (2021[47]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)*, https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm. For GVC indicators: Belotti, Borin and Mancini (2020[13]) based on Eora26 data.

StatLink https://stat.link/iv7hn5

Figure 4.8. Forward and backward GVC participation and informality, by sector



Note: GVC participation is defined as exported value added which crosses at least two borders. Forward GVC participation is exported value added of the reference country that is re-exported by at least one trading partner. Backward GVC participation is exported value added which is imported by the reference country. Here, forward and backward GVC participations are expressed as a percentage of value added. Country coverage: Argentina (2018), Armenia (2016), Brazil (2018), Burkina-Faso (2014), Chile (2017), Colombia (2018), El Salvador (2018), Gambia (2015), Ghana (2013), Liberia (2016), Madagascar (2012), Malawi (2016), Mali (2012), Mexico (2018), Namibia (2015), Nicaragua (2014), Niger (2014), Peru (2019), Senegal (2011), Tanzania (2014), Thailand (2017), Uganda (2015), Uruguay (2018), Viet Nam (2016) and Zambia (2015). Source: For the percentage of informal employment at the sector level: OECD (2021[47]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)*, https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm. For GVC indicators: Belotti, Borin and Mancini (2020[13]) based on Eora26 data.

StatLink https://stat.link/2uc9zs

GVCs stemming from agriculture have some of the largest footprints of informal employment

The agriculture sector is increasingly organised within GVCs (OECD, 2020[61]). While the agriculture sector represents a relatively small share of total GVC trade globally [with agriculture exports accounting for just 2% of world exports in 2014 (World Bank, 2020[62])], several countries witnessed significant growth in their agriculture sector in 2000s and 2010s.

The agriculture sector is part of a multitude of GVCs. It has backward linkages, which connect the agriculture sector to chemical and input industries producing seeds, fertilisers and pesticides; to education, research and development, producing agriculture scientists; and to equipment manufacturers producing tractors and other equipment, to name a few. It also has forward linkages, through which agricultural produce is further processed (i.e. used as inputs in the manufacturing of food, beverages, tobacco, clothing, fibre or fuel), transported, marketed, retailed, or used in the restaurant industry and catering.

One of the characteristics of agricultural sector products feeding into GVCs is that, unlike in other sectors, domestic value chains dominate GVCs, especially in what concerns food production, because most of the food production is consumed locally. Even when agricultural food products cross borders, often it is to be used as an intermediate in the final good for the domestic market of the first importing country (Greenville, Kawasaki and Beaujeu, 2017[63]). In other words, the forward GVC of the agriculture sector tends to be relatively short and less complex than the GVCs in other sectors. However, forward participation is also more important than backward participation, especially in developing countries, as shown in Figure 4.8 (OECD, 2020[61]).

Another characteristic is that there is substantial heterogeneity across countries in terms of the diversity of agriculture subsectors participating in GVCs, and therefore there is substantial heterogeneity in the employment effects of GVCs. Some countries have a strong specialisation: for example, in Malaysia, GVC engagement in the agricultural sector is influenced mainly by one commodity: palm oil (OECD, 2020[61]). A similar situation is observed in Colombia (bananas), Côte d'Ivoire and Ghana (cocoa), and Ethiopia (coffee). In other countries, several sectors may participate in GVCs.

Global estimates suggest that trade and agro-food GVCs generate about one-quarter of total agricultural workforce returns (OECD, 2020[61]). Among agriculture subsectors, wool, oilseeds and plant-based fibres feature the greatest employment reliance on trade and GVCs, while account for up to one-half of all employment.

Shifting from simple agriculture to higher-value-added industries is a common priority in many countries in Asia, such as Cambodia, Lao People's Democratic Republic, or Myanmar (ASEAN Japan Centre, 2020[64]), as well as in Africa (AUC/OECD, 2021[65]). These are the sectors that have the most significant potential for additional employment creation, including of better-quality jobs for women and youth, and for skills development.

In many developing countries, the evolution of the GVC in agriculture has been taking place not only through the increase of the yields and exporting of agricultural produce, but also through the upgrading of the quality of products and processes, and through improving capacities in the parts of the value chain beyond agriculture production, such as packaging and food processing, the restaurant industry, and catering. In Asia and in Latin America and the Caribbean (and, to a lesser extent, in Africa), the period since the 1980s seen a rapid development of supermarkets and of new SMEs in the food sector, such as chain restaurants, processors, and modern wholesale and logistics companies (Reardon and Timmer, 2012[66]). GVC participation has the potential to create employment in all parts of the value chain. About one-fifth of the total returns to labour generated by agro-food exports flows to the services sector, including transportation, retail and wholesale trade, and financial and business services (OECD, 2020[61]). In developing Southeast Asia, the multiplier effect of food products industries is significant: in Viet Nam, for example, when demand for food products increases by one million Dong, the economy grows by 2.5 million Dongs (ASEAN Japan Centre, 2020[64]). As a consequence, employment creation occurs throughout multiple sectors.

Despite this evolution, GVCs originating in agriculture account for the largest shares of informal employment when compared with any other type of GVC.

This is related to at least two key reasons: the pervasive informality in the first part of the value chain (namely agriculture production), and the organisation of the GVC, which does not encourage the transition to formality.

Indeed, in 2019, the first part of this GVC – agriculture production – still employed 32% of all workers in low- and middle-income countries, even though this share had decreased by 22 percentage points since 1991 under the effects of structural transformation (ILO, 2021[67]). Agriculture also remains the sector that has the highest share of informal employment.

The vast majority of agricultural production is organised through small-scale smallholder farming (OECD/FAO, 2019[68]; OECD, 2020[69]). Farmers are generally self-employed. In many developing countries, existing social security systems are either not adapted to this employment status, or not adapted to the agriculture sector specifically (or sometimes both). This means that, by definition, farmers in many developing countries are informal. Often, farms also employ farmers' contributing family members.

Farmers participating in a GVCs increasingly hire workers to help meet demand and increase production in fields and plantations. Some agricultural production is also organised through larger family enterprises, farmers' organisations and co-operatives. Some multinational companies have also invested in land and directly manage farms, thereby raising wage employment in agriculture.

Nevertheless, wage employment – which would be more prone than self-employment to formalisation – remains limited. Moreover, even among the wage employees in formal agriculture enterprises, informality is the norm rather than the exception (World Bank, 2020[62]). For example, a cross-country review of 49 studies related to the commodities and horticulture value chains showed that informal workers make up the majority of the workforce, even in formal enterprises (Chan, 2017[70]). Due to the seasonal nature of production (which is sometimes extreme, e.g. lychees in Madagascar (ILO, 2017[56])), large shares of employees are employed on a casual or seasonal basis. This means that workers in such jobs often do not enjoy full employment protection, and may not be subject to social protection, which again renders them informal. Moreover, current evidence from a range of developing countries shows a high prevalence of short-term contracts in the agriculture sector in those countries [for example, in Peru, this is the case for 79% of all men and 84% of all women working on artichoke farms and processing plants (World Bank, 2020[62])]. Evidence from Côte d'Ivoire and Ghana on participation in the pineapple and cocoa value chains also showed that participation in GVCs is associated with an increase in hiring of casual labour (Amanor, 2012[71]). But even among workers who do have a longer-term contract, such contracts are often based only on an informal oral agreement (Dihel et al., 2018[72]), which is usually more difficult to enforce or contest in courts when problems arise.

In addition to this, the organisation of production in a GVC, with some exceptions, generally follows the scenario of outsourcing and subcontracting without ownership of the lead firms in the GVC. Over the period 2018-19, the OECD, jointly with the Food and Agriculture Organization of the United Nations (FAO), conducted a survey of companies interested in implementing OECD-FAO Guidance for Responsible Agriculture Supply Chains. The companies that took part in this survey were all multinationals, and their voluntary participation meant that they were most probably self-selecting given that they were aware of potential labour problems in the GVC. The survey findings showed that, even among these companies, 75% were sourcing from hundreds and even thousands of smallholder farmers, often with no possibility of fully tracing them. For one-half of companies sourcing from smallholders, smallholders' produce represented a majority of the company's production (OECD/FAO, 2019[68]).

Indeed, farmers typically do not directly supply their products to multinational enterprises that are part of the GVC. Rather, enterprises source products from third-party suppliers that act as intermediaries. Such intermediaries can include local or international commodity traders, aggregators, wholesalers, and markets/exchanges, aggregating commodities in specific points in the supply chain (OECD/FAO, 2019[68]). This has a double consequence on the employment conditions of farmers. On the one hand, for multinational companies, it is usually difficult to fully map and trace supplying farmers (OECD, 2020[73]), and therefore participate to the improvement of their working conditions. On the other hand, many farmers participating in export-related production, including in GVCs, find themselves in the position of being dependent contractors with limited insight or access to market. Even if they may be officially registered as self-employed, paying taxes and social security contributions, they have only one main client (the intermediary) who sets the price for the products. In some instances, this client also controls other aspects of production. This dependency may have adverse long-term consequences if the farmer has limited bargaining power over prices or the quantity of goods. Small-scale farmers may not have enough power to bargain individually. In some countries, they may also be precluded from bargaining jointly, on the grounds of anti-monopoly laws forbidding them to form cartels. As a result, farmers may not be able to increase their profits as much as they could have. In addition, the responsibility between the dependent contractor and the client is not shared, especially with regard to OSH, fundamental rights and principles of work, or social protection (and thus, formality).

The share of informal employment in other parts of agriculture GVCs is also sizeable. For example, processing of agricultural produce (such as rice), pre-processing (such as shrimp peeling), or packaging is often done by subcontracted home-based workers, often women and children (World Bank, 2020[62]). Indeed, agriculture comprises 16% of homebased employment globally, and up to 30% in Eastern, Southern Europe and Central Asia, 33% in Southern Asia, and 39% in the Middle East and North Africa;

with most of it being informal (Bonnet et al., 2021[74]). In much of the developing world, final food preparation – including of the exported food that serves as intermediate input – is done on the street and in small-scale restaurants (ILO, 2021[75]). Restaurants, catering services and food delivery services increasingly feature disguised employment relationships – informal by definition – especially with the advent of digital apps.

Textiles and clothing GVCs embody the hopes and criticism attached to globalised manufacturing processes

As shown in Figure 4.8, textiles and clothing is a sector with higher-than-average backward and forward GVC participation, combined with high levels of informal employment (Figure 4.7). While the exact magnitude of informal employment involvement in this GVC's production processes is difficult to assess, linkages have been clearly documented (Labowitz and Baumann-Pauly, 2014[76]).

The industry is both a key influencer of labour-intensive export-led growth and, at the same time, the source of multiple scandals relating to working conditions at the lower-value-added parts of its value chain. Significant prevalence of informal employment has been identified, in particular in leather stitching and intricate handwork, such as embroidery and beading, as well as in upstream sectors such as cotton harvesting, often involving homework (OECD, 2018[77]). Child labour and forced labour have also been recorded in textile and clothing GVCs, according to a joint research effort by the ILO, OECD, the International Organization for Migration (IOM), and the United Nations Children's Fund (UNICEF) (2019[78]). As such, the sector embodies the hopes and criticism attached to globalised manufacturing processes.

Textiles production is structured across complex value chains that involve an international division of stages of production. These multiple stages differ greatly in terms of skill content and capture of the total value added. Thus, textiles production represents a clear example of a "smiling curve": a setting where the upstream (research, design) and downstream (retail) parts of the value chain capture larger added-value shares than the middle (manufacturing) part of the value chain (Frederick, 2010[79]). Manufacturing stages are themselves heterogeneous: synthetic textile fabrics production – which represents the vast majority of all fabrics[3] – is capital intensive and is concentrated in high- and upper-middle-income countries, with China, Germany and the United States being the top exporters in 2019.[4] By contrast, apparel production is much more low-skill and labour-intensive, in particular the "cut, make and trim" stage. Its exports are concentrated, besides China, in lower-middle-income countries, namely Bangladesh and Viet Nam.[5] As will be discussed, it is this part of the value chain where the highest level of vulnerabilities are found, including regarding informal employment.

The textiles and clothing trade experienced a dramatic increase between 1994 and 2005, when the importing quotas system for these products (the Multi-fibre Arrangement and the Agreement on Textiles and Clothing) was progressively phased out (Lopez-Acevedo and Robertson, 2012[80]). Over this period, Asian economies became key players in the industry, particularly in China, where textile exports grew 306% between 1995 and 2005. By contrast, countries originally favoured by the quotas system, such as Mexico, lost market power (ibid.).

Since then, textiles and clothing have been seen as the archetypal examples of means to achieve export-led growth and integration in international trade (ASEAN-Japan Centre, 2020[81]). This trend is characterised by notable upsides, including that workers in the industry tend to benefit from a wage premium for their level of skill (Robertson et al., 2009[82]). In the case of Honduras for example, *maquilas*, assembly enterprises concentrated in the textiles and clothing area, contributed to a 1.5-percentage-point reduction in poverty (de Hoyos, Bussolo and Núñez, 2008[83]). As an industry that employs a large share of women, the development of export-led garment manufacturing has had a positive effect on gender equality: in Bangladesh, households in villages more exposed to the garment manufacturing boom were more likely to favour girls' school enrolment, as a consequence of the higher expected returns on skills

development (Heath and Mushfiq Mobarak, 2015[84]). A link between better access to export markets and formalisation in textiles and clothing is also documented (McCaig and Pavcnik, 2018[23]): the 2001 Viet Nam-USA bilateral trade agreement resulted in a major decrease in tariffs on the manufacture of textiles and clothing, which is believed to have caused a large drop in informal employment in the sector.

The vulnerabilities of employment in textiles and clothing value chains were highlighted by the collapse of Rana Plaza, an eight-storey commercial building containing a garment factory, on 13 April 2013 in Dhaka, Bangladesh. The related death of 1 132 workers and injury of more than 2 500 workers sparked an international outrage and came as a shock to both multinational sourcing companies and their consumers. This specific incident reveals broader challenges regarding labour rights and working conditions in textiles and clothing value chains.

Garment manufacturing enterprises' tendency to subcontract parts of orders is a pervasive practice aimed at responding flexibly to changes in demand. It is a vector through which informal employment is likely to feed into GVCs through the sourcing from small informal enterprises and from home-based workers. Globally, craft and trades (which include, among others, handicraft, garment and related crafts), are the second major occupation for home-based workers, after services and sales. Twenty-nine percent of the 260 million home-based workers are found in these occupations (Bonnet et al., 2021[74]). In India alone, it is estimated that 5 million home-based workers are engaged in production for garment and textile supply chains (Anner, 2019[85]). This creates a strong likely link between informal employment and GVCs, as 90% of home-based workers (across all sectors) in 2019 in middle- and low-income economies were informal workers. This figure is based on surveys carried out in 69 countries; the corresponding figure for all workers in the same survey sample was 77% (ILO, 2021[75]).

The COVID-19 pandemic had a disruptive impact on textiles and clothing value chains, as textile companies worldwide reported that globally, orders dropped by 31% on average in 2020, with South America (-41%) and Africa (-38%) facing the sharpest declines (ITMF, 2020[86]). The crisis had a major adverse effect on informal workers. In particular, informal home-based workers suffered simultaneously from a collapse in inputs (i.e. fabrics) largely supplied from China and abrupt lockdowns which made it impossible to bring material home to carry out tasks (WIEGO, 2021[87]). Additionally, informal home-based were generally ineligible for COVID-19 pandemic relief schemes in most countries (ibid.).

In order to tackle vulnerabilities related to textiles and clothing industry working conditions, a range of initiatives by multilateral, national and private actors have been developed.

Increasingly, trade agreements play a key role in promoting decent working conditions. For example, the European Union's reviewed Trade and Sustainable Development policy aims at promoting, in trade agreements, the implementation of "international labour conventions […] including respect of core principles of the International Labour Organization (ILO)" (European Commission, 2022[88]). Trade agreements' labour provisions can play a role in improving working conditions in textiles and clothing GVCs specifically. Introduced originally as a provision in the 2006 Cambodia-USA 2006 Trade and Investment Framework Agreement, the ILO and the International Finance Corporation's Better Work programme aims to improve management practices and compliance with national legislation across 1 700 garment factories in 9 countries. An independent assessment concluded that the programme had made a positive impact on reducing the prevalence of harassment at work, increasing wages, and improving workers' household living conditions (ILO and IFC, 2016[89]).

A range of voluntary and legally binding due diligence standards have emerged. Adopted in 2017, the *OECD Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear Sector* establishes a common understanding of due diligence in the sector to help enterprises meet the due diligence expectations set out in the *OECD Guidelines for Multinational Enterprises*. The Guidance provides advice in terms of responsible purchasing practices, in particular to develop pricing models that account for the cost of decent wages (OECD, 2018[77]). In Bangladesh, since the Rana Plaza disaster, buyer-supplier relations and the actions of lead firms with respect to labour governance are believed to

have evolved favourably (Schüßler et al., 2019[90]). The 2013 Accord on Fire and Building Safety in Bangladesh, a legally binding agreement between lead firms, employers and trade unions to promote occupational safety and health in the textiles and clothing industry, is believed to have played a role in this evolution. At the national level, its adoption is associated with longer-term subcontracting relations, and improved workers' outcomes, namely regarding occupational safety and social benefits (ibid.). Among lead firms, the Accord is believed to have led to revisions in supply chain and sourcing policies among Australian and German enterprises (Schüßler, Frenkel and Wright, 2018[91]). In 2021, the 2013 Accord was superseded by the International Accord for Health and Safety in the Textile and Garment Industry (International Accord, 2023[92]). This new framework covers a broader set of occupational health and safety measures. Originally focused on Bangladesh, the Accord has been expanded to Pakistan in 2023 (ibid.).

Key policy messages

For much of the developing world, integration into the global economy creates significant economic opportunities as well as challenges in terms of handling adjustment dynamics and distributional consequences. The benefits of trade, including through GVCs, do not accrue automatically. Their adverse effects, among others, can manifest themselves in an increase in, or persistence of, informal employment, depending on the context. Often, the impact of trade on the informal economy cannot be separated from its impact on employment in general. The trade composition, supply capacities, details of trade liberalisation scenarios, the way production within the GVCs is organised, the governance modes, the possibilities of upgrading within and across the GVCs, the purchasing practices, and the sectors of activity and other specific circumstances such as labour market conditions determine the direction of the effect of trade on employment, and on informality.

The role of governments in mitigating the adverse effects, and sharing the benefits of trade on a more equitable basis, is paramount

Reinforcing the social contract in the open economy requires ensuring that governments have the will and the means to play their role of leaving no one behind. Of course, the fact that informality low levels of development also means that capacity constraints are not uniform across countries.

This chapter showed that, in regions and industries affected by trade shocks, informal employment is rarely a choice on the part of workers. Rather, it is often an individual worker survival strategy – as in the case of Brazil, where formal workers displaced by trade enter into informal employment after prolonged non-employment. In such cases, trade liberalisation should be accompanied by adequate social protections such as unemployment support and active labour market policies, including training and skills development. The use of targeted measures is important in order to create local work opportunities in regions with experienced major trade shocks; to create support programmes with a special focus on the most affected regions, workers, industries and occupations; to provide better information on available jobs in other regions and sectors of the economy; to ensure reskilling; and to support inter-regional labour mobility.

By creating new employment opportunities in some regions and sectors, and also by displacing workers in others, globalisation modifies the demand for skills and the skill composition of the workforce. The extent to which this new demand can be met, and skills properly matched, also relates to the issue of informality. Related studies also show that trade-related employment destruction affects disproportionately unskilled workers (for a review, see Marcolin and Squicciarini (2017[93])), who usually have fewer opportunities to receive formal training, or whose informally obtained skills may not be recognised. In this regard, the following are particularly relevant as complementary policies to trade liberalisation and GVC promotion policies: the availability of vocational training to adult learners (including special provisions for women and

migrant workers); life-long learning targeting skill changes arising from globalisation; the anticipation of skills changes in a country's changing production structure; and skill recognition policies.

Trade liberalisation may also create tight competition among formal enterprises, pushing them to cut corners on labour protection – as in the case of Peru, where formal enterprises started hiring more informal workers following trade liberalisation. In this case, effective labour inspection (with corresponding budgets to carry out inspections) and enforcement of current regulations may be one of the remedies. Regulations should also be conceived and regularly revised through social dialogue with workers and employers.

Trade-induced formalisation, when it happens, occurs primarily through the expansion of existing formal enterprises, formalisation within formal enterprises, and the new entry of enterprises directly into the formal sector, rather than the formalisation of existing less productive informal microenterprises. In such circumstances, there is a strong case for the introduction of policies that ease formal enterprise creation, including decreasing the administrative burden of their creation and the time needed for registration. Support for innovation and the provision of easier access to credit are also important in this regard.

Accompanying trade development within GVC, with the aim of reducing the incidence of informal work and reducing the vulnerability of informal workers should also be done by:

- promoting the use of written rather than oral contracts by foreign enterprises and their local suppliers
- developing policies to regulate sub-contracting and ensure fair treatment of locally employed workers, including dependent contractors
- raising awareness among businesses about the existence of *OECD Guidelines for Multinational Enterprises* (OECD (2011[49]) and *OECD Due Diligence Guidance for Responsible Business Conduct* (OECD, 2018[94]), as well as OECD due diligence recommendations in specific sectors and supply chains, including minerals, agriculture, garments and footwear, extractives, and finance; and working with businesses to ensure that they see value in adhering to the principles prescribed therein. To the extent possible, integrating these frameworks into national binding regulations
- recognising home-based workers and their homes as workplaces
- making voices of different actors, including informal workers' organisations, heard; including them in policy formulation, as well as into the design and oversight of enforcement mechanisms

For these policies to succeed and for the welfare-augmenting effect of integration in the global economy to materialise, a range of other actors also need to be mobilised

Governments are not the only actors responsible for addressing the deficiencies in the social contracts that are influenced by global developments. Strong social contracts presume a reciprocity of obligations between all actors in the society, including government, businesses and the public.

In this regard, the role of multinationals is also key to ensuring formal employment in their subsidiaries, and in promoting and encouraging formal employment and decent work for all workers among the multinationals' suppliers. Multinationals' suppliers' compliance with international and local laws and regulations, the implementation of good practices of formal labour employment from their home countries, and having responsible business conduct embedded within business decisions, operations, and supply chains are key in this respect. Moreover, the purchasing practices of some companies are identified as one of the factors in the potential rise of informal employment. Raising awareness of this, and taking steps to modify purchasing practices in order to improve forecasting can be a viable tool to reduce informality.

International frameworks, such as the United Nations' (2011[95]) *Guiding Principles on Business and Human Rights*, the ILO's (2017[96]) *Tripartite Declaration of Principles concerning Multinational Enterprises*

and Social Policy, and the *OECD Guidelines for Multinational Enterprises* (OECD (2011[49])), contain recommendations on due diligence for responsible business conduct.

The *OECD Due Diligence Guidance for Responsible Business Conduct* (OECD, 2018[94]), based on the OECD Guidelines, contains specific recommendations that help enterprises implement the Guidelines. These recommendations are enforced by governments on the multinational enterprises operating in their countries or from bordering countries. They aim to help enterprises conduct due diligence in order to identify, prevent or mitigate, and account for current and potential adverse impacts of their activities, consistently with applicable laws and internationally recognised standards. To date, the OECD Guidelines is the only multilaterally agreed and comprehensive code of responsible business conduct that governments have committed to promoting. The OECD Guidelines recognise that businesses create value by generating employment and bringing expertise, technology and financing capacities to regions in order to increase production sustainably and upgrade supply chains. Nevertheless, it is also recognised that businesses have a responsibility to conduct due diligence to identify and prevent risks impacting people and the planet. It contains practical recommendations that help enterprises operationalise the framework for risk-based due diligence in their own operations, supply chains and business decisions. These recommendations are addressed by governments to multinational enterprises operating in their countries or from other adhering countries. They aim to help enterprises conduct due diligence in order to identify, prevent or mitigate, and account for actual and potential adverse impacts of their activities, consistently with applicable laws and internationally recognised standards.

With respect to informal employment specifically, the *OECD Due Diligence Guidance* contains specific examples of adverse impacts of the actions of multinationals on human rights and on employment relations. The *OECD Due Diligence Guidance* explicitly recognises that due diligence should concern the interests of stakeholders affected by enterprises' activities, such as "workers and employees including under informal arrangements within supply chains and trade unions" (OECD, 2018[94]). To help enterprises identify operations that require prioritisation of assessments, the *OECD Due Diligence Guidance* suggests considering "the operation or business relationship [which] involves an activity or production process that is higher risk (characterised by high employment of informal work, use of hazardous chemicals, use of heavy machinery, etc.)" (OECD, 2018[94]). Finally, the *OECD Due Diligence Guidance* also recognises that some sectors may be more prone to the risk of informal employment and may require dedicated attention to those risks: "for example, garment products with beading or embroidery hold a higher risk of informal employment and precarious work" (OECD, 2018[94]).

The OECD has also developed due diligence recommendations in specific sectors and supply chains, including minerals; agriculture; garments and footwear; extractives; and finance. These international frameworks for multinationals are not binding, however. For this reason, it is particularly important to raise awareness among businesses about the existence of these recommendations, and to work with them to ensure that they see value in adhering to the principles prescribed therein. However, some countries have integrated these frameworks into national binding regulations, which aim to enable multinationals to operate on a level playing field [e.g. France, with its Duty of Vigilance law; see also other examples in (Broembsen and Harvey, 2019[97])].

Disengagement from a business relationship may be appropriate as a last resort after failed attempts at preventing or mitigating severe impacts; when impacts are irreversible; when there is no reasonable prospect of change; or when severe impacts or risks are identified and the entity causing the impacts does not take immediate actions. The decision to terminate a business relationship largely depends on the circumstances and the risk appetite of the supply chain actors, but companies are expected to exhaust other mitigation options before disengaging (OECD, 2019[98]).

There is also a need to encourage more transparency within multinational enterprises; for example, through reporting publicly (which is a key component of the *OECD Due Diligence Guidance*), and through

social audits, such as the ones conducted by enterprises that participate in the ILO and the International Finance Corporation's Better Work programme.

In addition to multinationals, other actors – including consumers, informal worker associations and NGOs – can help to ensure that integration into the global economy is beneficial for all.

One of the key determinants of making progress towards addressing informality is strengthening the voice and bargaining power of informal workers. There is a lot of focus in the GVC on the first-tier supplier, whereas informality is much more prominent in lower-tier suppliers. Informality is simply invisible for some workers, such as home-based workers. For this reason, it is important to help informal workers to make their voices heard and to enable them to participate in policy formulation, as well as into the design and oversight of enforcement mechanisms, as they are much more knowledgeable about their needs (Broembsen, 2022[99]).

This chapter has also demonstrated that within a GVC, upgrading of processes has the most significant potential to stimulate a transition towards formality, and to improve outcomes for informal workers. However, process upgrading is often the most difficult type of upgrading to achieve, as it is the least visible to the consumer. In this respect, consumer awareness regarding working conditions at the very bottom of the value chain can help to create the necessary momentum for improving working conditions and increasing formalisation.

Process upgrading is also linked to process traceability. Some GVCs have too many suppliers, and it may be prohibitively costly for individual lead firms to establish effective process traceability. In such cases, process traceability can be pursued by working with local NGOs in countries where products are sourced. Enterprises can also identify control points in the value chain and conduct an assessment of the due diligence actions of these entities. Also promising are collaborations in industry-wide initiatives through collective action among branded manufacturers, which can facilitate reaching out to a wider community in more uniform ways (ILO, 2017[56]). In some instances, a "landscape approach" may be useful, whereby social risks (including informal employment) may be identified through a geo-sociological analysis, accounting for the rural dimension, among others, rather than site-by-site assessments of each individual supplier (OECD/FAO, 2019[68]).

Finally, informality remains highly sector specific. Some sectors are more prone to informality than others. In some sectors, such as agriculture, informality is an "old", inherent problem. In others, it is "acquired", as a consequence of displacement or tight competition caused by globalisation, among other factors. Some new sectors and occupations that emerge may be fully informal from the outset. Given this situation, sector-specific approaches to informality should be particularly encouraged, taking into account its sector-specific root causes. Such approaches have the greatest potential to succeed if they are implemented in collaboration with informal workers' organisations, including those operating within specific sectors.

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Notes

[1] For a limited subset of countries, data are also available for the mid-2000s (Argentina, Colombia, Mexico, South Africa and Republic of Türkiye (hereafter: Türkiye). In these countries the risk of informal employment feeding into exports generally (measured by the sum of informal employment and employment embodied in foreign demand) appeared to slightly decrease in most cases between the mid-2000s and 2018. This very limited number of observations should not lead to any general conclusions, however.

[2] Examples of process and of other types of upgrading in food and agriculture value chains in Colombia, Indonesia and Madagascar can be found in (ILO, 2017[56]).

[3] Synthetic textile fabrics production represented 62% all fabrics production in 2020 (Textile Exchange, 2021[101]). Fabrics from natural fibres are less capital intensive and more tied to low- and middle-income countries.

[4] Source: Observatory of Economic Complexity (2022[100]) based on “Base pour l’Analyse du Commerce International” (BACI) by “Centre d'études prospectives et d'informations internationales" (CEPII).

[5] ibid.

5 Digital labour platforms: Opportunities and challenges for formal employment

Digital labour platforms have emerged as a new way of organising work. Thus far, their impact in terms of formal employment creation remains rather disappointing. This chapter discusses the typology of digital labour platforms that mediate work and shows how digital labour platform workers were affected by the COVID-19 pandemic. It then examines factors that increase the risk of informal employment on various digital labour platforms, and suggests ways in which digital labour platforms may help in formalising workers and employment relationships. The chapter concludes by offering policy solutions to regulate digital labour platform work, with a view to increasing their formal employment potential and tackling the vulnerabilities of informal workers.

Digital labour platforms have disrupted traditional business models

Digital platforms, also referred to as online platforms, are a product of technological innovation and a new manifestation of globalisation (OECD, 2019[1]). They are online entities encompassing a broad range of activities, which have in common the use of digital technologies to connect the demand and supply of particular services and products (OECD, 2019[2]; OECD, 2019[1]; ILO, 2022[3]).

Digital platforms are extremely diverse (Figure 5.1). One of their important subsets is constituted by *digital labour platforms that mediate work*, the dichotomy of which includes (ILO, 2021[4]; ILO, 2022[5]):

- Online web-based platforms for online delivery of services [e.g. Upwork, Amazon Mechanical Turk (AMT)]. These platforms allow for a digital delivery of non-material services by a workforce that is potentially scattered around the world.
- Location-based platforms (e.g. delivery platforms such as Uber Eats). These platforms allow workers to serve clients locally, and require the workers involved to be located in a specific area.

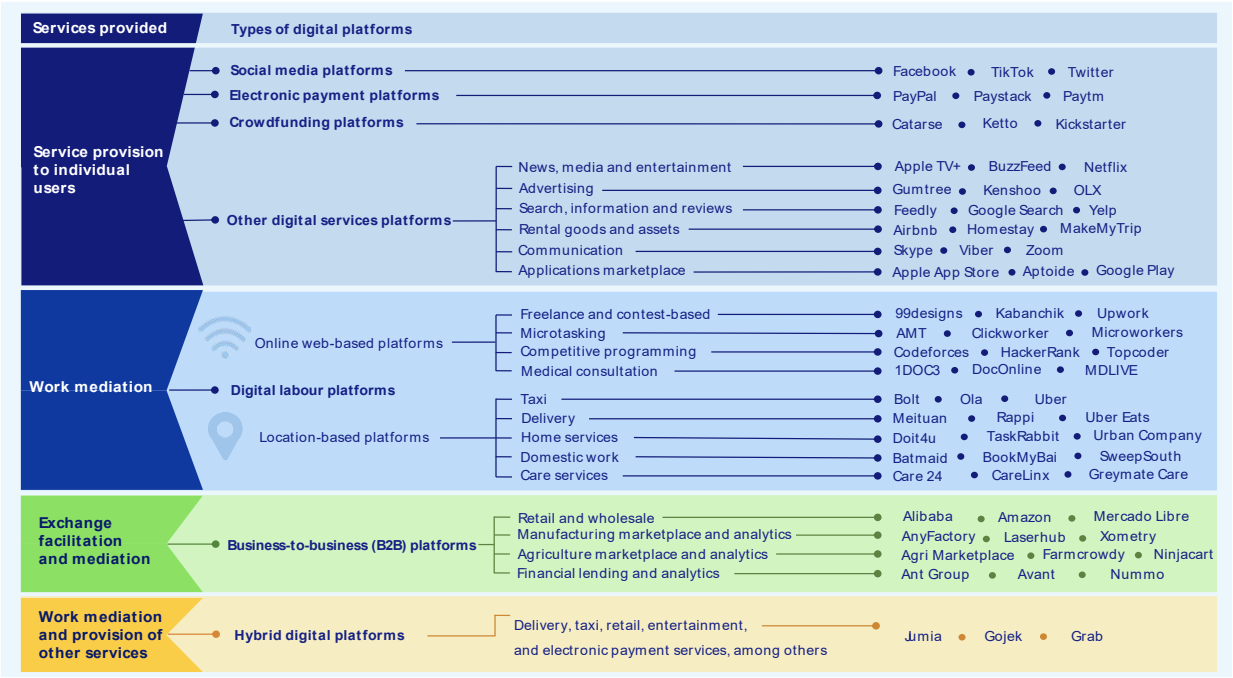
Digital labour platforms that mediate work provide new ways of organising production and work processes. As such, they also present a number of challenges to employers, workers and governments (ILO, 2022[5]; OECD/ILO/European Union, 2023[6]). Informal employment and social protection of workers is one of these challenges, although digital labour platforms also embed opportunities for formalisation.

Work through digital labour platforms is rapidly expanding, although it still represents a relatively small share of total employment

Work through digital labour platforms is penetrating a number of sectors of the economy (Figure 5.1) in all regions (Figure 5.2 and Figure 5.3), even though the share of digital labour platform workers is still small (ILO, 2021[4]; Schwellnus et al., 2019[7]). The number of online web-based and location-based platforms rose from an estimated 142 in 2010 to more than 777 in 2020 (ILO, 2021[4]). In 2021, there were approximately 14 million active workers on the 5 largest English-speaking online web-based platforms alone (Kässi, Lehdonvirta and Stephany, 2021[8]).

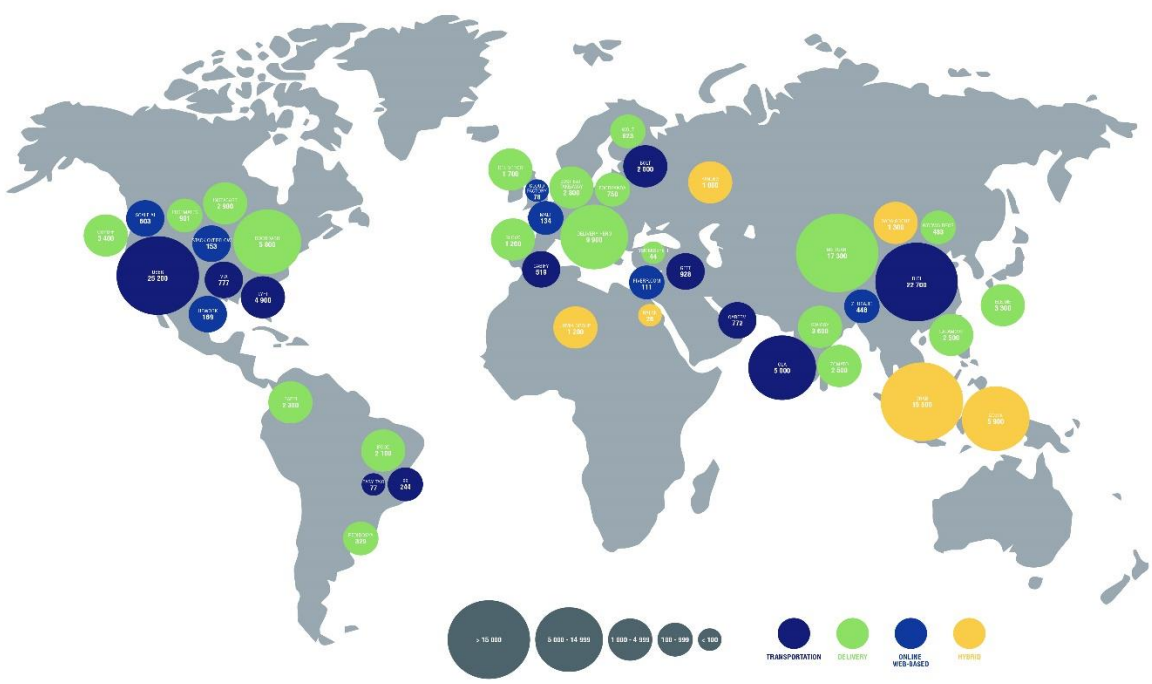
The majority of the global online workforce on online web-based platforms are based in Asia (ASEAN, 2023[9]), most notably India (33% of English-speaking online platform workers in 2021), followed by Bangladesh (15%) and Pakistan (9%) [see (Kässi and Lehdonvirta, 2018[10]) for the methodology]. Beyond English-language platforms, by 2015, Chinese-language online web-based platforms already had at least 12 million registered workers (Kuek et al., 2015[11]). The Asian region is also the world leader in terms of employment on online location-based platforms. By 2020, the online location-based platform Grab had 2.8 million active drivers in all countries of operation (Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam), and more than 9 million micro-entrepreneurs in the region had earned income through Grab's non-driver services. Gojek in Indonesia and Ola Cabs in India each employed 1 million drivers around 2020 (Asian Development Bank, 2021[12]).

Figure 5.1. Typology of digital platforms



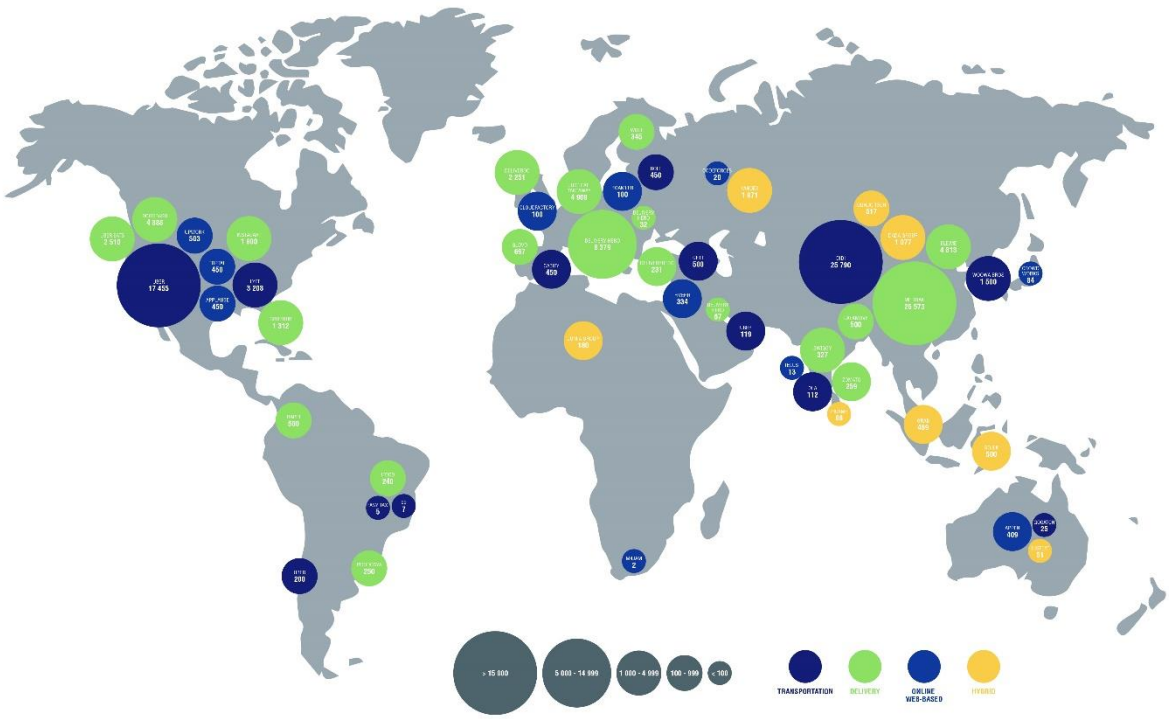
Source: (ILO, 2021[4]); courtesy of the ILO, with adaptations.

Figure 5.2. Total funding from venture capital and other investors, selected categories of digital labour platforms, by region, 1998-2021 (in USD millions)



Note: For details of construction, please refer to (ILO, 2021[4]).
Source: (ILO, 2021[4]), based on Crunchbase database. Courtesy of the ILO, with adaptations.

Figure 5.3. Estimated annual revenue of digital labour platforms, selected categories, by region, 2021 (in USD millions)



Note: For details of construction, please refer to (ILO, 2021[4]).
Source: (ILO, 2021[4]), based on Crunchbase database. Courtesy of the ILO, with adaptations.

In Africa, the development of digital work has lagged behind, but is nevertheless growing in importance. In Ghana, an estimated 60 000-100 000 workers rely on digital labour platforms for their livelihoods. In Kenya, there are more than 35 000 such workers, and this number is expected to grow to 100 000 in 2023 (Fairwork, 2021[13]). In South Africa, the number of digital labour platform workers is growing by more than 10% each year and could reach the millions by 2030 (AUC/OECD, 2021[14]). In Egypt, more than 200 000 drivers were registered on Uber alone in 2020 (Fairwork, 2021[15]).

Latin America and the Caribbean (LAC) has also witnessed a growth of digital work. Wealth inequality, high informality and high rates of within-continent migration (especially from Venezuela) create fertile grounds for the proliferation of location-based platforms (Morales, 2023[16]). For example, country-specific studies show that in Ecuador, the number of digital labour platform workers was around 40 000 in 2020, with 1.5 million users relying on this type of work (Fairwork, 2021[17]). The commonality of the Spanish language throughout LAC also creates particularly fertile grounds for the development of this regional (rather than global) online workforce on online web-based platforms, mediated by the common language (Galperin and Greppi, 2017[18]).

In Eastern Europe and Central Asia, by 2019, Russian-language online web-based platforms alone had at least 8 million registered workers, scattered throughout 14 Former Soviet Union countries and in other countries with significant Russian-speaking diasporas (Shevchuk, Strebkov and Tyulyupo, 2021[19]). Local language platforms serving local markets have also flourished, with Serbia and Ukraine becoming the leaders of digital labour platform work in the Eastern European region throughout the 2010s (Aleksynska, Bastrakova and Kharchenko, 2018[20]).

The COVID-19 pandemic generalised the use of digital labour platforms and enhanced our understanding of challenges associated with this work

The COVID-19 crisis had complex effects on digital labour platform workers, with sizeable variations observed by sector of economic activity and by country (OECD, 2021[21]; ILO, 2022[5]). The crisis also accentuated the challenges associated with digital platform work, in addition to the opportunities that it provides (Box 5.1).

At the onset of the crisis, the demand for work increased in areas not requiring physical proximity, but decreased in areas requiring physical proximity. For example, the demand for ride-hailing and home services declined drastically during the initial lockdowns, making workers on location-based platforms that specialised in these areas among the hardest hit by lockdown measures (Moulds, 2020[22]). The decline in demand persisted even after the restrictions were lifted because many consumers stopped using these services in order to avoid the risk of contagion. In contrast, lockdowns and mobility restrictions led to a surge in demand for delivery platforms, among others (Fairwork, 2021[23]; OECD, 2020[24]).

Both labour demand and supply increased drastically on online web-based platforms, mainly led by clerical and data entry tasks, professional services, and software development and technology. This reflected the cost-saving strategies of enterprises, the need for software solutions to enable the smooth functioning of a remote working environment, and the search for online work opportunities among many workers who lost jobs in offline economies due to lockdowns (ILO, 2021[4]). The increase in the use of both location-based and online web-based platform work tended to be larger in more developed and technologically advanced countries, in countries with better access to infrastructure and connectivity, in countries with higher skill levels, and in countries with more widespread use of the Internet (OECD, 2021[21]).

Box 5.1. Digital labour platform work tested by COVID-19

The COVID-19 crisis posed two major risks to digital labour platform workers: (i) exposure to the virus, and (ii) work and income loss due to lockdown measures and changing consumer behaviour (OECD, 2020[24]). The key challenge to handle these risks was related to the self-employment status of the majority of workers, which is often coupled with informality, particularly in developing countries. Most of these workers were not covered by social protections, including health insurance, work-related injury, disability, or unemployment insurance. Even if they were formal, many self-employed workers did not have paid sick leave, sick pay, or unemployment benefits. The situation was even more dramatic for informal self-employed workers, who could not afford to self-isolate or to take days off in the absence of paid sick leave and sickness benefits even if they tested positive for COVID-19 (ILO, 2021[4]). This presented important risks not only to workers but also to their clients.

The incidence and impact of these risks differed according to the type of work, individual and family characteristics, government lockdown restrictions, and mitigation measures, as well as specific measures undertaken by the digital platforms themselves to help their workers.

In 2020, the Organisation for Economic Co-operation and Development (OECD), together with Appjobs and the Appjobs Institute, carried out a survey of platforms (digital labour platforms as defined in Figure 5.1, as well as several others) and a survey of workers in order to understand the types of special measures that the platforms provided during the crisis. This survey covered 64 platforms mediating services as diverse as delivery (27 platforms), ride hailing (8 platforms), babysitting (4 platforms), property rental (3 platforms), cleaning (3 platforms), car sharing (2 platforms), removals and storage (2 platforms), gardening (2 platforms), pet sitting (2 platforms), and a variety of other services (11 platforms) in OECD member countries (OECD, 2020[24]).

More than 50% of the surveyed platforms reported taking measures to promote social distancing and/or the safe provision of services, such as introducing contactless delivery or temporarily ceasing high-risk services; 25% of platforms reported providing personal protective equipment or hygiene products to workers; and 23% of platforms reported providing full or partial pay for sick or self-isolating workers, generally up to a maximum period of two weeks.

Through the complementary survey of platform workers (working both on location and online), 35% of respondents confirmed that their platform(s) had taken measures to assist them during the crisis. However, only 44% of those workers were satisfied with the measures taken. They wished to have more assistance, better employment opportunities, more work through the platform, more financial support, access to benefits, a safer work environment, and better general treatment from the platform(s).

Similar examples were reported in other parts of the world. According to the International Labour Organization's (ILO's) rapid assessment surveys, a majority of location-based workers (71%) who were working at the time of the surveys reported that their platform(s) had introduced measures to mitigate the risks associated with the COVID-19 crisis. Among app-based taxi drivers, this share ranged from 24% (Kenya) to 81% (India). Among delivery workers, this share ranged from 48% (Chile) to 92% (Kenya). Various measures were cited, including compulsory mask wearing, contactless and cashless delivery, limiting the number of passengers, and sanitising hands, equipment and vehicles (Espi-Sanchis, 2022[25]).

In Kenya, some platforms offered safety training and subsidised the cost of safety clothing, gloves and masks for their "partners" (Fairwork, 2021[26]). In Indonesia, the Gojek ride-sharing platform provided direct cash support to active drivers and paid for the rides for its partners and their family members to get vaccinated. It also provided mattresses with direct access to oxygen when there was a spike of

COVID-19 cases (Dang, 2022[27]). Nevertheless, in countries such as Brazil, Chile and Ecuador, the support workers received from platforms was deemed "insufficient" and led to the first international digital labour platform workers' movement to request better protections and working conditions (Fairwork, 2021[17]).

Source: Authors' compilation. Author's computations based on the ILO rapid assessment surveys; for details, see (Espi-Sanchis, 2022[25]).

Work through digital labour platforms carries a risk of informal employment, but also opportunities for formalisation

The proliferation of digital labour platforms was initially heralded as a revolutionary solution to unemployment problems by providing access to more work and markets, and hence moving people out of poverty (Kuek et al., 2015[11]). At the same time, there has been a growing understanding of the risks associated with platform work, including in terms of informal employment.

Indeed, one of the challenges for modern labour markets is that a large share of workers operating on digital labour platforms are informal. There are two sources of this informality.

First, the vast majority of digital labour platform workers are classified as independent contractors, or self-employed workers (Berg et al., 2018[28]; ILO, 2021[4]; Schwellnus et al., 2019[7]). In principle, as self-employed workers, according to national rules, they can (and often should) be registered for tax purposes. They should also register for social security when the system in place requires this. If they are registered as self-employed workers, they are part of the formal sector, and thus are considered to have a formal job. However, the vast majority of digital labour platform workers in developing countries remain unregistered and hence are informal. Often this happens because platforms have disrupted traditional ways of doing business and allowed non-professionals to take up jobs available through the platforms (for example, Uber and several other transportation apps initially allowed anyone to work as a driver, while in most countries traditional passenger transportation drivers must be licensed and undergo health and security checks). In addition, many workers operating on digital labour platforms lack clarity on how to provide a service legally and how to report it to the authorities (Williams, Llobera Vila and Horodnic, 2020[29]). The available information on the registration status of digital labour platform workers suggests that, indeed, the share of non-registered (and hence informal) self-employed workers who work through digital labour platforms is higher than the share of informal workers in the traditional offline economy. Empirical evidence for this exists in Eastern Europe (Aleksynska, 2021[30]) and in India (Berg, 2016[31]). As a result, social protection is less frequently enjoyed by digital labour platform workers as compared with other workers, especially in developing countries where social protection institutions for the self-employed are weak (ILO, 2022[5]).

Second, even for those self-employed workers who are registered, and are hence *de jure* are part of the formal sector, there is a risk of sliding into dependent self-employment, and even into a disguised employment relationship – a situation where the worker is misclassified as an independent, self-employed worker, even though he or she is, in fact, in a subordinate employment relationship (ILO, 2016[32]). Algorithmic management, the use of approval rates to attribute work, time tracking, price-setting, and the system of non-transferable ratings that is practised by digital labour platforms (Berg, Cherry and Rani, 2019[33]) enhance worker dependency on a platform or a particular client of a platform. As a result, *de facto,* up to one-half of self-employed platform workers are actually in a disguised employment relationship or in a grey zone, even if they consider themselves to be independent workers (Aleksynska, Bastrakova and Kharchenko, 2018[20]). In other words, these workers share the vulnerabilities of employees and should benefit from labour protections, but they do not (OECD, 2019[2]). The extent of this phenomenon depends on the business model practised by each individual platform. For example, in developed countries, a series of landmark legal cases suggested that work on some location-based platforms can, in some instances,

be considered as a disguised employment relationship [e.g. Paris Criminal Court Decision of 19 April 2022, regarding Deliveroo France workers. See also other examples in (ILO, 2022[5])].

At the same time, work through digital labour platforms also represents an opportunity for formalisation (OECD, 2019[2]). Available technologies for digital work can be used to facilitate the formalisation of own-account workers on the digital labour platforms, as well as their inclusion in social security schemes whenever possible. Indeed, digital labour platforms create a unique setting where workers' and clients' identities are recorded through digital accounts, and all transactions are tracked. The digitalisation of transactions improves monitoring of economic activity, reduces its costs, and allows for traceability, and hence for transparency and accountability (ILO, 2022[5]), all of which are important elements for formalisation. Seizing this opportunity for formalisation, however, requires creating an enabling environment by governments, and co-operation between digital labour platforms and public agencies (in particular, social security and tax authorities). For effective future co-operation, it would be important for public authorities to acquire the consent of the digital labour platforms, especially in light of individual data protection requirements. Data protection laws may need to be modified, and new legal frameworks obliging digital labour platforms to provide information on all transactions carried out may need to be established (ILO, 2022[5]). In this light, co-operation with various ministries (such as the ministry of justice or the ministry of finance) is important.

The potential of digital labour platforms to create genuinely formal jobs is not yet fully grasped

In order to determine whether the proliferation of digital labour platforms increases the share of formal employment, it is important to understand whether: (i) digital labour platforms create new jobs; (ii) the new jobs that are created are actually formal; and (iii) conversion from informal to formal jobs is happening.

Digital labour platforms have new job creation potential in some sectors, but not in others

Digital labour platforms allow the monetisation of tasks that previously would not have been performed for money. For example, location-based platforms allow for the commodification of what might previously have been done within a household. Some of the work outsourced from developed to developing countries through online web-based platforms, especially in creative and multimedia services or software development (OECD, 2018[34]), would simply not be done in the absence of these platforms, as it would have been too expensive to perform in a developed country. In this sense, online labour platforms led to an increased demand for these services, which likely led to work creation in certain countries and sectors (Schwellnus et al., 2019[7]). Moreover, digital labour platforms also make it easier for parties to find each other and to match demand with supply. They solve a co-ordination problem, regardless of whether the worker is located in a developed country or not (De Stefano, 2016[35]). By doing this, they lower the transaction costs of finding labour and minimise friction in the labour markets (McKinsey Global Institute, 2015[36]), which can have the effect of raising employment, too.

On the other hand, much of the work channelled through digital labour platforms today – whether taxi driving, domestic work, cleaning, or auditing services – existed prior to the emergence of the platforms, and often co-exists today in the physical labour market. In other words, digital labour platforms have used technology to mediate work and help outsource services, rather than to actually create new jobs. Many jobs that already existed before the emergence of these platforms have simply changed their nature (ILO, 2016[32]; Schwellnus et al., 2019[7]). This especially concerns location-based platforms [which have simply reorganised work that already existed in a particular sector (ILO, 2022[5])], as well as some online web-based platforms that serve local markets.

Moreover, a large share of work undertaken through digital labour platforms is available as tasks or "gigs", which can often be fractionalised and outsourced further, rather than being a genuine full-time job. It is for this reason that digital labour platform workers are often referred to as "gig" workers. In their turn, many workers use platforms as a secondary activity to complement their primary source of income (Aleksynska, 2021[30]; Berg, 2016[31]), as well as because there is an excess of labour supply on platforms and simply not enough full-time work available (ILO, 2022[5]). As a result, the net full-time job creation impact of the digital labour platforms that are able to fully match labour supply has been considered relatively disappointing (ILO, 2021[4]).

Digital labour platforms enhanced informalisation trends in some sectors, but created opportunities for formalisation in others

How much of this new job creation is actually formal? The answer to this question is, again, country and sector specific.

In certain settings, the emergence of platforms has meant entrenching informality. For example, taxi drivers in India were traditionally self-employed before location-based platforms appeared. By adhering to these platforms, many drivers actually lost autonomy and the minimum price-setting guaranteed by municipalities; they saw an increase in their dependency and precarity (Rani and Gobel, 2022[37]; Rani and Dhir, 2020[38]). In some instances, digital labour platforms simply revealed an already high level of informality by making invisible economic activity visible. For example, city hitchhiking was not unusual and not formally prohibited in several Eastern European countries, but its extent was revealed by the arrival of location-based apps in the transport sector (Aleksynska, 2021[30]).

With the advent of digital labour platforms, some enterprises started more systematically outsourcing activities such as accounting, marketing, information technology, or legal services to platform workers, rather than hiring these specialists as wage employees. In other words, platform work allowed enterprises to more easily substitute wage employment with services delivered by self-employed individuals who, particularly in the context of developing countries, are largely informal. In this sense, in some countries platform work is often seen as a continuation of the outsourcing trend that started before the platforms emerged and that was associated in many settings with worsening working conditions (OECD, 2021[39]). As such, the development of digital labour platform work is also often seen as a continuation of the trend towards informality and precarity (Kahancova, 2016[40]; Meszmann, 2016[41]). Moreover, this has been happening within the local labour markets in developing countries. Indeed, it is often believed that online web-based platforms create work opportunities across borders, but in reality, much of the services work is non-transferable and has been channelled through online web-based platforms within local markets rather than within international labour markets through a simple modification of working relations rather than genuine new jobs creation (Meil and Akgüç, 2021[42]).

Many sectors, including logistics and business process outsourcing (BPO), are also experiencing "uberisation". For example, in the early 2000s, India was able to leverage BPO to generate employment, including formal employment (the famous example being call centres). Two decades later, BPO services are provided through platforms that aggregate freelancers and microtaskers, and no longer rely on wage employment (Rani and Furrer, 2020[43]). Moreover, workers with high levels of education and skill are becoming more precarious in their employment, alongside the simultaneous deskilling of workers – a challenge for developing countries in particular as highly skilled workers remain scarce and the costs to develop them particularly elevated (Berg et al., 2018[28]).

But it does not have to be this way. In addition to technologies allowing for formalisation (at least in principle), digital labour platforms themselves also have a role to play in helping formalise their workers. For example, in Indonesia, the location-based platform Gojek offers help to its drivers to subscribe to the government health insurance programme, while at Grab Bike, workers are automatically enrolled in the

government's professional insurance programme (Fanggidae, Sagala and Ningrum, 2016[44]). Given this, digital labour platforms do have the potential to serve as a bridge towards formality (OECD, 2019[2]).

In addition, some of the traditional jobs that existed prior to the emergence of these platforms were formalised thanks to being channelled to location-based platforms. For example, for domestic workers, digital labour platforms can act as temporary agency platforms and thus favour formalisation. In some national legislation (for example, in the People's Republic of China), access to social security is conditional on being employed by an enterprise. In this case, being employed by a temporary agency, including a temporary agency platform, is the only opportunity for domestic workers to access formal wage jobs.

Despite its challenges, in developing countries, platform work is sometimes seen as a step up compared with traditional informal employment

Although digital labour platform work comes with challenges to some workers and societies, many workers still often prefer it to traditional informal employment, especially in the developing countries with widespread informality. How can this paradox be explained?

First, much depends on the individual worker's trajectory. In developed countries, "uberisation" is often seen as a threat to traditional formal employment: workers joining digital labour platforms give up the rights and protections available through standard employment in exchange for the promise of greater freedom and autonomy, as compared to an employment relationship (which, in reality, is often illusory). In developing countries, however, many platform workers only had informal employment to start with, often with no rights whatsoever. In this regard, beyond formal employment, digital labour platforms can offer advantages such as secured financial transactions, dispute mediation services, or enhanced protection in terms of income stability when income disbursal is regulated through the platform. Depending on the initial work trajectory of each individual worker, digital labour platform work can in certain cases allow their movement towards fairer and less vulnerable employment (Box 5.2).

Second, when workers create accounts on digital labour platforms, they have to abide by the terms of service set up by those platforms. These terms govern how and when workers will be paid, how work will be evaluated, and what recourse and mediation is available in case of problems. Terms of service also outline the responsibilities and obligations of workers, platform operators and clients (Berg et al., 2018[28]). In addition, workers often have to supply sensitive personal information, such as copies of identification documents and bank account details (ILO, 2021[4]). All of this creates a perception of formality for workers, an improvement on a situation where no contract existed before. Yet, this type of "formality" is actually private: workers may comply with private formal arrangements designed and valid within a platform, but this does not mean that they are formal with respect to their country's employment laws. In other words, the perception of formality that digital labour platforms offer to workers differs from policy makers' understanding of formality. Moreover, private regulation of each platform actually substitutes public regulation. Such substitution of private regulation for public regulation raises broader questions about the societal desirability of such an outcome.

Third, the intense competition between digital labour platforms means that, on the one hand, platforms have been motivated by their bottom-line profits and unwilling to change their underlying model that relies on self-employed "partners" rather than employees. In fact, most of the platforms believe that they would go out of business if they had to reclassify their workers as employees (Uber, 2020[45]). On the other hand, platforms also need to compete among themselves in order to attract and retain workers and clients. Social responsibility towards workers has become a valid concern and an important reputational tool that platforms increasingly have to reply upon. The COVID-19 crisis has particularly intensified the quest for social responsibility among digital labour platforms and increased pressure from clients and society at large to improve working conditions. As a result, several platforms have modified their terms of service or committed to providing fairer treatment to their "partners". In some instances, platforms have also

co-operated with governments to provide specific protections to workers during the crisis. Most of these measures remain private, disparate, and in many instances insufficient compared with what is prescribed by local laws (Box 5.1). Yet, given the lack of enforcement of the local laws, and the lack of protection in other jobs, platform work can still represent an improvement, at least for some workers.

Box 5.2. Working conditions on digital labour platforms: Protections and vulnerability as a continuum

The Fairwork Foundation aims to certify the production networks of the digital labour platform economy. It does so on the basis of the Fairwork project, established by the Oxford Internet Institute and the WZB Berlin Social Science Center, which currently operates in 26 countries across 5 continents.

As of 2022, Fairwork researchers have undertaken a global survey of 800 workers in 75 countries working on 17 digital labour platforms, including web-based and location-based platforms. The objective was to evaluate the working conditions on digital platforms, and then to score and rank the platforms against the five principles of fair work: fair pay, fair conditions, fair contracts, fair management and fair representation. Higher scores indicate that a greater number of principles is satisfied. Even if "fair work" does not mean "formal work", and formal work is not always fair either, formality is an important condition for fair and decent jobs. As such, the results of the survey allow a better understanding of whether platform work is indeed a step up compared with fully unprotected, vulnerable employment.

The results show that none of the digital labour platforms in any of the reviewed developing countries fully satisfy all five principles of fair work.

In Bangladesh, the situation seems to be the worst, as six out of the ten largest location-based platforms operating in the country received a score of 0 (no respect for any of the fair work principles), and all remaining platforms received a score of 1 (the maximum score is 10). In India and Indonesia, two out of ten platforms largest platforms received a score of 0, and in Kenya, three of the ten largest platforms received a score of 0.

Meanwhile, in Ghana, three out of the largest ten location-based platforms received a score of 5 or above. In South Africa, one platform received a score of 9 and three received a score of 8, suggesting that it is possible for platforms to implement better standards.

Results in terms of contracts and management practices are promising in that workers are somewhat protected on a daily basis from minor risks. However, pay remains highly irregular, and there is no worker representation or safety and health protection.

The situation also seems to be systemic, as the global competition in the digital work economy encourages such practices towards their workers, and the current absence of regulations does not remedy the situation.

Note: See the Fairwork Foundation website and reports for details on the certification procedure.
Source: Authors' elaboration based on the *Fairwork 2021 Annual Report* (Fairwork, 2021[13]) and various country reports.

Key policy messages

Regulating digital labour platforms is challenging but not impossible, and is often demanded by workers, clients and businesses.

There exist several broad frameworks to address the deficit of decent work and the social protection challenges in digital labour platform work (Lane, 2020[46]; ILO, 2016[32]; OECD, 2019[2]). Based on those, a number of tools can be singled out that are specific to tackling the informality of digital labour platform workers, as well as to reducing the vulnerability of informal platform workers.

Bringing digital labour platform work under the scope of existing regulations

Many digital labour platforms position themselves as intermediaries between the workers and the clients that only provide the matching opportunity. Yet, they in fact often provide services in traditional sectors of economic activity for which regulations usually already exist. For example, most countries, including developing countries, have regulations in the passenger transportation sector (Box 5.3) or domestic work sector. Some of these regulations exist at the municipal level, while others are nation-wide. These regulations typically require that workers in these sectors comply with professional licensing and insurance obligations, and often be formally registered with tax and/or social security authorities. The emergence of digital labour platforms disrupted existing markets in that they allowed non-professionals to provide work in these sectors, thus further increasing the pool of informal workers. Bringing platform work under the scope of existing sectoral regulations can help reduce the pool of informal platform workers by restricting the use of these platforms to those workers who are professionals in their sector, and also by encouraging formalisation of informal non-professionals. Enforcing unfair competition laws can also help ensure that platforms are not paying too little in taxes, not perpetuating unjustifiably low fares, and not discouraging wage employment.

Box 5.3. Bringing platform work under the scope of existing regulations

The vast majority of location-based platforms build their business models around the idea that they are not employers, but rather mere intermediaries providing the infrastructure for a self-employed worker to find clients. Several jurisdictions reacted to this through court decisions that are now used as legal precedent at both national and regional levels.

One example of regional regulation is the European Union (EU)-level European Court of Justice 2017 ruling (in Case C-434/15) on the status of applications that provide intermediation services in the field of passenger transport, such as Uber. According to the ruling, services provided by such applications must be regarded not as "an information society service" but as "a service in the field of transport".

This landmark ruling allowed EU member states to extend the scope of the existing sectoral (transportation) laws to transport applications. For example, the Constitutional Court of Slovakia referred to this European Court of Justice 2017 Judgment in its decision, ruling that Uber should be viewed as a transportation company and hence comply with the existing laws on professional licensing of drivers and with the safety requirements applicable to the vehicles driven. Hungary amended its transport law to bring transportation application companies under the scope of current transport regulations. Such legal changes resulted in all drivers having to comply with professional licensing and insurance obligations. Some other non-EU countries in the region, such as Serbia, adopted similar legal amendments.

Source: (Aleksynska, 2021[30]).

Encouraging the formalisation of self-employment and ensuring that digital labour platforms are paying their share

Many self-employed platform workers do not register as self-employed. Moreover, a significant share of them do not believe that registration is necessary (Aleksynska, Bastrakova and Kharchenko, 2018[20]). Encouraging registration with tax and social security authorities whenever possible is the first step towards formalisation. Many countries have simplified tax regimes for micro-entrepreneurs (also called solo self-employed or auto-entrepreneurs). Governments should continue their efforts to create such simplified regimes where they are not yet in place, enforce them where they exist, and inform workers about these regimes and the benefits of formalisation. At the same time, governments should consider policies to ensure that digital labour platforms pay their fair share of taxes and social security contributions (which could differ from those for traditional businesses), taking into account the high share of dependent self-employment created through these platforms.

Strengthening and enforcing regulations to correctly classify workers as employees

The risk of a disguised employment relationship means that workers are deprived of the labour and social security protections that are due to them. Many developing countries do not have legal instruments that allow for the clear identification of the existence of the employment relationship. In some cases, only judicial practice exists, but it remains ineffective and slow. In this regard, it is important to strengthen the existing regulations, including mandating, through labour laws, a series of criteria to determine the legal nature of the work relationship. Clear laws enabling the determination of an employment relationship and appropriate worker classification, and their effective enforcement, can reduce the incentive for enterprises to unduly

rely on self-employed workers. They can also help workers better understand their rights and empower workers to claim their rights as employees.

Empowering workers to challenge their employment status

For an individual worker, it may be prohibitively costly to challenge their employment status, and may cost them the very work opportunity they need. Workers may also not be aware of their rights, and usually do not have the time or money to file court complaints. In their turn, digital labour platforms may deactivate workers' accounts if they learn that workers have decided individually to contest their employment status, and workers may fear retaliation if they attempt this. Given this, it is up to governments to protect workers against retaliation and to facilitate workers' classification, including through information campaigns, more efficient courts, reduced court fees, simplified procedures, and mass reclassifications by sector of activity.

Modernising laws to address digital labour platform modes of work

Several countries have recognised that digital labour platform modes of work create a genuine ambiguity about employment status, with workers finding themselves in a "grey zone" between dependence and self-employment (OECD, 2019[2]). In order to minimise this grey zone as much as possible and to protect digital labour platform workers, some countries, such as Canada, Italy and Spain, have created a third employment category that lies between self-employment and wage employment. However, even if this has helped to formalise workers, worries remain that this has not changed working conditions, and in some instances has created additional confusion for workers and businesses (Cherry and Aloisi, 2016[47]). Others treat digital labour platforms as temporary work agencies, for which international guidance already exists (OECD, 2019[2]). In Chile, a new bill intends to add a chapter to the Chilean labour code, creating a special legal regime for digital labour platform work. It contains special protections for this form of work, and also extends some of the protections afforded by the general rules of the labour code to platform workers, most notably in the matters of working hours and remuneration (Leyton et al., 2022[48]). Beyond labour laws, some countries have also modified the provisions of other regulations. For example, regarding passenger transportation, Estonia adopted a law in 2017 specifying the conditions for providing transport services mediated by digital labour platforms and aligning their position with that of traditional taxi services. Under this law, neither traditional taxi drivers nor drivers associated with new digital providers need to comply with the previous conditions for professional training. Instead, transport providers are now under obligation to provide their own training for their drivers. Similarly, Lithuania amended its Road Transport Code in 2016; the updated provisions allow passenger transport to be organised by both natural and legal persons in both taxi and ordinary passenger cars. In return, passenger transport enterprises must provide passenger data to road transport control authorities, declare the service to the municipal authority, and declare the income received from these activities to the State Tax Inspectorate. The Road Transport Code no longer requires passenger transport operators to obtain a permit to carry passengers (OECD, 2018[49]). Latvia amended its Road Transport Law in 2018, providing for equal licensing requirements for any personal transport-operating entity and obliging "ride-sharing" apps to accept only electronic payments, to register in the Enterprises Register as legal entities and to provide full accounting of business activity.

Leveraging technologies to formalise

Digital labour platforms' transactions are traceable. This traceability offers a real opportunity to support the formalisation of digital labour platform workers and to bring them into tax and social security systems. Digital accounts that track workers' output for clients and their earnings through dedicated platforms can be used for the inclusion of own-account workers in the platform economy not only in the tax system in order to formalise them, but also in social security schemes to ensure access to social protections. Making this a reality is a question of political will, co-operation between platforms and government authorities, and compliance. There is also a need for new legal frameworks which would build bridges between labour and

commercial laws, as well as for laws on data privacy. There are several examples of how this can happen successfully. For example, the Estonian Tax and Customs Board initiated a pilot project for the transport sector in co-operation with Uber in order to connect the transport provider's digital payment system directly to the state digital taxation system. This reduces undeclared payments, decreases the administrative burden for service providers, puts platforms and their users on equal footing with the traditional economy, and helps generate tax revenues (National Training Fund, 2017[50]). Also in Estonia, there is an ongoing discussion on possible broader co-operation with digital labour platforms, such as using workers' digital accounts to track their income for social security purposes. While it is not fully operationalised yet, it is nevertheless technically possible, since Estonia's digital tax system can already access the total amount of transactions on the platforms directly through the banking system. For effective future co-operation, it would be important to obtain the consent of the platforms, or to impose an obligation for them to provide such data, in accordance with the country's individual data protection requirements. Data protection laws may also need to be modified.

Including digital labour platform workers within existing social protection schemes

Developed and developing countries alike have been actively experimenting with ways to extend social insurance coverage to self-employed workers as well as microenterprises and small enterprises. In India, the Code on Social Security was introduced in September 2020 to extend protection to all workers, including platform workers, irrespective of the existence of an employment relationship (ILO, 2021[4]). In LAC, a number of countries have introduced a "monotax" system with the aim of encouraging the formalisation of self-employed workers, including platform workers (ILO, 2021[4]). One of the leading examples is Uruguay, where monotax participants pay a flat rate covering tax and social security contributions, which entitles them (or their workers) to the same benefits as employees (other than unemployment benefits); they can also choose to voluntarily contribute to social health insurance. Specific measures were also introduced to extend monotax coverage to workers on taxi platforms: obtaining a licence to operate is conditional on individual workers being registered with social insurance and tax authorities under the same conditions as employees. The apps allow drivers to register while automatically adding a social security contribution to the price of service (Freudenberg, 2019[51]). In Egypt, during the COVID-19 crisis, the government announced that it planned to "identify and support two million gig workers in the country by the end of the year 2021" (Fairwork, 2021[15]). In order to do so, the government planned to register digital labour platform workers' employment status as "irregular employment", and under this status grant them access to free social security insurance, including healthcare coverage, life insurance, disability benefits, and other state welfare programmes such as a three-month COVID-19 grant (Fairwork, 2021[15]). Although this initiative was welcomed as a crisis measure, in the long term it may also create adverse incentives for the platforms not to pay their fair share of social security provision for their workers. More generally, it is important that all workers, regardless of their employment status, have access to an adequate set of social protections (OECD, 2019[2]; ILO, 2016[32]).

Supporting the universal right of all workers to bargain collectively

Worldwide, the development of digital labour platform work has so far proven particularly challenging to both worker organisation and representation (Johnston and Land-Kazlauskas, 2019[52]). Many digital labour platform workers face a labour monopsony situation in which they have an unbalanced power relationship in relation to the platform and/or clients. Digital labour platforms also have more power compared with workers because they can simply deactivate the accounts of those workers who join workers' rights movements. This makes workers vulnerable and potentially in need of the protections that are normally granted only to employees (OECD, 2019[2]). However, as self-employed workers, digital platform workers usually cannot be part of a trade union. Collective bargaining agreements often do not apply to them, and workers do not have a clearly attributable employer who would serve as a collective bargaining counterpart. Moreover, the universal right to collective bargaining may conflict with competition

laws in certain jurisdictions (ILO, 2016[32]). Nevertheless, workers throughout the world have taken different steps to organise. In 2018, the first Platform Staff Association in South America registered with the Ministry of Labour of Argentina, with a view to solving the problems encountered in the digital labour platform work environment (ILO, 2020[53]). Elsewhere, as dialogue with these platforms is difficult, digital labour platform workers increasingly engage in dispute actions such as strikes, demonstrations and litigation. The number of such actions around the world has been rising since 2015, with at least 1 253 occurring in 57 countries between January 2017 and July 2020 (Bessa et al., forthcoming[54]). The worsening conditions during the COVID-19 crisis have further pushed many platform workers to take action. Workers in Brazil, Chile, Ecuador and several other LAC countries initiated the first international gig workers' movement. In 2020, they organised multiple transnational actions, demanding better working conditions and employee status (Fairwork, 2021[17]). In view of workers' needs to organise, governments should aim to establish a legislative framework to remove impediments to the affiliation to existing trade unions of all workers, regardless of their employment status, as a prerequisite for ensuring inclusive union strategies and actions in favour of platform workers.

Encouraging platforms to exercise social responsibility

The fact that different digital labour platforms offer different working conditions (Box 5.2) means that platforms make choices, through their business models, of what can be possible. Encouraging competition between digital labour platforms, user awareness of working conditions, and social responsibility on the part of the platforms themselves can be an important step forward to protect workers regardless of their formality status. For example, BigBasket, a platform that has a significant presence in India, instituted a "Gig Workers Payment Policy" to ensure that its partner workers earn at least the national minimum hourly wage after all work-related costs are accounted for (Fairwork, 2021[13]). Several other platforms around the world have committed to improving a range of other conditions; however, these improvements remain disparate, and there is definitely scope for scaling them up.

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Informality and Globalisation

IN SEARCH OF A NEW SOCIAL CONTRACT

Globalisation and rapid technological change have radically transformed labour markets, affecting the lives and prospects of billions of workers. Those in the informal economy, the vast bulk of the workforce in the Global South, have been bearing the brunt. This report is for policy makers seeking to address the factors that make those workers in informality vulnerable. It provides them with a distinctive cross-country comparison of recent informality trends, and how they were affected by the recent crises such as the COVID-19 epidemic, casting light on the impacts of sub-contracting models in global value chains, and digital labour platforms. It argues that an inclusive recovery and greater resilience to future crises necessitate that many countries renew their social contracts, to make them more inclusive of informal workers and their families.

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