



**Women in Informal Employment  
Globalizing and Organizing**

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# **The Informal Economy: Definitions, Theories and Policies**

Martha Alter Chen



# WIEGO Working Papers

The global research-policy-action network Women in Informal Employment: Globalizing and Organizing (WIEGO) Working Papers feature research that makes either an empirical or theoretical contribution to existing knowledge about the informal economy especially the working poor, their living and work environments and/or their organizations. Particular attention is paid to policy-relevant research including research that examines policy paradigms and practice. This series includes statistical profiles of informal employment and critical analysis of data collection and classification methods. Methodological issues and innovations, as well as suggestions for future research, are considered. All WIEGO Working Papers are peer reviewed by the WIEGO Research Team and/or external experts. The WIEGO Publication Series is coordinated by the WIEGO Research Team.

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# Abstract

Today, there is renewed interest in the informal economy worldwide. This is because a large share of the global workforce and economy is informal and because the informal economy is growing in many contexts and appearing in new places and guises. This working paper, the first in the WIEGO series, provides an overview of the definitional, theoretical, and policy debates on the informal economy. The paper opens with a brief historical overview of the informal sector concept and related debates, focusing on the four dominant schools of thought about the informal economy. It then turns to recent rethinking of the concept, detailing the expanded statistical concept of informal employment and holistic conceptual models of the composition and causes of informality. The paper also examines the linkages between the informal economy, formal firms, and formal regulations and the “formalize the informal economy” debate. The paper proposes a comprehensive policy response to the informal economy with four main pillars: create more formal jobs; regulate informal enterprises and informal jobs; extend state protections—social and legal—to the informal workforce; and increase the productivity of informal enterprises and the incomes of informal workers. The paper concludes with a call for a fundamental rethinking of the future of the informal economy.

# Introduction

It was widely assumed during the 1950s and 1960s that, with the right mix of economic policies and resources, low-income traditional economies could be transformed into dynamic modern economies. In the process, the traditional sector comprised of petty trade, small-scale production, and a range of casual jobs would be absorbed into the modern capitalist—or formal—economy and, thereby, disappear. This perspective was reflected in the prediction by W. Arthur Lewis, in the 1954 essay for which he received a Nobel Prize in Economics, that economic development in developing countries would, in the long-term, generate enough modern jobs to absorb surplus labour from the traditional economy. This would lead to a turning point when wages would begin to rise above the subsistence level: what is referred to even today as the “Lewis Turning Point” (Lewis 1954).

This perspective was reinforced by the successful rebuilding of Europe and Japan after World War II and the expansion of mass production in Europe and North America during the 1950s and 1960s. By the mid-1960s, however, the optimism about the prospects for economic growth in developing countries began to give way to concerns about persistent widespread unemployment. This led development economist Hans Singer to argue in 1970 that he saw no sign of the “Lewis Turning Point” in developing countries. In sharp contrast with the historical experience in developed countries, unemployment and under-employment of various kinds were on the rise in developing countries, even those that were growing economically. Singer attributed this trend to an imbalance resulting from technological advances: an imbalance between limited creation of jobs due to the extensive use of capital-intensive technology and significant growth in the population—and labour force—due to technological progress in health and disease control. He predicted a persistent “dangerous” dualism in labour markets with high levels of casual and intermittent employment, as well as disguised or open unemployment. He also warned of an employment crisis due to acute land shortage in overcrowded farming communities and an acute job shortage in overcrowded urban communities (Singer 1970).

Reflecting this concern, the International Labour Office Organization mounted a series of large multi-disciplinary “employment missions” to various developing countries. Hans Singer and Richard Jolly were asked to lead the first employment mission to Kenya in 1972. The Kenya Mission found that the traditional sector in Kenya, which they called the “informal sector,” included profitable and efficient enterprises as well as marginal activities (ILO 1972). The term “informal sector” had been coined the year before by a British anthropologist, Keith Hart, in his 1971 study of low-income activities among unskilled migrants from Northern Ghana to the capital city, Accra, who could not find wage employment (Hart 1973).

Both Keith Hart and the Kenya Mission were largely positive about the informal sector. Hart concluded that, although they faced external constraints and capitalist domination, most internal migrants in Accra were engaged in informal activities that had “autonomous capacity for generating incomes” (Ibid.). The Kenya Mission stressed the potential of the informal sector to create employment and reduce poverty (ILO 1972).

But the informal sector as an economic reality received a mixed review in development circles. Many observers considered the informal sector to be marginal or peripheral and not linked to the formal sector or to modern capitalist development. Some of these observers believed that the informal sector in Ghana, Kenya, and other developing countries would disappear once these countries achieved sufficient levels of economic growth or modern industrial development. Others argued that industrial development might take a different pattern in developing countries—including the expansion of informal economic activities—than it had in developed countries.

By the 1980s, the terms of the informal sector debate expanded to include changes that were occurring in advanced capitalist economies. Increasingly, in both North America and Europe, production was being reor-

ganized into small-scale, decentralized, and more flexible economic units. Mass production was giving way to “flexible specialization” or, in some contexts, reverting to sweatshop production (Piore and Sabel 1984). These changes were (and are still) associated with the informalization of employment relations. Standard jobs were being turned into non-standard or atypical jobs with hourly wages but few benefits, or into piece-rate jobs with no benefits; production of goods and services was being subcontracted to small-scale informal units and industrial outworkers. In the process, the informal economy had become a permanent, but subordinate and dependent, feature of capitalist development (Portes, Castells and Benton 1989).

Meanwhile, the economic crisis in Latin America in the 1980s highlighted another feature of the informal sector: namely, that employment in the informal sector instead of—or alongside—open unemployment, increases in many countries during periods of economic crisis (Tokman 1984). During the Asian economic crisis of the 1990s, millions of people who lost formal jobs in the former East Asian Tiger countries tried to find jobs or create work in the informal economy (Lee 1998). Meanwhile, structural adjustment in Africa and economic transition in the former Soviet Union and in Central and Eastern Europe were also associated with an expansion of employment in the informal economy.

Why does employment in the informal economy often expand during periods of economic adjustment or transition? When enterprises are downsized or shut down, the workers who are laid-off and cannot find alternative formal jobs often end up working in the informal economy. This is particularly true of those who cannot afford to be unemployed, more so in countries without unemployment insurance or compensation. If hard economic times are accompanied by rising inflation or cutbacks in public services, households often need to supplement formal sector incomes with informal earnings.

During the 1990s, globalization of the economy contributed to the informalization of the workforce in many industries and countries (Standing 1999). Whereas globalization can generate new jobs and open new markets, many of the jobs are not “good” jobs and many of the new markets are inaccessible to small-scale or disadvantaged producers. This is because, in response to global competition, formal firms tend to hire all but a few core workers under informal arrangements or to outsource the production of goods and services to other firms and countries (Rodrik 1997). Further, informal firms and small producers often lack the market knowledge and skills to compete with formal firms for export markets and often face competition from imported goods in domestic markets.

At present, there is renewed interest in the informal economy worldwide. In part, this is because the informal economy has grown worldwide and also emerged in new guises and in unexpected places. In part, this stems from the fact that informal employment expanded significantly during the recent great recession (Horn 2009). Today, *informal employment is more than half of non-agricultural employment in most developed regions and as high as 82 per cent of non-agricultural employment in South Asia* (Vanek et al. 2012). If data on informal employment in agriculture were included in these estimates, the proportion of informal employment in total employment would be even higher in heavily agricultural regions, especially in sub-Saharan Africa and more so in South Asia.

This renewed interest also stems from the recognition of the links between informality and growth on the one hand and the links between informality, poverty, and inequality on the other. There is increased recognition that much of the informal economy today is integrally linked to the formal economy and contributes to the overall economy; and that supporting the working poor in the informal economy is a key pathway to reducing poverty and inequality. And there is increased recognition that women tend to be concentrated in the more precarious forms of informal employment, so that supporting working poor women in the informal economy is a key pathway to reducing women’s poverty and gender inequality (Chen et al. 2004, 2005).

In sum, although interest in the informal economy has waxed and waned since the early 1970s, the concept has continued to prove useful to many policymakers, activists and researchers. This is because of the

significance of the reality that it seeks to capture: the large share of the global workforce that contributes significantly to the global economy, while remaining outside the protection and regulation of the state.

Today, the informal economy is a field of study in its own right, drawing an increasing number of scholars from multiple disciplines ranging from economics, anthropology, and industrial relations to gender studies, political science, sociology, and urban planning. Recent scholarship on informality focuses variously on the size and composition of the informal economy, what drives or causes informality, what the consequences of informality are in terms of welfare or productivity, and what linkages exist between informality and formality, growth, poverty and inequality. This resurgence of interest in the informal economy has generated significant rethinking of the concept and improvements in official measurement of the phenomenon.

This working paper, the first in the WIEGO series, provides an overview of the definitional, theoretical, and policy debates on the informal economy. This paper is in four parts. The first section provides a brief historical overview of the informal sector concept and related debates. The second summarizes recent rethinking of the concept, including the expanded concept of informal employment and holistic models of the composition and causes of informality. The third section discusses the linkages between the informal economy, formal firms, and formal regulations. The next two sections explore policy responses to the informal economy, including the formalization debate. A short concluding section calls for a fundamental rethinking about the future of the informal economy.

## I. Historical Debates

Street vendors in Mexico City; push-cart vendors in New York city; rickshaw pullers in Calcutta; jitney drivers in Manila; garbage collectors in Bogotá; and roadside barbers in Durban. Those who work on the streets or in the open air are the most visible informal workers. Other informal workers are engaged in small shops and workshops that repair bicycles and motorcycles; recycle scrap metal; make furniture and metal parts; tan leather and stitch shoes; weave, dye, and print cloth; polish diamonds and other gems; make and embroider garments; sort and sell cloth, paper, and metal waste; and more. The least visible informal workers, the majority of them women, work from their homes. Home-based workers are to be found around the world. They include: garment workers in Toronto; embroiderers on the island of Madeira; shoemakers in Madrid; and assemblers of electronic parts in Leeds. Other categories of work that tend to be informal in both developed and developing countries include: casual workers in restaurants and hotels; subcontracted janitors and security guards; day labourers in construction and agriculture; piece-rate workers in sweatshops; and temporary office helpers or off-site data processors.

Conditions of work and the level of earnings differ markedly among those who scavenge on the streets for rags and paper, those who produce garments on a subcontract from their homes, those who sell goods on the streets, and those who work as temporary data processors. Even within countries, the informal economy is highly segmented by sector of the economy, place of work, and status of employment and, within these segments, by social group and gender. But those who work informally have one thing in common: they lack legal and social protection.

Over the years, the debate on the large and heterogeneous informal economy has crystallized into four dominant schools of thought regarding its nature and composition, as follows:

- The *Dualist* school sees the informal sector of the economy as comprising marginal activities—distinct from and not related to the formal sector—that provide income for the poor and a safety net in times of crisis (Hart 1973; ILO 1972; Sethuraman 1976; Tokman 1978).

- The *Structuralist* school sees the informal economy as subordinated economic units (micro-enterprises) and workers that serve to reduce input and labour costs and, thereby, increase the competitiveness of large capitalist firms (Moser 1978; Castells and Portes 1989).
- The *Legalist* school sees the informal sector as comprised of “plucky” micro-entrepreneurs who choose to operate informally in order to avoid the costs, time and effort of formal registration and who need property rights to convert their assets into legally recognized assets (de Soto 1989, 2000).
- The *Voluntarist* school also focuses on informal entrepreneurs who deliberately seek to avoid regulations and taxation but, unlike the legalist school, does not blame the cumbersome registration procedures.

Each school of thought subscribes to a different causal theory of what gives rise to the informal economy.

- The *Dualists* argue that informal operators are excluded from modern economic opportunities due to imbalances between the growth rates of the population and of modern industrial employment, and a mismatch between people’s skills and the structure of modern economic opportunities.
- The *Structuralists* argue that the nature of capitalism/capitalist growth drives informality: specifically, the attempts by formal firms to reduce labour costs and increase competitiveness and the reaction of formal firms to the power of organized labour, state regulation of the economy (notably, taxes and social legislation); to global competition; and to the process of industrialization (notably, off-shore industries, subcontracting chains, and flexible specialization).
- The *Legalists* argue that a hostile legal system leads the self-employed to operate informally with their own informal extra-legal norms.
- The *Voluntarists* argue that informal operators choose to operate informally—after weighing the costs-benefits of informality relative to formality.

The dominant schools of thought have different perspectives on this topic, although some do not explicitly distinguish between the two or adequately deal with both.

- The *Dualists* subscribe to the notion that informal units and activities have few (if any) linkages to the formal economy but, rather, operate as a distinct separate sector of the economy and that the informal workforce—assumed to be largely self-employed—comprise the less advantaged sector of a dualistic or segmented labour market. They pay relatively little attention to the links between informal enterprises and government regulations. But they recommend that governments should create more jobs and provide credit and business development services to informal operators, as well as basic infrastructure and social services to their families.
- The *Structuralists* see the informal and formal economies as intrinsically linked. They see both informal enterprises and informal wage workers as subordinated to the interests of capitalist development, providing cheap goods and services. They argue that governments should address the unequal relationship between “big business” and subordinated producers and workers by regulating both commercial and employment relationships.
- The *Legalists* focus on informal enterprises and the formal regulatory environment to the relative neglect of informal wage workers and the formal economy per se. But they acknowledge that formal firms—what de Soto calls “mercantilist” interests—collude with government to set the bureaucratic “rules of the game” (de Soto 1989). They argue that governments should introduce simplified bureaucratic procedures to encourage informal enterprises to register and extend legal property rights for the assets

held by informal operators in order to unleash their productive potential and convert their assets into real capital.

- The *Voluntarists* pay relatively little attention to the economic linkages between informal enterprises and formal firms but subscribe to the notion that informal enterprises create unfair competition for formal enterprises because they avoid formal regulations, taxes, and other costs of production. They argue that informal enterprises should be brought under the formal regulatory environment in order to increase the tax base and reduce the unfair competition to formal businesses.

In yet another approach—often focused on developed or transition countries—the informal sector is seen as *illegal* or *hidden/underground* production. *Illegal production* refers to production activities which are forbidden by law or which become illegal when carried out by unauthorized producers; while *underground production* refers to production activities which are legal when performed in compliance with regulations, but which are deliberately concealed from authorities (United Nations Statistical Commission 1993). Any type of production unit (formal or informal) can engage in any type of production (illegal; legal underground; legal, not underground). The empirical and policy question is what share and which components of the informal economy, especially in developing countries, are deliberately illegal or underground.

Given the heterogeneity of the informal economy, there is merit to each of these perspectives as each school reflects one or another “slice of the (informal) pie.” But the informal economy as a whole is more heterogeneous and complex than the sum of these perspectives would suggest.

Some of the self-employed choose—or volunteer—to work informally in order to avoid registration and taxation, while others do so out of necessity or tradition. Also, many of the self-employed would welcome efforts to reduce barriers to registration and related transaction costs, especially if they were to receive the benefits of formalizing. Further, much of the recent rise in informal wage employment is due to the informalization of once-formal employment relationships. In many such cases, it is the employers, not their employees, who are avoiding regulation and taxation. Employers often choose to retain a small, core, regular workforce and hire other workers on an informal basis in order to avoid payroll taxes and employer’s contributions to social security or pensions. In some such cases, payroll taxes and social security contributions are avoided by mutual consent of the employer and employee, as when employees prefer to receive greater take-home pay instead of employer contributions to social security. This may be the case when social security systems are managed poorly—or their terms and conditions are not transparent or well understood—with the result that employees do not expect any benefits in return for contributions.

In sum, some informal entrepreneurs choose, or volunteer, to work informally. Yet informal employment tends to expand during economic crises or downturns, suggesting that necessity—in addition to choice—drives informality. Also, informalization of employment relations is a feature of contemporary economic growth and the global economy. Further, in many developing countries, the vast majority of the workforce has never had a formal job and continues to engage in traditional or survival activities.

## II. Recent Rethinking

Over the past 15 years, a good deal of thought and effort has gone into developing holistic frameworks that take into account all aspects of informality and all categories of informal workers. Statisticians and informed users of data have focused on statistical definitions and measures in order to improve official labour force and other economic data on informality. Other observers have focused on understanding the composition of the informal economy and what drives its different components, as well as the linkages of the informal economy with the formal economy and formal regulations.

### Expanded Statistical Definition

The International Labour Office (ILO), the international Expert Group on Informal Sector Statistics (called the Delhi Group), and the global network Women in Informal Employment: Globalizing and Organizing (WIEGO) worked together to broaden the concept and definition to incorporate certain types of informal employment that had not been included in the earlier concept and definition of the “informal sector.” They sought to include the whole of work-related informality, as it is manifested in industrialized, transition and developing economies and the real world dynamics in labour markets today, particularly the employment arrangements of the working poor.

The expanded definition focuses on the nature of employment in addition to the characteristics of enterprises and includes all types of informal employment both inside and outside informal enterprises. This expanded definition was endorsed by the International Labour Conference (ILC) in 2002 and the International Conference of Labour Statisticians (ICLS) in 2003. In 1993, the ICLS had adopted an international statistical definition of the informal sector to refer to employment and production that takes place in unincorporated small and/or unregistered enterprises. In 2003, the ICLS broadened the definition to include the various types of informal employment outside informal enterprises: statisticians refer to this expanded notion as “informal employment.” For more details, see WIEGO Working Paper N° 2 (Vanek et al. 2012).

Informal employment, so defined, is a large and heterogeneous category. For purposes of analysis and policymaking it is useful to, first, sub-divide informal employment into self-employment and wage employment,<sup>1</sup> and then within these broad categories, into more homogeneous sub-categories according to status in employment, as follows:<sup>2</sup>

**Informal self-employment** including:

- employers in informal enterprises
- own account workers in informal enterprises
- contributing family workers (in informal and formal enterprises)
- members of informal producers’ cooperatives (where these exist)<sup>3</sup>

**Informal wage employment:** employees hired without social protection contributions by formal or informal enterprises or as paid domestic workers by households. Certain types of wage work are more likely than others to be informal. These include:

- employees of informal enterprises
- casual or day labourers

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<sup>1</sup> Another way to disaggregate informal employment is by whether it takes place inside or outside the informal sector: see WIEGO Working Paper N° 2 (Vanek et al. 2012) for more details.

<sup>2</sup> Status in employment is used to delineate two key aspects of labour contractual arrangements: the allocation of authority over the work process and the outcome of the work done; and the allocation of economic risks involved (ILO 2002a).

<sup>3</sup> The guidelines also include production for own final use (i.e., subsistence production) as informal. In countries where this is not considered an important category, it is not included in employment statistics.

- temporary or part-time workers
- paid domestic workers
- contract workers
- unregistered or undeclared workers
- industrial outworkers (also called homeworkers)

This expanded definition extends the focus from *enterprises* that are not legally regulated to include *employment relationships* that are not legally regulated or socially protected. It also serves to focus attention on informal workers: i.e., those who are informally employed.<sup>4</sup> This employment-centered focus has been accompanied by significant rethinking of the composition, causes, and consequences of informal employment. Today, informal employment is widely recognized to include a range of *self-employed persons*, who mainly work in unincorporated small or unregistered enterprises, as well as a range of *wage workers* who are employed without employer contributions to social protection.

To sum up, there are three related official statistical terms and definitions which are often used imprecisely and interchangeably: the *informal sector* refers to the production and employment that takes place in unincorporated small or unregistered enterprises (1993 ICLS); *informal employment* refers to employment without legal and social protection—both inside and outside the informal sector (2003 ICLS); and the *informal economy* refers to all units, activities, and workers so defined and the output from them. Together, they form the broad base of the workforce and economy, both nationally and globally.

## Holistic Conceptual Models

There are different theories of what comprises and gives rise to informality. Many mainstream economists subscribe to the notion that the informal economy is comprised of informal entrepreneurs who choose—or volunteer—to work informally (Maloney 2004). Yet other economists recognize that informal employment tends to expand during economic crises or downturns, suggesting that necessity—in addition to choice—drives informality. Other observers point out that informalization of employment relations is a feature of contemporary economic growth and the global economy and that informal wage workers hired by formal firms or households are growing in numbers in many countries. There is also increasing recognition that different factors drive different segments of the informal economy. In recent years, several sets of observers have posited models that seek to capture the components of informality and/or the different factors driving informality.

### WIEGO Network

The global action-research-policy network called Women in Informal Employment: Globalizing and Organizing (WIEGO)<sup>5</sup> has developed and tested a multi-segmented model of informal employment defined in terms of statuses in employment. The five main categories of the International Classification of Status in Employment—employer, employee, own account worker, unpaid contributing family worker, and member of a producer cooperative—are defined by the type/degree of *economic risk* (of losing job and/or earnings) and of *authority* (over the establishment and other workers). WIEGO has made the case that two additional categories need to be added to the standard set of categories: namely, casual day labourers and industrial outworkers or subcontracted workers. This is because casual day labourers face greater economic risk than informal employees (as they face the risk of losing job and/or earnings on a daily basis) and industrial outworkers do not exercise the same authority over their work as own account op-

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<sup>4</sup> The term “informal workers” is used here in a broad inclusive sense to include informal wage workers as well as the informal self-employed.

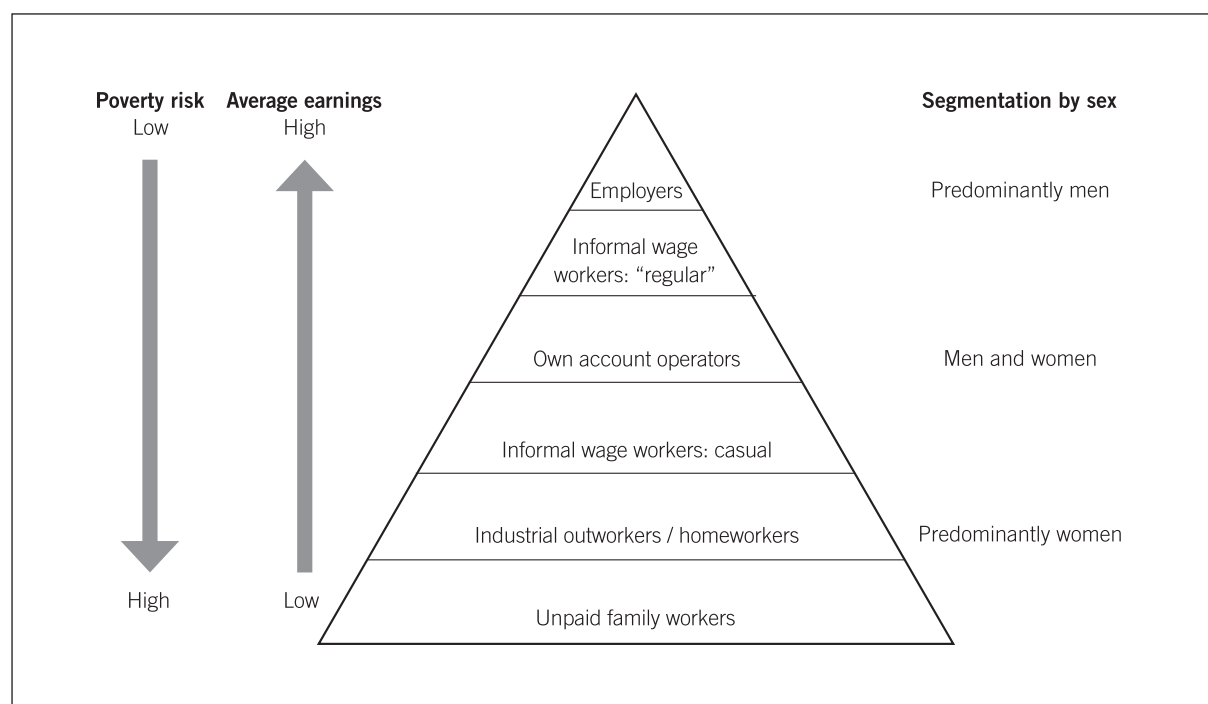
<sup>5</sup> Founded in 1997, WIEGO is a global action-research-policy network that seeks to improve the status of the working poor in the informal economy, especially women, by building and strengthening organizations of informal workers; improving research and statistics on informal employment; and promoting fair and appropriate labour, social protection, trade, and urban policies. For more on WIEGO and on the informal economy, please see [www.wiego.org](http://www.wiego.org).

erators (as they depend on employers/contractors for work orders, product specification, raw materials, and product sales). The WIEGO model features six statuses in employment: informal employers, informal employees, own account operators, casual wage workers, industrial outworkers or subcontracted workers, and unpaid but contributing family workers.

In the late 1990s, WIEGO commissioned two reviews of the links between informality, poverty, and gender: one of available literature (Sethuraman 1998), the other of available statistics (Charmes 1998). Both reviews found a similar hierarchy of earnings and segmentation by employment status and sex. These common findings provided the basis for the WIEGO multi-segmented model illustrated in figure 1.

In 2004, WIEGO commissioned data analysts to test this model in six developing countries—Costa Rica, Egypt, El Salvador, Ghana, India, and South Africa—by analyzing national data in those countries (Chen et al. 2005). Data for casual day labourers and industrial outworkers were not available in these countries. But the available data allowed for a comparison of employment status (measured at the individual level) and poverty (measured at the household level), making it possible to estimate the percentage of workers in specific employment statuses who were from poor households (what WIEGO calls “poverty risk”). In all countries, average earnings went down and the risk of being from a poor household went up as workers moved down the employment statuses in the WIEGO model.

**Figure 1: WIEGO Model of Informal Employment: Hierarchy of Earnings & Poverty Risk by Employment Status & Sex**



### World Bank Latin America Division

In 2007, the Latin America Division of the World Bank published *Informality: Exit and Exclusion*, a book co-authored by Guillermo Perry, William F. Maloney, Omar Arias, Pablo Fajnzylber, and Jaime Saavedra. The co-authors proposed a holistic model of the composition and causes of informality. In regard to the composition of informality, the authors specified “three pairs” of economic agents. In regard to what causes or drives informality, the authors specified different forms of both Exit (voluntary informality) and Exclusion (involuntary informality); see box 1.

**Box 1: World Bank 2007 Model of Informality: Composition & Causes****“Three Pairs” of Economic Agents**

- **Labour:**
  - with insufficient human capital to get formal job
  - who quit formal job in order to: be their own boss, make more money, avoid taxes, and/or enjoy flexibility
- **Micro-firms:**
  - with no intention or potential for growth, hence no intention of engaging with state
  - who are stymied by high barriers to entry
- **Firms:**
  - who are avoiding taxation and other regulations
  - who are partially registering their workers and sales

**Causal Theory #1: Different Forms of *Exit***

- **Opportunistic evasion:**
  - tax-evasion
  - illegal activities
  - avoidance of labour codes:
    - unprotected workforce
    - subcontracted production
- **Defensive evasion** in response to...
  - burdensome state
  - captured state
  - weak state
- **Passive evasion and state irrelevance:**
  - pre-modern or bazaar economy
  - informal or non-state institutions

**Causal Theory #2: Different Forms of *Exclusion***

- **Labour market segmentation**—prevents workers from getting formal jobs
- **Burdensome entry regulations**—prevents enterprises from formalizing
- **Hiring practices of firms**—in response to excessive tax and regulatory burdens

**Ravi Kanbur**

In 2009, development economist Ravi Kanbur posited a conceptual framework for distinguishing between four types of economic responses to regulation, as follows:

- A - Stay within the ambit of the regulation and comply.
- B - Stay within the ambit of the regulation but do not comply.
- C - Adjust activity to move out of the ambit of the regulation.
- D - Outside the ambit of the regulation in the first place, so no need to adjust.

Under the Kanbur framework, category A is “formal.” The other three categories are “informal.” B is the category that is most clearly “illegal.” According to Kanbur, regulations do not apply to either C or D: for example, because the regulation stipulates minimum enterprise size and these enterprises are below that minimum size. But there is clearly a difference between them: category C has adjusted its size to come below the minimum size, while category D was below the minimum size in any case so the regulation has not affected it at all (Kanbur 2009).

Kanbur argues that using a single label, “informal,” for B, C, and D obscures more than it reveals—as these are distinct categories with specific economic features in relation to the regulation under consideration. While acknowledging that it is useful to have aggregate broad numbers on the size and general characteristics of the informal economy, Kanbur concludes that disaggregation provides for better policy analysis.

Guillermo Perry and his fellow authors from the World Bank Latin America Division specified their causal model in terms of three different types of both Exit and Exclusion. Ravi Kanbur specified his model in terms of responses to formal regulations: his categories B, C, and D parallel the three types of Exit (from formal regulation) in the Perry et al. model. However, Exit is not an appropriate label for those informal operators and workers who have never been formal: for whom the state or formal regulations are often irrelevant. Hence the need to include Exclusion as another causal explanation. But factors not captured under either Exit or Exclusion are often at work, including larger structural imbalances as well as informal regulations. The Dualists argue that an imbalance between population growth and employment growth—with not enough jobs being created—helps to drive informality. The WIEGO network would add that social norms and traditions play a role. Gender norms governing the mobility and behavior of women help to explain why, in most countries and contexts, unpaid contributing family workers and home-based producers are predominantly women, while informal employers are predominantly men. Many informal operators are engaged in hereditary occupations, passed down from one generation to the next.

Two (of the three) types of Exclusion specified by the World Bank echo the causal theories of two of the dominant schools of thought: “burdensome entry regulations” are the primary causal explanation of the Legalist school and the “hiring practices of firms” is a primary causal explanation of the Structuralist school. However, the Structuralist school would argue that capitalist firms not only seek to avoid regulations and taxes but also to dominate and exploit their informal employees.

According to the WIEGO network, most causal theories are valid—but only for certain segments of informal employment; and no single causal theory can explain each segment of informal employment. Further, the four dominant causal explanations—exit from, exclusion from, and entry barriers to formal regulations as well as subordination to or exploitation by formal firms—are not a sufficient set of causal explanations. Wider structural forces and informal regulations also drive informality.

In sum, a mix of factors drives the different segments of informal employment. Some of the self-employed choose—or volunteer—to work informally in order to avoid registration and taxation. Others do not choose to work informally but do so out of necessity, social conditioning, or tradition. Many of the self-employed would welcome efforts to reduce barriers to registration and related transaction costs, especially if they were to receive the benefits of formalizing. The recent rise in informal wage employment is associated with the decline in formal wage employment and the informalization of once-formal jobs. Informalization is due, in large measure, to the hiring practices of employers, who opt to retain a small core regular workforce and hire other workers on an informal basis in order to avoid payroll taxes, employer contributions to social security or pensions, or other obligations as employers. In some such cases, payroll taxes and social security contributions are avoided by mutual consent of the employer and employee.<sup>6</sup>

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<sup>6</sup> This may occur when employees prefer to receive a higher take-home pay and/or when social security systems are so poorly managed that workers do not consider social security contributions as being a good investment.

### III. Links with Formal Firms & Formal Regulations

Another key topic of historic debate and recent rethinking is whether and how the informal economy is linked to the formal economy on one hand and to the formal regulatory environment on the other. What follows is a summary of what the WIEGO network has found, through research and practice, about the linkages between the informal economy, formal firms, and the formal regulatory environment.

#### Linkages with Formal Firms

##### Informal Enterprises

Few informal enterprises, except perhaps some survival activities, operate in total isolation from formal firms. Most source raw materials from and/or supply finished goods to formal firms either directly or through intermediate (often informal) firms. Sourcing and supplying of goods or services can take place through *individual transactions* but are more likely to take place through a *sub-sector network* of commercial relationships or a *value chain* of subcontracted relationships.

To understand the linkages between informal enterprises and formal firms it is important to consider the nature of the production system through which they are linked. This is because the nature of the linkage—specifically, the allocation of authority and risk between the informal and formal firm—varies according to the nature of the production system, as follows:

- *Individual transactions*: Some informal enterprises or own account operators exchange goods and services with formal firms in what might be characterized as open or pure market exchange (in the sense of independent units transacting with each other). In such cases, the dominant firm in terms of market knowledge and power—usually the formal firm—controls the exchange or transaction.
- *Sub-sectors*: Many informal enterprises or own account operators produce and exchange goods and services with formal firms in what are called sub-sectors, that is, networks of independent units involved in the production and distribution of a particular product or commodity. In such networks, individual units are involved in a series of transactions with suppliers and customers. The terms and conditions of these transactions are governed largely by the dominant firm in specific transactions (as above) but also by the “rules of the game” for the sub-sector as a whole, which typically are determined by dominant firms in the network.
- *Value chains*: Some informal enterprises and own account operators and, by definition, all subcontracted workers produce goods within a value chain. The terms and conditions of production in value chains are determined largely by the lead firm: in domestic chains, a large national firm and, in global value chains, a large transnational company. The major suppliers to the lead firm—and often formal firms—also help determine the terms and conditions of subcontracts to informal firms and workers down the chain.

Take the case of garment makers. Some produce for the open market selling goods to individual customers or to firms in the specific garment subsector they operate in. These garment makers operate with some authority or control and assume all of the risks of production. Others produce goods under a subcontract for a supply firm linked to a lead firm, domestic or multinational. These garment makers have little (if any) authority or control over what they produce but assume much of the risk in the form of non-wage costs (workspace, equipment, and electricity), rejected goods, and delayed payments.

## Informal Workers

Historically, around the world, the “employment relationship” has represented the cornerstone—the central legal concept—around which labour law and collective bargaining agreements have sought to recognize and protect the rights of workers. Whatever its precise definition in different national contexts, it has represented “a universal notion which creates a link between a person, called the ‘employee’ (frequently referred to as ‘the worker’) with another person, called the ‘employer’ to whom she or he provides labour or services under certain conditions in return for remuneration” (ILO 2003a: 2).

The concept of employment relationship has always excluded those workers who are self-employed. Increasingly, some categories of wage workers have found themselves to be, in effect, without legal recognition or protection because their employment relationship is either:

- *disguised*: The employment relationship is deliberately disguised by giving it the appearance of a relationship of a different legal nature. For example, the lead firm in a subcontracting chain may claim that it has a “sales-purchase”—or commercial—relationship with those who produce goods for it, rather than a subcontracted employment relationship.
- *ambiguous*: The employment relationship is objectively ambiguous so there is doubt about whether or not an employment relationship really exists. This is the case, for instance, with street vendors who depend on a single supplier for goods or sell goods on commission for a distributor.
- *not clearly defined*: The employment relationship clearly exists but it is not clear who the employer is, what rights the worker has, and who is responsible for securing these rights. For example, in value chain production, it is not clear who the real employer is: the lead firm, the supply firm, or the subcontractor. Similarly, in the case of temporary work, it is not clear who the real employer is: the agency that supplies temporary workers or the firms that hire them on a temporary basis (Ibid.).

Under each of these employment relationships, workers tend not to be protected under labour law or covered by collective bargaining agreements: in brief, they are informally employed. It is important to note that, in many such cases, the employer seeks to disguise the employment relationship or avoid definition of who is responsible; and that the employer in question may well represent a formal firm, not an informal enterprise.

Beginning in the 1980s, as noted earlier, formal firms in developed countries began to favour flexible labour relationships. This form of labour market segmentation took place in the interest of flexible specialized production, not in response to rising wage rates or labour costs (Piore and Sabel 1984). Also increasingly since the 1980s, many formal firms in developed countries have decided to subcontract production out to unprotected workers in developing or transition countries, where labour costs are already low and where there is no real threat of rising wages due to legislation or unionized labour. In producing countries, there is often further segmentation between the core semi-permanent workforce and a peripheral temporary workforce, which is mobilized during peak seasons and demobilized during slack seasons (what has been called a “permanent temporary workforce”).<sup>7</sup>

In summary, to be more flexible and specialized, to be more competitive, or simply to reduce labour costs, many formal firms hire workers under informal employment relationships. In most such cases, it is the formal firm, not the informal worker, that chooses or “volunteers” to operate informally and enjoys the “benefits” of informality.

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<sup>7</sup> The permanent temporary workforce is a well-known phenomenon in the tourist industry. In Spain, the Union General de Trabajadores (UGT) got job security for such workers in the form of a guarantee that they would be re-hired in the same jobs when the season started again (Dan Gallin, personal communication).

## Linkages with the Formal Regulatory Environment

### Over-Regulation

As noted earlier, the legalists have focused on excessive regulations that create barriers and costs to working formally. From the WIEGO perspective, over-regulation not only raises barriers to working formally but also raises costs to operating informally. Consider the case of gum and salt production in India:

- *Gum collectors*: Although there is a thriving open market for gum that includes textile and pharmaceutical companies, to sell in the open market requires a special permit or licence. Most gum collectors—except those who can afford to obtain a permit or license—have to sell to the Forest Development Corporation at a price far below the prevailing market price (Crowell 2003).
- *Salt makers*: The cheapest way to transport salt within India is via railway. But, historically, small salt producers have been unable to use rail service to transport salt. This is because of a long-standing government regulation that stipulates that salt farmers need to own a minimum of 90 acres of land to be eligible to book a train wagon. Given that most small salt farmers lease land from the government or local landlords, most small salt farmers are not eligible to use rail transport. Because they have to use private transport, small salt farmers face high transportation costs and, therefore, remain less competitive than larger salt farmers (Ibid.).

### Deregulation

There has been a good deal of *deregulation* in recent years, not only in financial markets but also in labour markets. Deregulation of labour markets is associated with the rise of informalization or “flexible” labour markets (discussed above). In today’s global economy, many wage workers are caught between two contradictory trends: *rapid flexibilization* of the employment relationship (making it easy for employers to contract and expand their workforce as needed) and *slow liberalization* of labour mobility (making it difficult for labour to move easily and quickly across borders) (Chen et al. 2004). When it comes to labour market regulations, as with financial market regulations, the question should be what are appropriate regulations rather than whether or not to regulate.

### Lack of Regulation

The regulatory environment often overlooks whole categories of the informal economy. A *missing* regulatory environment can be as costly to informal operators as an *excessive* regulatory environment. For example, city governments around the world tend to adopt one of two stances towards street trade: trying to eliminate it or turning a blind eye to it (Bromley 2000). Either stance has a punitive effect: eviction, harassment, and the demand for bribes by police, municipal officials and other vested interests. Around the world, few cities have adopted a coherent policy—or set of regulations—towards street trade. Rather, most cities assign the “handling” of street traders to those departments—such as the police—that deal with law and order (Bhowmik 2004; Mitullah 2004).

Clearly, over-regulation, deregulation, and lack of regulation are not ideal for the informal workforce or the economy. There is a need to rethink regulations to determine what regulations are appropriate for which components of informal employment. There is a need to recognize that sector-specific regulations affect the informal self-employed in those sectors and are often biased in the interests of formal firms. There is a need to rethink both commercial and labour regulations to match the realities today of informal self-employment and informal wage employment, respectively. Finally, there is a need to recognize the contradiction inherent in calling for regulation of informal enterprises (i.e., formalizing informal enterprises) and deregulation of labour markets (i.e., informalizing employment relationships).

## IV. The Formalization Debate

At the heart of the policy debates on the informal economy is the question of whether and how to formalize the informal economy. Different observers have different notions of what formalization of the informal economy means. To some, it means shifting informal workers to formal wage jobs—but this requires creating more formal wage jobs. To others, it means registering and taxing informal enterprises. For informal workers and operators, many of whom already pay taxes (such as VAT) or fees of various kinds (e.g. licence fees to operate and/or site fees to operate in specific locations) or are willing to pay taxes or fees in return for benefits, it means gaining access to legal and social protection as well as support services (e.g. skills or business training) and being allowed to organize and to be represented in relevant rule-setting, policymaking, and collective bargaining processes.

It is important, also, to understand that formalization has different meanings and implications for different categories of informal workers. To date, the formalization debate has focused primarily on the self-employed in informal enterprises; and often, more specifically, on informal entrepreneurs who hire others. At a minimum, the formalization debate needs to distinguish between wage workers in informal jobs and self-employed in informal enterprises. Ideally, it should further distinguish between different segments of the self-employed and wage employed in the informal economy: as each segment has its particular needs and constraints (Chen 2006).

Further, it is important to ensure that formalization offers the benefits and protections that come with being formal and does not simply impose the costs of becoming formal. For the self-employed, formalization should not mean just obtaining a license, registering their accounts, and paying taxes: these represent, to them, the costs of entry into the formal economy. What they would like is to receive the benefits of operating formally in return for paying these costs, including: enforceable commercial contracts; legal ownership of their place of business and means of production; tax breaks and incentive packages to increase their competitiveness; membership in trade associations; protection against creditors and clear bankruptcy rules; and social protection.

What about informal wage workers? To them, formalization means obtaining a formal wage job—or formalizing their current job—with a secure contract, worker benefits, membership in a formal trade union, and employer contributions to their social protection. It is important to highlight that formalizing wage work requires a focus on employers, as employers are more likely than employees to avoid compliance with labour regulations. In this context, it should be noted that many informal wage workers work for formal firms and households, not just for informal enterprises.

Finally, therefore, it is important to note that formalization has different dimensions beyond just registering and paying taxes, including: receiving the legal and social protections enjoyed by formal firms and formal workers; receiving the tax holidays and incentive packages enjoyed by formal firms; being allowed to organize and to have representative voice in rule-setting and policymaking processes; and more. Policymakers should recognize these various dimensions of formalization and the fact that formalization is not, therefore, a one-step process but rather an on-going process of extending benefits of formalization incrementally to informal workers. In asking informal workers to register and pay taxes, they should offer informal workers one or more benefits of formalization: asking each group of workers which benefit/s of formalization would be most important to securing their livelihoods. In short, policymakers should consider the optimal dimensions and sequence of formalization from the perspective of different categories of informal workers.

In sum, what is required is an approach to formalization of the informal economy which is comprehensive in approach but context-specific in design and practice. A comprehensive approach for formalizing the informal economy is outlined in box 2:

**Box 2: Formalization of the Informal Economy: A Comprehensive Approach****1. Formalization of Informal Enterprises**

- registration and taxation:
  - simplified registration procedures
  - progressive registration fees
- appropriate legal and regulatory frameworks, including:
  - enforceable commercial contracts
  - private property rights
  - use of public space
  - occupational health and safety regulation
- benefits of operating formally:
  - access to finance and market information
  - access to public infrastructure and services
  - enforceable commercial contracts
  - limited liability
  - clear bankruptcy and default rules
  - access to government subsidies and incentives, including procurement bids and export promotion packages
  - membership in formal business associations
  - access to a formal system of social security

**2. Formalization of Informal Jobs**

- legal recognition and protection as workers
- rights and benefits of being formally employed:
  - freedom from discrimination
  - minimum wage
  - occupational health and safety measures
  - employer contributions to health and pensions
  - right to organize and bargain collectively
  - membership in formal trade unions

As outlined above, formalization of the informal economy can and should take different forms, including: shifting informal workers to formal jobs; registering and taxing informal enterprises; providing business incentives and support services to informal enterprises; securing legal and social protection for the informal workforce; recognizing the organizations of informal workers; and allowing their representatives to take part in rule-setting, policymaking, and collective bargaining processes.

However, the limits to formalization need to be understood. First, it should be recognized that formalization is *not* a one-time process involving a specified set of steps. Rather, formalization should be seen as a gradual on-going process involving incremental steps and different dimensions leading towards varying degrees and types of formality. Second, it should be recognized that formalization will *not* proceed quickly or automatically for all those who choose to formalize. The bureaucratic procedures and incentives for registered informal businesses need to be retooled and streamlined. Labour standards and benefits for informal workers need to be carefully negotiated by employers, workers, and government. Third, it should be recognized that formalization will *not* be feasible or desirable for all informal enterprises or all informal wage workers. Rather, it should be assumed that many informal enterprises and informal wage workers will continue to do what they do and remain informal or semi-formal (at least in some dimensions) for the foreseeable future.

## V. Comprehensive Policy Approach

Clearly, no single, overarching policy goal or prescription can address the concerns associated with all categories of informal enterprises, activities, or workers. What follows is a comprehensive policy framework with four broad goals to address informality:

1. create more jobs
2. register informal enterprises and regulate informal jobs
3. extend state protections to the informal workforce, especially the working poor
4. increase the productivity of informal enterprises and the income of the informal workforce

There is a growing consensus in development policy circles around these four broad goals, especially in support of the working poor who comprise the majority of the informal workforce. But there is limited consensus and ongoing debate regarding how to implement the goals.

### Goal #1 – Create More Jobs, Preferably Formal Jobs

There is a broad consensus that more jobs need to be created—preferably decent or formal jobs—through labour-intensive growth. Some observers argue that this can be done through employment policies alone while others argue that employment goals need to be integrated into development strategies more generally. Some observers also argue that this should involve a transformation in the overall structure of employment opportunities and the ability of the working poor to take advantage of such opportunities as they become available (Heintz 2004).

### Goal #2 – Register Informal Enterprises & Regulate Informal Jobs

Registering and taxing informal enterprises, as noted above, is the common narrow approach to formalizing the informal economy. This should be done by simplifying the bureaucratic procedures involved in registration and offering benefits and incentives in return for paying taxes.

It is also important to design appropriate regulations that will discourage employers, both formal and informal, from hiring workers informally—or informalizing once-formal jobs—and encouraging them to make employer contributions to health and pensions for their workers and to extend other benefits to their workers.

### Goal #3 – Extend State Protection to the Informal Workforce

Two types of state protection for the informal workforce—especially the working poor—are currently being debated: social protection and legal rights.

*Social Protection*—Social protection is once again high on the development policy agenda, especially in the aftermath of the global economic crisis which undermined the livelihoods of many working poor in the informal economy (Horn 2009, 2011). In June 2012, the International Labour Conference (ILC) adopted a Recommendation for a Global Social Protection Floor that would cover people at all stages of the life cycle and be comprised of a combination of cash transfers and access to affordable social services, especially health care. There is a growing consensus in development policy circles on the need to...

- prioritize extension of social protection coverage to excluded groups
- adapt both social and private insurance to incorporate informal workers by providing fiscal and other incentives for their affiliation
- coordinate diverse forms of protection

More specifically, there is a growing consensus around the need for universal pensions and health coverage. But there is little agreement on the appropriate role of government, the degree of government responsibility and public expenditure, and the mix of private versus public insurance and provision.

*Legal Protection*—There is also a growing commitment in development policy circles to extending legal protection to the working poor in the informal economy. In its final report entitled *Making the Law Work for Everyone*, the United Nations Commission on Legal Empowerment for the Poor prioritized three areas of legal rights and empowerment for the poor in general and the working poor in particular: property rights, labour rights, and business rights. The Commission argued that without property rights, the intrinsic economic power of the assets owned by the poor remains untapped (de Soto 2000). Without labour rights, the working poor lack worker benefits and decent working conditions. And, without legally recognized businesses, the working poor cannot access credit or markets, enforce contracts, or insure their businesses against bankruptcy. The Commission also highlighted that the poor need access to justice and, more generally, the rule of law (CLEP 2008).

But extending legal protection to the working poor in the informal economy will require rethinking and reforming existing legal regimes in most countries. Most informal workers are not covered or protected under existing *labour regulations* (which are premised on an explicit employer-employee relationship) and most informal enterprises are not covered or protected under existing *commercial or business laws* (which are premised on a formal commercial contract). Further, many informal enterprises and activities are governed by *industry-specific regulations* or by *local government regulations*.

Consider the urban informal workforce. Their activities are governed by industry-specific regulations (e.g. those governing trade in fresh food) as well as by urban planners and local governments that set rules and determine norms and practices which govern who can do what, and where, in cities. Often the rules are framed or interpreted in ways that discourage—if not outright ban—informal activities.

## Goal #4 – Increase Productivity of Informal Enterprises & Incomes of the Informal Workforce

There is a broad agreement that efforts should be made to increase the productivity of informal enterprises and the incomes of the informal workforce, especially the working poor. Standard approaches include: targeted measures such as financial services, enterprise support, and training; and general measures of state support, such as infrastructure services. The informal workforce needs productive assets, technical and business skills, and infrastructure services to better compete in the markets.

But increasing the productivity of informal enterprises and the incomes of the informal workforce also requires changes in the wider institutional environment, as follows:

*Favourable Policy Environment*—The economic policy environment needs to be supportive of informal operators, especially the working poor, rather than blind to them or biased against them. This requires addressing biases in existing economic and sector policies, as well as designing and implementing targeted policies. It also requires ensuring that macro policies and government procurement create demand for the goods and services produced by informal enterprises and workers.

*Improved Terms of Trade*—To compete effectively in markets, the working poor need not only resources and skills but also the ability to negotiate favourable prices and wages for the goods and services they sell, relative to their cost of inputs and their cost of living.

*Appropriate Legal Frameworks*—As noted above, the working poor in the informal economy need new or expanded legal frameworks to protect their rights and entitlements as workers and as entrepreneurs, including the right to work (e.g., to vend in public spaces), labour rights, business or commercial rights, and property rights.

*Protection Against Risk and Uncertainty*—The working poor need protection against the risks and uncertainties associated with their work, as well as against the common core contingencies of illness, disability, property loss, and death.

There are, in sum, two broad ways to increase the productivity of informal enterprises and the incomes of the working poor in the informal economy. The first is to *increase the positives*: through supportive measures to improve assets and market access, to provide legal identity and rights, and to raise productivity. The second is to *reduce the negatives*: through measures that not only reduce risks but also address market power imbalances and policy or institutional biases that work against informal enterprises and workers. This requires recognizing when and how market power imbalances and policy biases favour large formal enterprises over smaller informal enterprises, formal workers over informal workers, and men over women within each of these categories.

Consider, for example, how such a comprehensive framework would apply to the urban informal workforce. In most cities around the world, there is an acute shortage of jobs due to various factors, including increased population but also investment decisions that favor relocation of industries outside cities and/or use of capital-intensive technologies. Government and the private sector need to rethink their investment decisions and place a priority on generating urban jobs. Meanwhile, in most cities around the world, existing employment opportunities in the informal economy are being undermined or destroyed due to urban renewal schemes that demolish the places of work of the urban informal workforce; urban planning that fails to incorporate urban informal livelihoods in city plans; and municipal procurement policies that exclude urban informal operators from bidding for contracts for goods and services.

In this context, most of the urban informal workforce pays taxes, fees, or bribes of various kinds to various local authorities simply to be able to pursue their livelihoods. What they receive in return is negligible—often negative. Most home-based producers do not receive the basic infrastructure that would make their home-cum-workplace more productive; they pay residential (rather than commercial) rates for utilities, and are subject to zoning regulations that restrict commercial activities in residential areas. Most street vendors are treated as criminals subject to evictions, confiscations, and harassments. Few waste pickers are recognized for their contributions to waste management and recycling, many are denied access to waste, and most are not allowed to bid for solid waste management contracts. All three groups would be willing to register and pay appropriate taxes to the city, if they would receive benefits in return—including the right to pursue their livelihoods.

Urban planners and local authorities need to embrace the informal economy—it is the main generator of jobs and livelihoods in most cities in the developing world. They need to include urban informal livelihoods, not just urban informal settlements, in their urban plans and local economic development. This will require urban planners and city officials to develop an approach to urban policies, planning, and practices that includes—rather than excludes—urban informal livelihoods and the urban informal workforce. To begin with, they need to stop doing harm to urban informal livelihoods.

## VI. The Future of Informality

In today's global economy, not enough formal jobs are being created and many existing formal jobs are being informalized. Informal employment is here to stay in the short, medium, and probably long term. It is the main source of employment and income for the majority of the workforce and population in the developing world. On average, compared to formal workers, informal workers have lower earnings and face higher risks, are less likely to enjoy economic opportunities and legal protections, and are less able to exercise economic rights and collective voice (ILO 2002). The informal economy and workforce need to be recognized as the broad base of the global economy and workforce. Both informal enterprises and the informal workforce need to be valued for their contributions and integrated into economic planning and legal frameworks.

There is no single overarching policy intervention to address the concerns associated with the informal economy—a range of interventions need to be considered and implemented. Further, these interventions need to be tailored and targeted to meet the specific constraints, needs and risks of different groups of informal workers: informal self-employed as well as informal wage workers; high end versus low end informal enterprises and workers; those who avoid regulations and those for whom existing laws and regulations are inappropriate or irrelevant.

Another broad policy lesson is that all economic and social policies need to be reviewed in terms of their impact on the informal economy and its constituent parts. It should not be assumed, as it was by the World Bank and others in the mid-1990s, that economic policies cannot reach and do not impact the informal economy (World Bank 1995). Most economic and social policies have an impact—direct or indirect—on the informal economy. The challenge is to monitor the impacts, both positive and negative, of different policies on different categories of the informal workforce and to address the negative impacts.

This requires recognizing and addressing the fact that the employment effects of economic growth work their way through markets, policies, and institutions (social, economic, and political) in different ways for formal and informal enterprises; for formal and informal workers; and for women and men within each of these categories.

Further, to ensure policy responses are appropriate to the constraints and risks faced by informal workers, especially the working poor, they need visibility in official statistics and representative voice in rule-setting and policy-making processes. Current efforts to improve the measurement of informal employment and informal enterprises in official labour force statistics, as well as other economic statistics, need to be strengthened and sustained.

Most importantly, efforts to strengthen organizations of informal workers and to promote the representation of these organizations in rule-setting and policymaking processes need to be increased and sustained.

What is needed, most fundamentally, is a new economic paradigm: a model of a hybrid economy that embraces the traditional and the modern, the small scale and the big scale, the informal and the formal. What is needed is an economic model that allows the smallest units and the least powerful workers to operate alongside the largest units and most powerful economic players. That allows home-based producers in global value chains to be able to bargain with dominant players in those chains for their rightful share of value added. That allows street vendors to operate alongside retailers and wholesalers—alongside shops, wholesale markets, and malls—in central business districts. That allows waste pickers to access waste and to bid for solid waste management contracts alongside large corporations. That allows informal construction workers to gain some of the protections and benefits of formal construction workers. That allows informal transport workers to be integrated on equitable terms in public and private transport systems. That allows small holders and agricultural day labourers to compete on equitable terms with large holders and corporate farms. That allows small-scale producers to compete in export markets on fair terms alongside large-scale commercial farms.

Some years ago, the world embraced *bio* diversity—and still does. Today, the world needs to embrace *economic* diversity. Both are needed for sustainable and inclusive development.

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**About WIEGO:** Women in Informal Employment: Globalizing and Organizing is a global research-policy-action network that seeks to improve the status of the working poor, especially women, in the informal economy. WIEGO builds alliances with, and draws its membership from, three constituencies: membership-based organizations of informal workers, researchers and statisticians working on the informal economy, and professionals from development agencies interested in the informal economy. WIEGO pursues its objectives by helping to build and strengthen networks of informal worker organizations; undertaking policy analysis, statistical research and data analysis on the informal economy; providing policy advice and convening policy dialogues on the informal economy; and documenting and disseminating good practice in support of the informal workforce. For more information visit: [www.wiego.org](http://www.wiego.org).



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