

The Informal Sector

- The informal sector is a sub-sector of the Households sector
- The informal sector consists of units engaged in the production of goods and services
- The aim of the units is to generate income for the people involved

- The Informal Sector Units (ISUs) are characterised by
- On a small scale
- a low level of organisation
- Employment is casual
- “Organisation” through kinship, personal or social relations

- ISUs production units are like household enterprises
- There are no formal internal contracts or agreements
- ISUs have no legal existence
- ISUs cannot own assets, or sign contracts, or exchange as an entity
- ISUs cannot borrow in their own right

- The owners /members of an ISU are personally responsible for
- Borrowing
- Liabilities arising from the conduct of the business
- Production expenses are indistinguishable from Household consumption
- Assets are indistinguishable from household durable goods

- Examples of ISU activities
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- Selling extra home-made cakes to neighbours from a street stall
- Running a taxi-service in own car for locals, “pay what you can”
- child-care for at least a working day – money received or other favours returned

- Most of ISU activity is not criminal
- The activities are carried out to help neighbours / gain some money but not to avoid tax
- Much of ISU activity will be “non-observed” transactions

- What do we mean by “non-observed”?
- Non-observed productive activities are those not captured in the basic data sources of national accounts

Examples of unobserved activities

- Underground to deliberately avoid tax payment, avoid regulations, avoid liability for the results of activity
- Illegal activities – production and distribution of drugs, smuggling, unlicensed practice, stealing
- Production of goods by households for own use
- Most of the productive activities by the ISUs (which may be part of the above)

- Essential criteria for an ISU
- No legal existence
- “owned” by households
- No accounts
- Production is for sale or barter

- Other criteria to be used in practice
- Small number of “employees” (less than 5?)
- No form of registration
- Activity type – non-agriculture (agriculture will be household own account production, recorded as part of the formal household sector)

- Working in or for an ISU
- No contract of employment
- No worker benefits (no holidays!)
- No social protection (no union, no pension)

- What does an ISU look like
- Family micro-business
- Single person own-account casual
- Neighbours working together to market something for local benefit

Measuring the informal economy directly

- Special customised survey
- Add-ons to regular labour force or household surveys
- Conduct of such surveys require experience and professional sociological skills
- They are very expensive to carry out, and may negatively affect regular statistical surveys

Measuring the informal economy indirectly

- Discrepancy method – mismatch between income and expenditure
- Monetary methods – cash in circulation less cash in observed economy gives indication of non-observed economy and so activities of the ISUs
- Physical input methods
- Mismatch between electricity supply and use

Measuring the informal economy - models

- MIMIC – Multiple Indicator – Multiple Cause
- This imputes activities of ISUs from causes such as tax levels, inflation, unemployment, etc
- The modelling approach is not recommended for compiling national accounts (!!)
- *“these methods [are not useful] for any purpose in which accuracy is important, such as the estimation of national accounts indicators”*

Measuring the informal economy

- If the users insist
- Expand the coverage and questionnaire of the Labour Force Survey, and the Household Budget Survey, to gather information on “employment” in ISUs
- Expand business surveys to capture household informal activities
- Conduct special surveys (probably cluster sampling)

- Concluding remarks (my view)
- If governments are serious about measuring the activities of Informal Sector Units
- They should conduct custom-built specialised cluster surveys carried out by skilled professional sociological interviewers
- Results can be raised to whole economy level by stratified upgrading according to location and dwelling characteristics